

St. Petersburg University  
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Master in International Business Program

**Crowdfunding and entrepreneurship:**  
Threats and success factors in reward-based crowdfunding  
*(The case of USA and Russian companies)*

Master's Thesis by the 2<sup>nd</sup> year student

Concentration — MIB

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## ЗАЯВЛЕНИЕ О САМОСТОЯТЕЛЬНОМ ХАРАКТЕРЕ ВЫПОЛНЕНИЯ ВЫПУСКНОЙ КВАЛИФИКАЦИОННОЙ РАБОТЫ

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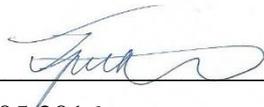
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<b>Ключевые слова</b>	Краудфандинг, Предпринимательство, Стартап, Маркетинг, Коммуникации

## ABSTRACT

<b>Master student's name</b>	Grigorii Romanovskii
<b>Master thesis title</b>	Crowdfunding and entrepreneurship: threats and success factors in reward-based crowdfunding (The case of USA and Russian companies)
<b>Faculty</b>	Graduate School of Management
<b>Main field of study</b>	Management
<b>Year</b>	2016
<b>Academic advisor's name</b>	Juan Solervicens Freixanet
<b>Description of the goal, tasks and main results</b>	<p><u>The main goal:</u> To identify how can entrepreneurs exploit the full potential of crowdfunding for their business.</p> <p><u>Main tasks:</u></p> <ul style="list-style-type: none"> <li>- To review the existing theoretical knowledge on crowdfunding, its origins, main types and participants;</li> <li>- To create a theoretical framework for assessment of crowdfunding through a prism of entrepreneurship, startup and marketing theories;</li> <li>- To identify benefits and drawbacks of crowdfunding;</li> <li>- To identify characteristics of project creators on CFPs;</li> <li>- To understand what goes into pre-planning and execution of a crowdfunding campaign;</li> <li>- To identify what are other applications of crowdfunding besides fundraising;</li> </ul> <p><u>Main results:</u></p> <ul style="list-style-type: none"> <li>- The description of entrepreneurial characteristics of crowdfudners;</li> <li>- Evaluation of the Pre-planning and Execution phases of crowdfunding campaign;</li> <li>- Startup perspective of crowdfunding;</li> </ul>
<b>Keywords</b>	Crowdfunding, Entrepreneurship, Startup, Marketing, Communications

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## INTRODUCTION

### 1.1 Context and relevance of the study

The events of 2008 global economic and financial crisis have significantly influenced the way investors look at venture and high-risk projects. Willing to minimize risks, many banks decided to distance themselves from venture projects, making many SMEs and start-ups short on funding. Because of that more and more entrepreneurs started to shift their attention towards alternative ways of obtaining finance for their projects (Golic, 2013). One of such methods became to be known as crowdfunding: an internet-based technology that allows unlimited amount of people to donate small portions of money in exchange for certain rewards – either material or emotional. During the last decade, this approach has gained significant following from entrepreneurs all over the world. Crowdfunding attracts creative people not only as a capital raising tool, which allows individuals and SMEs to get financing in the context of limited options, but also as a way to test and validate marketability of their ideas. Individuals, on the other hand, receive a unique opportunity to have an impact on the producers by supporting and contributing to the ideas they believe in. Amongst other benefits of crowdfunding is also its positive effect on the global and local economies – job creation, innovation foster, etc.

The basic idea of crowdfunding is not that novel. There are lots of historical evidences of people uniting to finance certain project or cause. The most common example would be a construction of Statue of Liberty pedestal, when the needed sum of money has been received through an open call in the newspapers, encouraging every US citizen to donate. The more recent example would be Barack Obama’s election campaign in 2008 where his team managed to raise almost \$57 mil. via single donations of less than \$200.

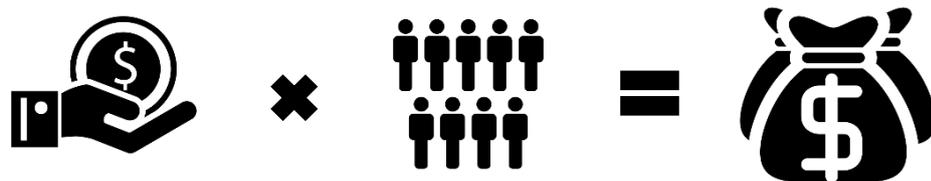


Figure 1. Basic concept of crowdfunding. Source: own creation.

However, it is only the development of communication technologies, such as Internet, that allowed for this simple idea to grow into the phenomenon of crowdfunding. It needs to be mentioned that term “crowdfunding” is a derivative from a broader term “crowdsourcing”, which was introduced by American journalists Jeff Howe and Michael Robinson in their article “The Rise of Crowdsourcing”<sup>1</sup> in June 2006. While the idea of crowdsourcing was about using digital

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<sup>1</sup> <http://archive.wired.com/wired/archive/14.06/crowds.html> - J.Howe, M.Robinson “The Rise of Crowdsourcing”, Wired Magazine, June 2006

technologies to unite and share people's talents and skills, crowdfunding stated the same principles to be applied to the world of finance. At that time the idea didn't clicked with the business world, but after the described events of 2008 global financial crisis, when the banking sector's willingness to lend and invest into venture projects has significantly decreased, this new option started to gain following.

Therefore, the financing needs of innovative ideas, start-ups and already existing SMEs, as well as the development of digital technology and financial innovations has brought to life an alternative form of financing, one that uses internet platforms to moderate between project ideas and crowds of backers willing to invest funds. Compared to traditional types of financing – like banks, venture capitalists or business angels – crowdfunding offers entrepreneurs a much more flexible and complex set of tools that can be adjusted to needs of both the entrepreneur and his potential investors.

However, running a crowdfunding campaign is a project of its own. In order to successfully reach stated goal, crowdfunders need to plan every step, carefully avoiding threats and getting advantage of various opportunities. While in financial return crowdfunding actors mostly operate with standard financial pragmatic motives, volunteer crowdfunding operates on some totally different principles. In this thesis an attempt to understand how can entrepreneurs successfully utilize crowdfunding for their business will take place. Reward-based model of crowdfunding will be studied.

## **1.2 Problem formulation**

Crowdfunding is becoming one of the fastest growing trends on the Internet that is transforming the socio-economic environment of today's society. It allows creative and innovative individuals to target a crowd on the Internet in order to develop products and create business start-ups by acquiring donations or investments from widely dispersed individuals on the Internet (Belleflamme et al., 2010). Over the last 5 years, the global crowdfunding market has grown from \$1,5 billion dollars in 2011 up to \$34,4 billion in 2015<sup>2</sup>. Such growth rates can lead to thinking that organizations and individuals around the world are slowly turning away from traditional organizational structures and professional investors. This signifies that crowdfunding is tapping in to become a major alternative to traditional business models, where individuals have, for the first time, the power to shape their success solely by themselves (Beer & Badura, 2012).

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<sup>2</sup> <http://www.crowdsourcing.org/editorial/global-crowdfunding-market-to-reach-344b-in-2015-predicts-massolutions-2015cf-industry-report/45376> - 2015CF Crowdfunding Industry Report

What is more, individuals are discovering crowdfunding as an easy solution for generating funding for their creative endeavors. One of the most popular crowdfunding platforms (CFPs) for creative projects – Kickstarter – has attracted almost \$2,5 billion dollars in investments and helped to successfully fund more than a 100,000 projects<sup>3</sup>. Kickstarter is one of the many reward-based crowdfunding platforms that attracts both professional and inexperienced creators worldwide. However, looking at the top ten most funded projects of Kickstverarter, all of those projects are created by companies or individuals with professional experience, background in the creative category of that certain project and previous experience in the industry (Appendix 1). The most interesting case would be Pebble Industry company, which has managed to successfully crowdfund 3 of its products by significantly surpassing its funding goal. This signifies, that experienced creators have higher chances for receiving successful funding and even exceeding the funding goal tremendously. Projects by inexperienced creators do not appear among the most successful projects of Kickstarter to date. This situation is not unique to Kickstarter and can be found on other CFPs.

The problem, therefore, is as follows: individuals with professional experience have accumulated knowledge and understanding on how to position their creative project in order to attract attention of target audiences and therefore receive the needed funding. Individuals without professional experience or background lack this significant advantage. The steps they take in order to crowdfund their projects are led entirely by their personal conceptions. As crowdfunding phenomenon has not been extensively researched yet, there is an evident lack of professional guidance for individuals of how to successfully utilize this instrument for their projects.

Running creative projects on reward-based crowdfunding platforms is a challenge for inexperienced individuals and entrepreneurs. Therefore, an established framework, constructed with qualitative research findings, observations and examples, is needed. To determine if and how creative individuals can benefit from using a model of reward-based crowdfunding, qualitative research on the most popular reward-based platform – Kickstarter – will be conducted.

### **1.3 Problem justification**

Crowdfunding has not been studied and researched to a large extent as this phenomenon emerged only recently. Economists and social science researchers have not yet created a stable and reliable framework for understanding the implications of crowdfunding, and how it should be perceived and applied for attaining successful results. Moreover, the concept of crowdfunding is still evolving and continues to identify new forms and activities within its practice. Research that

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<sup>3</sup> <https://www.kickstarter.com/help/stats> - Kickstarter statistics

is currently available and has been conducted addresses mainly the economic intricacies of crowdfunding. Recently, crowdfunding has been greatly used for funding projects by organizations and individuals. This signifies a growing demand for both creative project utilization and the potentials that crowdfunding can provide.

The original idea for this thesis came to me back in 2014. In that year, the massive media attention was emphasizing a new era for creative people being shaped by the rise of online crowdfunding. Individuals who have utilized their creative projects by entirely relying on a wide audience of people were spotlighted. Consequently, it made me wonder how, especially in these difficult economic times, individuals manage to achieve their goals by relying on geographically dispersed and unacquainted individuals, and their support. Moreover, I began to think about possibilities that crowdfunding could bring to creative individuals and whether it is an effective alternative for raising funds for entrepreneurial projects.

Therefore, the main purpose of this study is to improve the overall understanding of crowdfunding as a socio-economic phenomenon, explain how crowdfunding functions, what are the drivers of success as well as its other possible applications for business. The analysis will be based on qualitative research and investigation of a crowdfunding platforms and projects presented on them.

#### **1.4 Goals and objectives**

Based on what has been stated above, the main goal for this thesis has been formulated as:

*To identify how can entrepreneurs successfully utilize crowdfunding for their business*

In correlation with the stated goal, the following research questions have been formulated:

1. What are the benefits and drawbacks of crowdfunding?
2. What individual characteristics are required for successful crowdfunding?
3. What are the specifics of pre-planning and execution of crowdfunding campaign?
4. What are other applications of crowdfunding beyond fundraising?

## LITERATURE REVIEW

### 2.1 Capital raising for entrepreneurial ventures

During the last decades, entrepreneurship has begun to be recognized as one of the main drivers of economic growth. It increases employment opportunities, enhances technical innovation level, and promotes economic growth. From a dynamic perspective, entrepreneurs are agents of change since entrepreneurship implies starting new businesses, experimenting with new technology, organization of production, introduction of new products or even creating new markets. Schumpeter (1934) saw entrepreneurial activity as a tool that encourages innovation and technological development, that way stimulating economic growth. Kizner (1997) described entrepreneurial process as an “*action through which supply and demand are equilibrated*”.

However, at the moment, scientific research of entrepreneurship is still a matter of high academic interest. Analysis of Google Scholar database shows positive trend in topic discussion for the last 30 years (Figure 2). It is not surprising, considering the fact that entrepreneurship brings economic and social benefits and drives development of the economy. However, not until late 1980s the research focus of entrepreneurship has shifted away from simple analysis of entrepreneurial behavior to understanding the reasons for going venture and start-up (Bolton & Thompson, 2000).

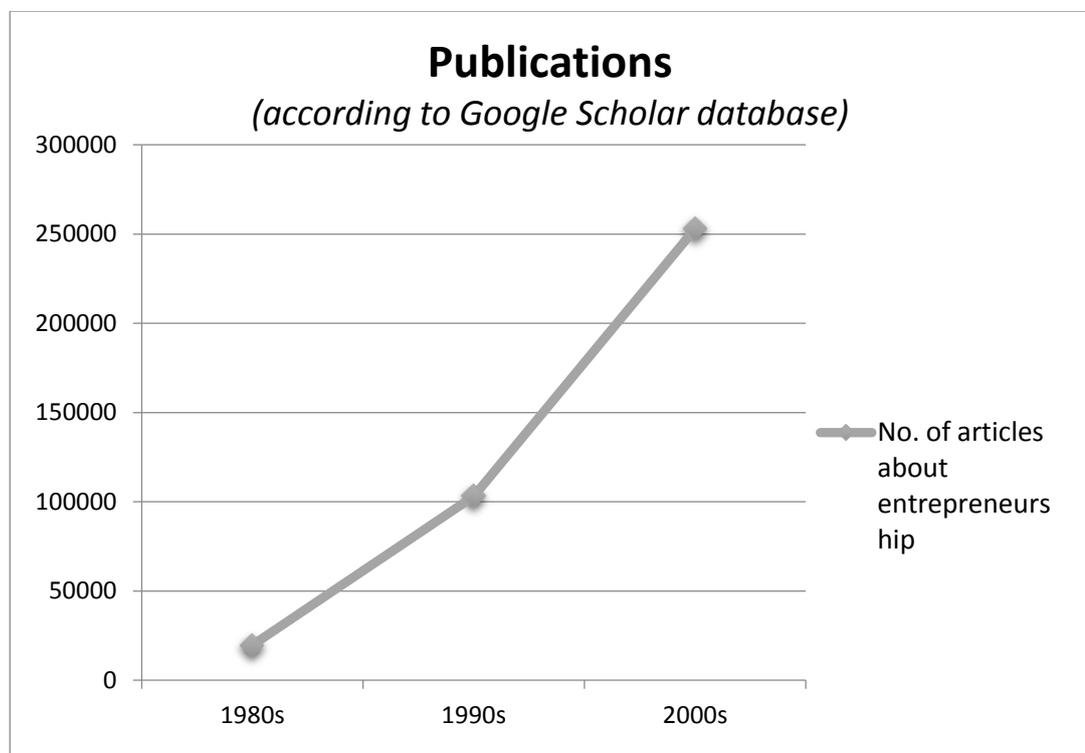


Figure 2. Publications with the key word “entrepreneurship”. Source: Google Scholar database.

Entrepreneurship is considered to be one of the main drivers of innovation and change. It serves as a channel, through which new knowledge transforms into real products and services.

This idea derives from the definition of entrepreneurship as a process by which “*opportunities to create future goods and services are discovered, evaluated, and exploited... New goods, services, raw materials, and organizing methods can be introduced and sold at greater value than the cost of their production*” (Shane & Venkataraman, 2000).

As Shane & Venkataraman explain, entrepreneurship is not always about starting a new business. It’s a complex process of existing resources being recombined in a new innovative way, making entrepreneurship a creative process. The goal of this process can be entrepreneurs willing to develop previously identified market opportunity (Shane, Locke & Collins, 2003). As a result, the proposed idea can be formulated, manufactured, and provided to customers in a form of product or service.

Nevertheless, according to many studies the most serious problem for small businesses has always been accessible capital. Further, Denis (2004) claims that “*one of the most important issues facing entrepreneurial firms is their ability to access capital*”. This problem of capital accessibility lies in the basis of entrepreneurial finance research.

Yazdipour defines entrepreneurial finance as the finance offered to ventures during the phase when they are between opportunity recognition and IPO. According to him corporate finance is for large ventures that have the capability to get listed in the stock exchange. Sapienza, Korsgaard & Forbes (2003) use the principles of agency theory to differentiate entrepreneurial finance from corporate finance where the roles of principal and agent assigned to investors and managers, respectively. Entrepreneurs play the role of both the agent and principal, as in most cases they hold ownership rights in the venture. In a corporate venture, the managers take finance decisions on behalf of the owners or board of directors However, in entrepreneurial finance, the entrepreneur assumes agency risk of both agent and principal, therefore “*positioning himself high both in management skills as well risk and uncertainty of finance*” (Sapienza, Korsgaard, Forbes, 2003).

Generally, chose of the financing method is correlated to a firm’s stage of life cycle. Small enterprises are usually capitalized through selling of venture equity. However, this process tends to be rather chaotic and unpredictable, due to the fact that neither entrepreneurs, nor investors know how to assess the firm real value and potential. And as it was mentioned in the previous paragraph, traditional financial theories do not have a specific answer to these questions.

Start-up life cycle is generally divided into different stages or financing rounds, which somewhat correspond to the firm’s level of development (Figure 3).

## Startup Financing Cycle

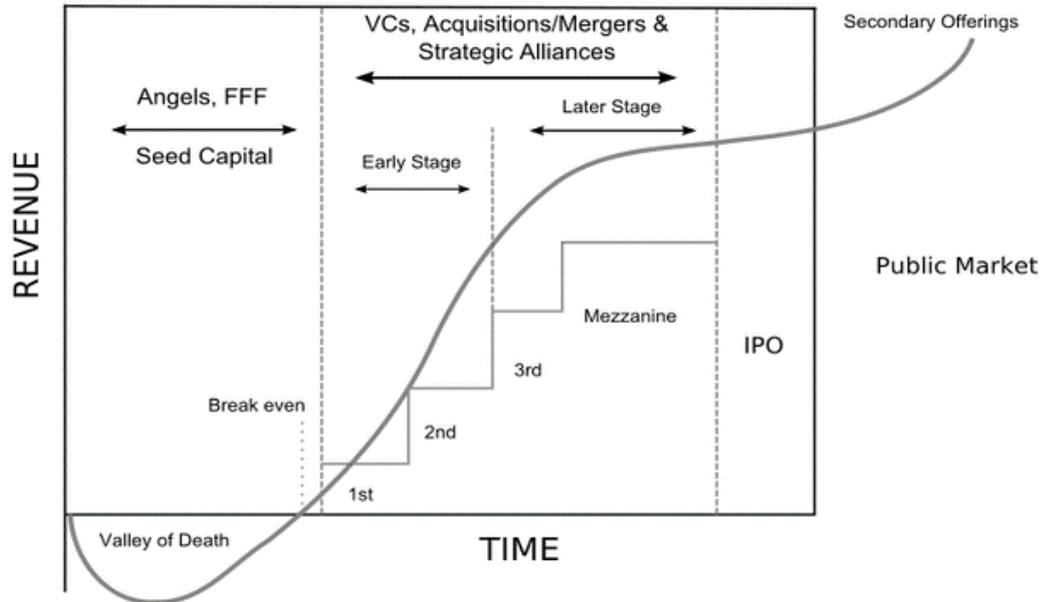


Figure 3. Startup financing cycle. Source: Wechsler (2013).

The first stage is called the *seeding stage* – it’s a period of company’s life when creators try to find a suitable place on a market to enter. At this point, various concepts and ideas are tested and validated, and funding is provided by entrepreneurs own savings or friends and family funds. When all the planning is done and firm starts its slow process of development the amount of capital needed is increasingly grows. At this moment, firm’s future perspectives attract business angels, wealthy individuals who are interested in investing into ideas which correlate with their values and agenda. With the spent of time, firm’s expenditures continues to grow. This is when firm starts to enter the *early stage* – it’s still not big enough to obtain funding via public capital markets, but already getting the attention of certain venture capitalists. This process accelerates when the firm hits the break-even point and achieves its market share, therefore becoming an object of high value for VC agencies. The next step begins when company’s sales rapidly increasing but production capacity lags. This means that the company is becoming more mature and enters the *later stage*. Expansion continues, with more and more investors being attracted by that process. The lifecycle concludes when the owners decide that the company is ready to go public and conduct an IPO. (Lehner, 2013).

However, the presented scheme is not the only possible depiction of start-ups lifecycle. Ross, Westerfield & Jaffe (2013) formulated an alternative classification of financing stages:

- **Seed money stage** – relatively short amount of financing needed. Goal: to validate ideas, construct prototypes;

- **Start-up** – funding provided to start production process and finish the R&D;
- **First-round financing** – funding provided to start sales and expand production unit;
- **Second-round financing** – financing need in order to start the product diversification process;
- **Third-round financing** – further diversification and expansion of production;
- **Fourth-round financing** – final capitalization of a company prior to its IPO;

Nevertheless, no matter what type of categorization to choose, one thing will remain common. At the beginning the entrepreneurs have an idea, relatively small amount of funds, and quite a limited access to external capital. This phenomenon is known as “*funding gap*” of start-ups, and it is considered to be one of the main barriers for entrepreneurship development. As it was mentioned earlier, after the 2008 financial crisis this problem has become even clearer, with VC and banks being even more skeptical about investing in high-risk projects. This situation forced entrepreneurs to look for alternative solutions to obtain capital and influenced rapid development of alternative finance market.

## 2.2 Crowdfunding concept

### 2.2.1 Definition and context of crowdfunding

Crowdfunding (or crowd funding, crowd-funding) is defined as “*an open call, mostly through the Internet, for the provision of financial resources either in the form of donation or in exchange for some form of reward and/or voting rights in order to support initiatives for specific purposes*” (Lambert & Schwienbacher, 2010, p. 6). Crowdfunding is made possible through the advancement of Internet technology and features, otherwise referred to as Web 2.0 (Belleflamme et al., 2010; Kleemann et al., 2008), and also the advent of widely used social networks such as Facebook, Twitter, Instagram or, in case of Russia, VK, etc. The main objective of crowdfunding is to collect money needed for investment from a large audience of individuals, otherwise called ‘the crowd’ (Lambert and Schwienbacher, 2010). It differs from traditional business model for it allows individuals to generating investment for creative and innovative ideas not from professional and specialized investors, but by small donations from individuals within the crowd.

Due to the fact that crowdfunding is a relatively new concept, the amount of literature on the topic is rather short. However, according to the Google Scholar database, number of publications, with key word “crowdfunding” in them, is exponentially increasing each year, which can be explained by a booming growth of a crowdfunding market itself.

## Publications (according to Google Scholar database)

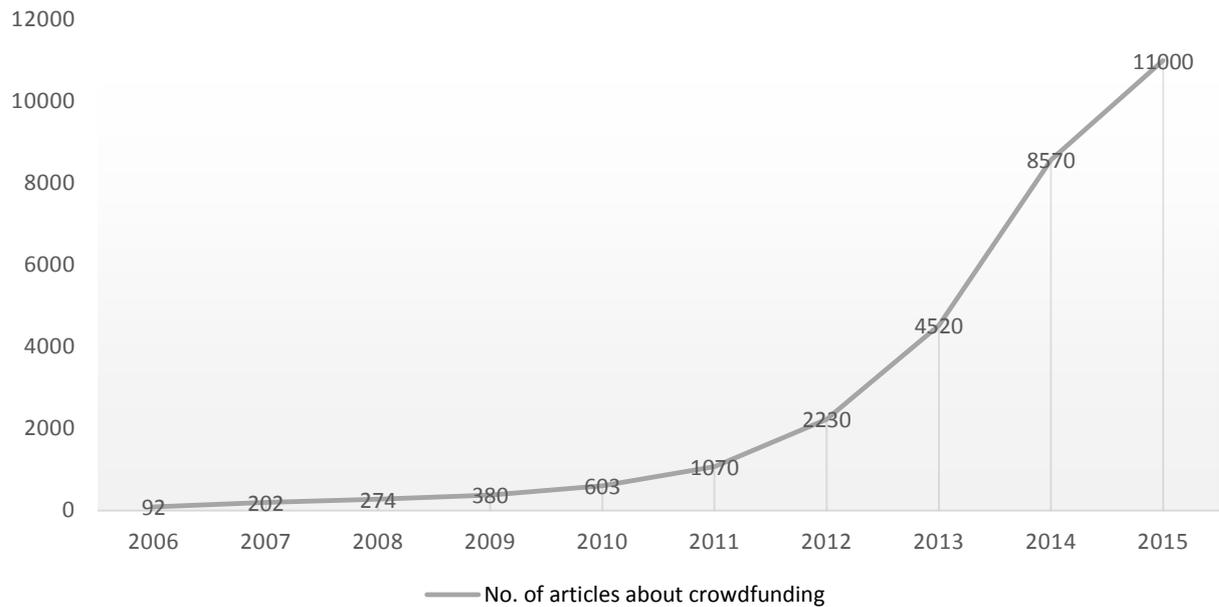


Figure 4. Publications containing the term “crowdfunding”. Source: Google Scholar statistics

### 2.2.2 Types of crowdfunding

There are four types of crowdfunding models that can be divided into two blocks (Crowdsourcing.org, 2016):

WITH FINANCIAL RETURN	WITHOUT FINANCIAL RETURN
Equity-based crowdfunding	Donation-based crowdfunding
Lending-based crowdfunding	Reward-based crowdfunding

Table 1. Types of crowdfunding. Source: own creation

Equity and lending-based crowdfunding focus on financial returns. Platforms that specialize in these crowdfunding types enable project owners to ask for donations from the crowd, for which they grant equity in exchange (Crowdsourcing.org, 2016). These projects are usually focused on entrepreneurial motives and business start-ups as final result. Donation and reward-based crowdfunding is based more on philanthropic motives. In donation-based model individuals are purely donating and receiving nothing in exchange, whereas in reward-based model individuals receive a non-monetary tangible reward (Crowdsourcing.org, 2016). Donation-based crowdfunding has been mainly exploited for charitable causes. Reward-based crowdfunding is mostly used for creative projects like film, music, design etc. and innovative technological projects. These crowdfunding models signify different scope of activities and project types.

As already discussed in the introduction, this thesis is focused on *reward-based crowdfunding model*. Belleflamme et al. (2010), who were among the first researchers to investigate the economic model of crowdfunding, identified crowdfunding initiatives to be greatly based on rewards. Today, reward-based crowdfunding accounts to the largest number of all crowdfunding platforms (Crowdsourcing.org, 2016). In 2014 individuals worldwide collected more than \$7,2 billion on reward-based crowdfunding platforms (Crowdsourcing, 2014).

Reward-based crowdfunding is based on providing rewards in exchange to monetary donations. Individuals from the crowd, who donate money for a project, receive tangible, non-monetary rewards as a compensation for their money. For example, t-shirts, CDs, books and stickers are among the most popular rewards. Pre-orders of the final product copy are also popular among reward-based crowdfunding platforms.

Initial research suggests that reward-based crowdfunding is based more on ideas or contents of projects (Beer & Badura, 2012), rather than monetary inputs as individuals do not receive shares in projects. This model is, therefore, the core focus of qualitative research of this thesis. The figure below presents the main components of reward-based crowdfunding:

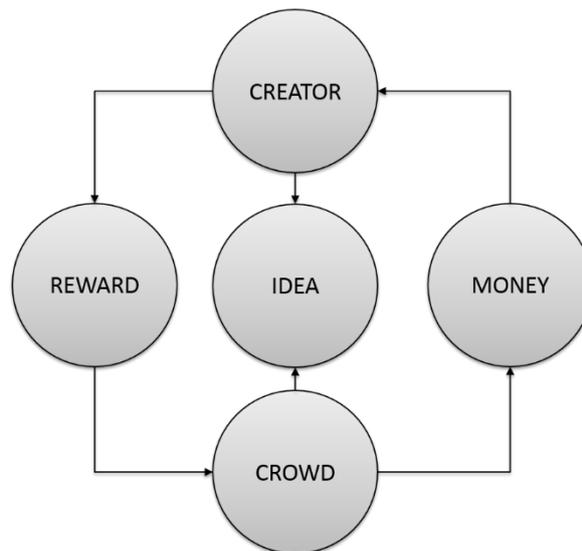


Figure 5. Concept of reward-based crowdfunding on CFPs. Source: own creation

## 2.3 Crowdfunding platforms

As it has been mentioned in the introduction, the growth dynamics of crowdfunding market is quite positive. According to Crowdsourcing.org (2016), which is the biggest online community for crowdsourcing and crowdfunding news; as of April 2016 there are more than 2000 crowdfunding platforms worldwide. Platforms are active and are based on equity, lending, reward or donation-based models of crowdfunding. Even though the mass usage of crowdfunding initiatives began only recently, several platforms have been operating long before the term ‘crowdfunding’ has even been defined. Therefore, the following platforms that influenced the development of crowdfunding are presented:

- **Kickstarter** – founded in 2009 is a reward-based crowdfunding platform based in New-York, USA. It operates on an “all-or-nothing” business model, where project creators do not receive money unless the project reaches its funding goal on time (Kickstarter, 2012). Kickstarter specializes in creative projects related to music, film, design, food, video games and other. The platform charges five percent for successfully funded projects, along with additional charges from Amazon Payments (Kickstarter, 2016). Kickstarter is regarded as the most popular reward-based crowdfunding platform today (Crowdsourcing.org, 2016)
- **IndieGoGo** – based in San Francisco, California, is a reward-based crowdfunding platform launched in 2008 that enables funding for any type of campaign, be it film, charity or business (IndieGoGo, 2016). It is based on two types of funding models: individuals can choose, if the project is not successful, to either keep the generated funds and pay nine percent fee, or withdraw from taking the money (money is transferred back to people who funded the project) without any additional fees (IndieGoGo, 2016).
- **RocketHub** – is a reward-based crowdfunding platform for creative projects launched in 2010. It is based on an “all & more” funding business model that enables project owners to collect the pledged money even if a project does not reach its complete funding goal on time; when the project does reach its goal, project owners receive an additional bonus (RocketHub, 2016). RocketHub charges a four percent fee along with additional three to five percent charged by credit card companies for transactions (RocketHub, 2016).
- **Kiva** – founded in 2005 and based in San Francisco, California, is a non-profit organization with a mission to “connect people through lending to alleviate poverty.” (Kiwa, 2016) This crowdfunding platform is based on philanthropic intentions (Agrawal et al., 2011) and is categorized as a donation-based crowdfunding platform. According to Kiva website, the platform has already collected more than \$308 million in loans (Kiva, 2016).

- **Sellaband** – is a crowdfunding platform launched in 2006 for undiscovered musicians, who seek to get funded by fans. Based in Munich, Germany, it is a popular platform for musical artists all over the world, with over \$4,000,000 already invested to independent musicians (Sellaband, 2016). According to Sellaband’s funding model, artists have 100% freedom of rights to create the music they like and pertain all the copyrights. Individuals and fans that invest into a music project on Sellaband, have the ability to withdraw their money anytime before the project’s funding goal is reached (Sellaband, 2016). Sellaband is often referred to as the granddaddy of crowdfunding” (Agrawal et al., 2011).
- **ArtistShare** – launched in October 2003 in USA, is among the first crowdfunding platforms for artists online. It is based on a “fan funding” model, where fans can fund musical artists and their creations, and in exchange receive some form of access to the creative process (ArtistShare, 2016). According to ArtistShare, the platform’s projects have received five Grammy awards and 15 Grammy nominations (ArtistShare, 2016).
- **Sponsume** – launched in 2010 is a reward-based crowdfunding platform for creative individuals and organizations based in London, UK and operating worldwide. It operates on a similar funding model to RocketHub, where project creators are allowed to keep the accumulated pledges even if the target goal is not reached on time. The platform charges a four percent fee for successful projects and a nine percent fee to projects that do not reach the funding on time (Sponsume, 2016). Sponsume offers funding in four different currencies (US dollars, Euros, UK pounds and Australian dollars) (Sponsume, 2016). This differentiates it from other international platforms that are operating activities only in US dollars.

All of these platforms operate internationally and attract individuals from all over the world. This fact substantiates the entire concept of crowdfunding practice – borders do not limit crowdfunding activities. In fact, Agrawal et al. (2011) acknowledge that distance-related frictions are overcome by crowdfunding platforms, and highlight three properties that crowdfunding platforms have in common:

- They provide a standardized format for entrepreneurs to present their project in a comprehensive manner to anyone with internet access
- They allow for small financial transactions (e.g., USD\$10) to enable broad participation with limited downside risk
- They provide investment information (i.e., cumulative amount raised to date and the online identity of current investors) as well as tools for investors to communicate with each other;

## THEORETICAL FRAMEWORK

In the previous chapter, a detailed overview of crowdfunding phenomena and current state of the crowdfunding market has been given. Analysis of existing literature has highlighted the growing popularity of this new instrument. However, in order to have a deeper understanding of the dynamics of crowdfunding, the concept should be analyzed through prism of related theoretical concepts.

### 2.1. Crowdfunding theories

Amongst the existing academic literature on crowdfunding, three papers have been identified as highly important for this particular thesis. The first one by Belleflamme et al. (2014) concentrates on various types of benefits of crowdfunding for entrepreneurs: financial and non-financial, with mention of non-financial benefits being more important than financial ones. In addition, Belleflamme et al. (2014) states that social side of crowdfunding – community building – is the crucial part of crowdfunding process. Just as with the entrepreneurs, crowdfunding investors are also driven by factors that go beyond acquiring materialistic benefits. Backers are interested in becoming a running partners alongside the project creators, being an active co-creator and privileged user. These non-financial benefits concept seems especially important, as it is the one that distinctively separates crowdfunding from traditional sources of financing as banks or venture capitalists. Furthermore, Belleflamme et al. highlights a much more complex nature of crowdfunding as a business tool: due to its nature it can be utilized both as a marketing and testing tool. Entrepreneurs can apply crowdfunding for product validation, promotion, marketing, co-creation and as a customer engagement channel. Therefore, Belleflamme et al. state the importance of further analysis of crowdfunding as learning tool through which different types of useful information can be utilized in business.

This idea is further supported in the second paper by Mollick (2014) who identifies that backers are in fact expect to receive some unique material benefits in exchange for their patronage, but also driven by motivations of co-creation and active participation. Furthermore, Mollick (2014) highlights other sides of crowdfunding besides its prime goal of providing financing. By analyzing statistical data of successfully funded crowdfunding campaigns, Mollick (2014) concludes that crowdfunding serves as a transition channel, which helps creative individuals transform into entrepreneurs. In conclusion, Mollick (2014) provides some valuable insights into factors that affect the outcome of the crowdfunding campaign. The listed factors include:

- **Ability to signal preparedness** – to create a basis for potential investors by assuring the quality of the product. This can be achieved by utilization of existing social networks and connections to one's loyal community.

- **Formulation of justified strategy** – to successfully deliver promised goods in the given time period. This can be achieved using careful time and resource management in coordination with setting of realistic goals.
- **Development of campaign execution plan** – to successfully reach the stated funding goal. This can be achieved by in-depth through planning of campaign execution process and all of its components.

Mollick points out the need for research on these topics in order to understand how exactly do entrepreneurs can signal quality, trustworthiness and ability to fulfill in the context of crowdfunding campaign.

Author	Mollick (2014)	Belleflamme et al. (2014)	Kuppuswamy and Bayus (2014)
Concepts	Micro-finance and crowdsourcing (interdisciplinary)	Reward and equity based crowdfunding	Dynamics of backers' support
	Entrepreneurial context - funding of ventures	Entrepreneurial finance perspective	Social information and goal gradient
	Innovators transit into entrepreneur	Monetary and nonmonetary benefits for creators	Potential backers influenced by % of funding goal reached rather than total number of backers
	Demonstrates demand for a product	Backers enjoy community benefits	Further backer support is related to project updates
	Backers as patrons and early consumers	Crowdfunding as a promotion tool	
	Creators need to signal preparedness	Entrepreneurial learning from the crowd	
	Planning of goals and the campaign process is crucial for the success		

*Table 2. Overview of theoretical concepts on crowdfunding. Source: various authors.*

The last paper by Kuppuswamy and Bayus (2014) mostly concentrates on the different aspect of crowdfunding – attraction of supporters in the process of crowdfunding campaign. By analyzing the historical data from Kickstarer, the authors conclude that many backers tend to make a decision to support the project using the so-called social information. In other words, the backers' willingness to support the project increases in correlation with the current percentage of funding that campaign has already attracted i.e. the more money has been pledged the more attractive the

project becomes for new participants. Kuppuswamy and Bayus also state that this financial information is more influential than the total number of investors. Another important evidence from Kuppuswamy and Bayus work is that campaign success is directly tied with the way campaign process goes: how much of the communication goes between creators and backers either in a form of direct communication or by posting updates. The time period of the update publication is also positively related to the success rate. Usually funding peaks are located within first and last three days. During these periods the project creators are tend to be more persuasive with promotion and marketing.

### 3.1 Entrepreneurship theories

#### 3.1.2 Classification of entrepreneurs

Classification of entrepreneurs into different types provides a starting point for gaining an insight into how different types of entrepreneurial ventures work and what are the underlying factors of their success. There exist a large variety of approaches to classification of entrepreneurs, which can be divided into two main types: either by personality or by venture (Wickham, 2006). However, as the goal of this chapter is to provide basis for analysis of a crowdfunder as a person, only personal-based classification will be studied.

Considering the nature of crowdfunding and its possible role in the system of entrepreneurial finance, the following classification matrix (Figure 2) by R. Landau has been chosen.

Landau (1982) has identified the key criteria as level of innovativeness and readiness for risk bearing. Both of these criteria also play a significant role in entrepreneur's decision to choose the crowdfunding way. The four types of entrepreneur identified by Landau include:

- **Gambler** – an entrepreneur characterized by a low degree of innovation and a high level of risk bearing. The gamble here arises from the fact that entrepreneur risks by attempting to operate in the market without the needed level of innovativeness, therefore having limited chances to deliver value in the context of competition from existing players.
- **Consolidator** – an entrepreneur who understands his limited level of innovation and is not willing to take risks. The expected results here include only marginal improvements over current value provided by competitors.

R i s k	H i g h	<b>G A M E</b>	<b>E N T R E P R E N E U R</b>
	L o w	<b>C O N S E R V A T I V E</b>	<b>D R E A M E R</b>
		L	H
		I n n o v a t i o n	

Table 3. Landau's classification of entrepreneurs. Source: Landau (1982).

- **Entrepreneur** – a “true” entrepreneur who understands the risks associated with new venture creation and is ready to accept and mitigate those using skills and resources.
- **Dreamer** – an entrepreneur who attempts to combine high level of innovativeness with low risk. Ideally, all entrepreneurs would like to operate in this category. However, the amount of risk associated with innovation and new product development makes it almost unachievable. Nevertheless, one of the propositions of this thesis is to show that crowdfunding can be one of the instruments that allow entrepreneurs to become one step closer to this category.

### 3.1.3 Entrepreneurial characteristics

Even though there is no way to identify all possible characteristics of entrepreneur, there exist certain degree of consistency in the way entrepreneurs approach tasks. The following list includes some of the most common attributes of a successful entrepreneur (Wickham, 2006):

- **Hard-working** – an entrepreneur understands that development of a venture takes a lot of physical and mental effort.
- **Self-starting** – entrepreneur needs no directions to when, how and why he needs to operate. He identifies the tasks for himself and follows them through without any endorsement from others.
- **Setting of personal goals** – entrepreneurs tend to set themselves clear and demanding goals. They benchmark their achievements against these personal goals. As a result, entrepreneurs

tend to follow internal standards, rather than looking to others for assessment of their performance.

- **Resilience** – entrepreneur understands that failure is a common part of an entrepreneurial process. He must not only know how to continue operating after things go wrong, but also how to gain advantage from this experience by learning and using this knowledge for further improvement.
- **Confidence** – entrepreneurs must demonstrate that they believe in themselves and especially in the venture they are creating. In the end, if they do not believe in it, why should potential customers? However, there always exist a problem of overconfidence, where entrepreneurs do not will to see their own flaws.
- **Receptiveness to new ideas** – in order to solve the problem of overconfidence, entrepreneurs need to be able to recognize their own limitations and possibilities of how they can overcome those. They must be willing to revise their ideas in the light of new experience.
- **Assertiveness** – entrepreneurs need to have a clear understanding of what they want to gain and express their intentions. Being assertive does not mean being aggressive or stubborn. It means to have a commitment to *outcome*, but not the *means*. True assertiveness relies on mutual understanding and is founded on good communication skills.
- **Information seeking** – an entrepreneur is usually characterized by inquisitiveness and is always looking for new relevant information. Successful entrepreneurs tend to ask questions rather than making statements.
- **Eager to learn** – successful entrepreneurs are always aware that they could potentially operate better. They are always aware of both the skills they have and their limitations, and are always receptive to a chance to improve their skills and to develop new ones.
- **Attuned to opportunity** – successful entrepreneurs are constantly looking for new opportunities. They are never completely satisfied with the way things are now and use this sense of dissatisfaction to make sure they never become complacent.
- **Receptive to change** – entrepreneurs are always eager to accept change in a positive fashion, actively embracing the possibilities presented by change, rather than resisting them.
- **Commitment to others** – successful entrepreneurs are not self-centered. They recognize the value that other people bring to their ventures and the importance of motivating those people to make active contributions. In order to do this, entrepreneurs need to show commitment to them, which involves large investments in understanding how this support can be turned into a real value.

### 3.1.4 Entrepreneurial skills

A skill can be simply defined as a knowledge which is demonstrated by action (Wickham, 2006). In entrepreneurship, the precise set of needed skills depends on a whole variety of factors like: selected industry, market in which company operates, etc. Generally, all those skills can be divided into four main categories (Wickham, 2006):

- **General management skills**

- *Strategy skills* – an ability to consider the business as a whole, to understand how it fits within its marketplace, how it can organize itself to deliver value to its customers, and the ways in which it does this better than its competitors.
- *Planning skills* – an ability to consider what the future might offer, how it will impact on the business and what needs to be done to prepare for it now;
- *Marketing skills* – an ability to see the past the firm’s offerings and their features, to be able to see how they satisfy the customer’s needs and why the customer finds them attractive;
- *Financial skills* – an ability to manage money, to be able not only to keep track of expenditures and to monitor cash flows, but also to assess investments in terms of their potential and their risks;
- *Project management skills* – an ability to organize projects, to set specific objectives, to set schedules and to ensure that the necessary resources are in the right place at the right time;
- *Time management skills* – an ability to use time productively, to be able to prioritize important jobs and to get things done to schedule;

- **Human relationship skills**

- *Leadership skills* – an ability to inspire people to work in a specific way and to undertake the tasks that are necessary for the success of the venture. Leadership is about more than merely directing people, it is also about supporting them and helping them to achieve the goals they have set;
- *Motivation skills* – an ability to enthuse people and get them to give their full commitment to the task. Being able to motivate demands an understanding of what drives people and what they expect from their jobs. It should not be forgotten that, for the entrepreneur, an ability to motivate oneself is as important as an ability to motivate others;

- *Delegation skills* – an ability to allocate tasks to different people. Effective delegation involves more than instructing. It demands a full understanding of the skills that people possess, how they use them and how they might be developed to fulfil future needs;
- *Communication skills* – an ability to use spoken and written language to express ideas and inform others. Good communication is about more than just passing information. It is about using language to influence people's actions;
- *Negotiation skills* – an ability to understand what is wanted from a situation, what is motivating others in that situation and recognize the possibilities of maximizing the outcomes for all parties. Being a good negotiator is more about being able to identify win-win scenarios and communicate them, than it is about being able to bargain;
- **Industry knowledge** – in order to be successful entrepreneur needs not only to identify opportunity in the market, but also understand its perspective in the given context. This can be achieved by spotting a gap and figuring out how can this gap can be filled, what features will be needed and why they will appeal to potential customers.
- **Personal motivation** – entrepreneurship is not an easy way. It involves a lot of hidden pits and other potential risks. An individual who's willing to try his best in creating a new venture should be prepared for all the future obstacles and downfalls. In order to successfully overcome those, entrepreneur needs to have a strong vision and understanding of why he's doing what he's doing. This confidence should also be translated to potential customers.

Eventually, businesses are made and run by people and can become successful only if the people who make it up are properly directed and are committed to make an effort on its behalf. An entrepreneurial venture also needs the support of people from outside the organization such as customers, suppliers and investors. To be effective, an entrepreneur needs to demonstrate a wide variety of skills in the way of general management, dealing with other people, in-depth knowledge of the industry he operates in as well as some degree of personal desire for success. All these different skills are interrelated and are not of given nature. They must be learnt and practiced both from entrepreneurs' personal experience or by exchanging knowledge with others. Entrepreneurs should constantly audit their abilities, recognize their strengths and shortcomings and plan how to develop those skills in the future.

### 3.2 Startup theories

This segment is devoted to description and discussion on related startup theories. The main reason for choosing the startup perspective is because the crowdfunding process is incorporating a set of elements – opportunity recognition, designing, pitching, development of a prototype,

organizing a media coverage, etc. – that are very similar to the actions which startup entrepreneurs undertake in the process of product development and new venture creation.

For a long period of time, researches classified startups just as a smaller version of regular enterprises. However, in 2011, one of the most famous books on startups in recent years – “The Lean Startup” by Eric Ries – has significantly changed the way startups are recognized. In it, the author states that startups operate on completely different principles and therefore require a different set of skills and approaches. Ries identifies startups as “*organizations dedicated to create something new under conditions of extreme uncertainty*”. This uncertainty turns out to be a result of startup entrepreneurs having very limited understanding of who are their future customers, how the final product should look like and therefore how to exactly manage the emerging venture. All of this leads to the fact that majority of startups go shutdown within first couple of years of their lifespan. In this context, Ries identifies the key success drivers for startup survival in *discovering* and *engaging* of early adopters of company’s products instead of targeting average customer groups. Ries describes early adopters as individuals who “*feel the need for the product most acutely*”. This need later translates into higher indulgency towards entrepreneur’s mistakes and increased eagerness for provision of feedback. In case of crowdfunding, successful outcome of the campaign is directly tied in with the attraction of these early adopters (backers) and their further engagement in creation process. Ries states that the end goal of establishing early contacts with early adopters is not about gaining definitive answers, but rather clarifying and validating entrepreneurial understanding of the potential customer base and the problems they demand to be solved. Based on that, entrepreneurs can “*craft a customer archetype*” which will become the basis for further strategic planning. However, it needs to be mentioned that this idea has already been introduced earlier by Steven Blank in his groundbreaking book “Four Steps to Epiphany” (2006). In it, Blank criticizes the suitability of product development approach for startups and proposes the new *customer development approach*. As it has been stated earlier, the main problem for startups lies not in the field of new product development, but rather in lack of existing customer base and tested revenue model.

Considering all of this, Ries proposes a concept of *Build-Measure-Learn*, where he states that for startups the vital part and way for building a sustainable successful business is to organize constantly accelerating process of receiving *feedback*. “*The fundamental activity of a startup*” according to Ries “*is to turn ideas into products, measure how customers respond, and then learn whether to pivot or preserve*”. The importance of rapid feedback is also highlighted by Mullins and Komisar (2009).

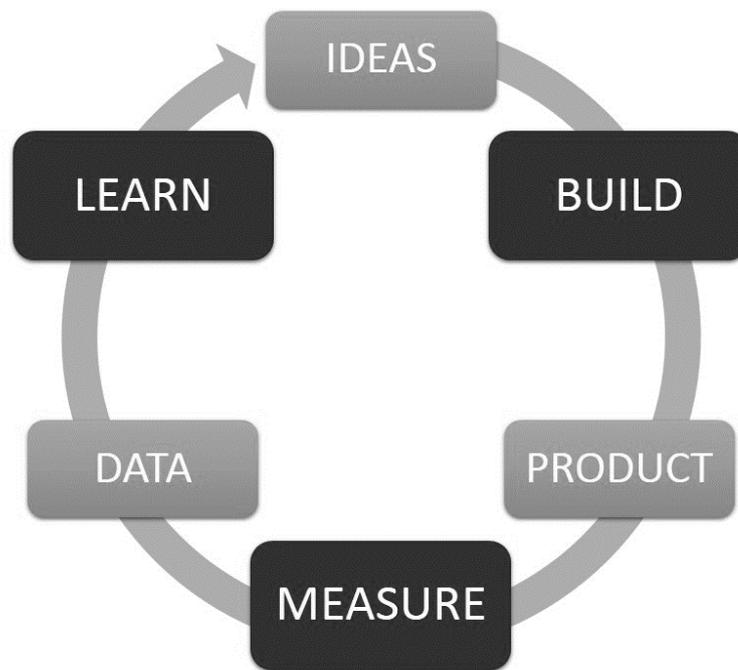


Figure 7. “Build-Measure-Learn” loop. Source: Eric Ries “The Lean Startup” (2011)

In case of crowdfunding, the expected findings of this thesis will highlight that this disruptive instrument allows for outperforming utilization of Ries’s concept by simultaneously proposing the product concept, receiving real-time feedback and further pivoting. This also leads to the hypothesis that the accelerated learning loop is as valuable for crowdfunders as getting funding is.

Another important element of Ries theory is so called *minimum viable product* (MVP) – a rough prototype of the final product, which incorporates the key features that need to be tested in front of potential customers. The goal of an MVP is to validate ideas and enable fast learning by assessing initial reactions of users, and even though MVP can “*lack many features that may prove essential later on*” it allows for justified pivoting in the process of production. The concept of MVP perfectly fits into crowdfunding idea – on CFPs entrepreneurs are provided with the unique testing ground, where they can find out for themselves whether or not their idea is attractive and has a potential for future growth.

The concept of MVP also highlights the differences between traditional strategy of bringing an idea to market, and the one of crowdfunding, where potential customers are directly involved in the process of product development. In this context, the ideas of Roberto Verganti (2009) seem to resonate well with the crowdfunding way. Verganti states that instead of bringing on the finished products, companies need to shift to introducing of *proposals* – a perspective concepts of entrepreneur’s *vision*. In that way, CFPs serve as a showroom of these proposals, where early

adopters (backers) decide which proposals (projects) deserve to be realized (funded) and which need to be reimaged. Due to the relatively low costs associated with running of a crowdfunding campaign, entrepreneurs can experiment with such proposals, in order to mitigate uncertainty by locating customer retention point that Verganti calls *borderline*. According to him, knowledge about *borderline* is extremely beneficial for entrepreneurs, which also corresponds with Eric Ries ideas of *validated learning*. Ries states that “*validated learning is the process of demonstrating empirically that a team has discovered valuable truths about a startup’s present and future business prospects*”. This type of knowledge can be considered as an essential competitive advantage of the firm.

The last important theoretical element that needs to be taken in consideration would be Ries understanding of why do startups tend to fail. He argues that majority of the problems lies within the field of management, which translating onto the crowdfunding concept highlights the following possible weak points:

### 3.2 Marketing theories

As it has been stated earlier, the result of crowdfunding campaign on CFPs is directly related to the amount of investors (backers), that project creator has managed to attract. Majority of guides on crowdfunding state the importance of communication as the cornerstone of any crowdfunding campaign. In addition, even though the crowdfunding’s main goal is fundraising, its mechanisms mostly incorporate marketing elements – pitching, promoting, communicating, etc. In this segment, an attempt to assess crowdfunding campaign as a marketing process will take place.

Osterwalder and Pigneur (2010) approach the process of customer attraction as a result of company’s *value propositions* to them. Value propositions can be identified as a set of potential benefits offered by the company with the goal to satisfy customer’s needs. Considering the basic principle of crowdfunding – pitching ideas to get funding – formulation of attractive value proposition is vital for campaign success.

However, just stating the potential benefits is not enough. In order to grasp the attention of potential customers, the message should be delivered in convincing way. As a results of the convincing pitch, potential customers should have a clear picture of product’s benefits and value offerings in order to make a justified decision to support the project. However, it’s also important not to mislead customer’s perception of the product, by inadequately formulating product functional benefits (USP) and non-functional benefits (ESP). In order to additionally support the

message, amongst other things, Pelsmacker et al. (2010) highlights the importance of throughout media coverage of the advertising campaign, the point which can be directly translated onto crowdfunding.

In the context of this thesis, one of the research goals is to understand *why* crowdfunders communicate with backers, *what* is going to be communicated and *how* it's going to be communicated.

### Summary of the chapter

In accordance with the stated research questions, the selected theories have been divided into three parts – Entrepreneurship theories, Startup theories and Marketing theories.

	Theme	Concepts
<b>Entrepreneurship theories</b>	Crowdfunder as entrepreneur	Entrepreneurial characteristics
		Entrepreneurial motivations
		Entrepreneurial skills
<b>Startup theories</b>	Crowdfunding as a business strategy	Build-Measure-Learn
		Validated learning
		MVP
		Proposal
		Borderline
		Early adopters
		Feedback
Customer discovery		
<b>Marketing theories</b>	Crowdfunding process as a marketing campaign	Value propositions
		Advertising campaign
		USP and ESP
		Customer engagement
		Co-creation

Table 4. Overview of theoretical framework. Source: Own creation

## METHODOLOGY

This chapter discusses in detail the qualitative research methods used for this thesis in order to answer the main research questions. Explanations and introductions are given for specific subjects that each research method is focused on. Moreover, the choice for all research methods is thoroughly justified.

The research methods conducted for this thesis are entirely based on in-depth qualitative research. The research methods consist of three methods:

- Desk research
- Exploratory case study
- Qualitative semi-structured interviews

The body of research findings examines and explains the main motivations, the characteristics of main actors, the success factors, and drawbacks for using crowdfunding for one's business. Furthermore, gathered findings contribute and build on a better understanding of socio-economic aspects and setting of crowdfunding in general, with a focus on utilization for business purposes.

### 3.1 Desk research

Desk research was carried out to examine the literature and web resources available and related to the phenomenon of crowdfunding. The main subject of crowdfunding is considerably new, that is why literature is limited almost entirely to online sources. Examination and observation of journal articles, research and working papers, as well as web pages dedicated to crowdsourcing and crowdfunding practice make up the biggest part of secondary data analysis.

### 3.2 Case study

A case study of several successfully funded crowdfunding projects on Kickstarter was conducted as one of the research methods for this thesis. The cases were selected to be accurately representative for the research topic, as we are examining the potential of crowdfunding for utilization by entrepreneurs. The creators of selected cases reflect the target research group.

A case study method was chosen as one of the qualitative research methods because of its exploratory nature in investigating a real-life phenomenon (Yin, 2009). As already mentioned earlier, crowdfunding is a new socio-economic phenomenon that has emerged only recently. Even though it has been generating a great deal of attention from the media, the long-term sustainability of its practice has not yet been proven.

A case study method was used instead of a survey, for it permits a more detailed examination on this subject, which findings contribute to the relatively little research about crowdfunding in general. The case study approach has a strong advantage over a survey, as it uncovers complexities for the subject of focus (Denscombe, 2007).

Furthermore, this study focuses on reward-based crowdfunding model, which is associated with philanthropic motivations and personal aims. Therefore, in order to understand and denote the social setting of this model of crowdfunding the focus on qualitative in-depth research has been selected.

<b>Interviewee</b>	<b>Location</b>	<b>Project name</b>	<b>Project category</b>
Michel Gagne (creator, interviewee)	Washington, USA	The Saga of Rex: The Animated Film Project	Animation
Matthew Snyder (creator, interviewee)	Illinois, USA	SNOOZ: Sound. Sleep.	Technology
Xavier Peich (creator, interviewee)	New-York, USA	SmartHalo	Technology
Scott Cross (creator, interviewee)	New-York, USA	flatev - The Artisan Tortilla Maker	Product Design
Yuriy Boguslavsky (creator, interviewee)	Moscow, Russia	Ships of years past - stop-motion film	Animation
Dmitry Gorilovsky (creator, interviewee)	Izhevsk, Russia	Lightpack — ambient backlight for your displays	Hardware
Avenir Babin (creator, interviewee)	Moscow, Russia	ATRI – the light tablet	Technology
Rafael Gaynullin (creator, interviewee)	Moscow, Russia	PEGTOP	Product Design

*Table 5. Overview of the cases. Source: own creation*

### 3.4 Data collection

The case study of selected companies involves four data collection methods:

- In-depth semi-structured interview with CEOs or co-founders;
- Analysis of secondary data like presentations, documents and notes, news clippings and other articles in the mass media, newspapers, websites, blogs and social media websites;
- Direct observations of crowdfunding campaigns and its dynamics in general;

The selected sources of data allow for more valid research as they fit into the concept of triangulation, which allows for cross-checking and elimination of invalidity issues (Saunders, 2009).

### 3.5 Interview structure

Semi-structured in-depth one-to-one interviews were conducted as one of the qualitative research methods for this thesis. Interviews were chosen in order to gain insight information highlighting entrepreneurial characteristics, motivations, success factors, social relationships and drawbacks of crowdfunding. Interviewees provide this information based on their experience with crowdfunding platforms.

As discussed earlier, crowdfunding is complex in nature and it presents an unexplored area for research. Interviews were chosen, as part of the qualitative data collection of research, for their attribute of providing explorative data on subtle phenomena (Denscombe, 2007). The aim of this dissertation is to investigate crowdfunding practice from various perspectives in order to answer the main research question. Interviewees provide insight information and serve as informants to a complex subject such as crowdfunding is (Yin, 2007). In order to gain insights concerning feelings, emotions, opinions and experiences of individuals (Denscombe, 2007), interviews were chosen to provide more in-depth data for research findings. The information collected is not simple, but rather complex. Therefore, a questionnaire method would not have been sufficient to investigate crowdfunding phenomenon in-depth with a focus on social aspects.

Semi-structured one-to-one interviews were conducted in order to let interviewees develop and broaden their ideas while keeping a clear focus on the subject. A list of open questions regarding the main sub-questions of this research topic was used, allowing space for the 'snowball effect' of ideas, opinions and thoughts to be discussed, and thus provide insight information on the phenomenon of crowdfunding. The majority of interviews were conducted one-to-one using live Internet-video software Skype, due to interviewees residing in different countries or cities. One-to-one approach was used for it allows to identify and elaborate on specific ideas of interest, mainly the sub questions addressing personal characteristics, motivations, relationship between individuals, success factors and drawbacks for using crowdfunding.

A total of six individuals were interviewed for this study. Interviews took place in the period from February 2016 to April 2016. All interviewees had been project owners of their creative projects on crowdfunding platforms. Interviewees were chosen for their experience in running a project campaign on CFP and the privileged information they possess.

## EMPIRICAL RESEARCH

This chapter concentrates on the analysis of results obtained from the qualitative research using methods of desk research, case study and semi-structured interviews. In order to be able to answer the main questions of this study, the research methods focused on obtaining results from conducted interviews to answer the following research questions:

1. What are the benefits and drawbacks of crowdfunding?
2. What individual characteristics are required for successful crowdfunding?
3. What are the specifics of pre-planning and execution of crowdfunding campaign?
4. What are other applications of crowdfunding beyond fundraising?

The obtained research findings and observations conducted via desk research, multiple case study and qualitative interviews with six entrepreneurs contribute to the main answer of the research question, which is defined in the conclusion chapter. Moreover, the findings from the entire qualitative research, as well as the examination of the theoretical framework, serve as a foundation for final recommendations for individuals willing to utilize reward-based crowdfunding model in order to successfully achieve desired goals.

### 4.1 Valuation of crowdfunding

In order to find out what are the benefits and drawbacks of the crowdfunding phenomena we will take a look at opinions of various expert in the field. The analysis will be carried out using secondary sources of data. The final conclusions will be presented using SWOT analytical matrix.

We will begin by taking a look at what are the noticeable *strengths* of crowdfunding. The first major benefit includes maintaining full control of company's assets. In the case of venture capital and business angels, investors gain significant control over company's decisions. Crowdfunding is different – entrepreneurs do not need to give away such rights. So, when a company's capital is raised through crowdfunding, entrepreneurs do not lose the right to make company's decisions themselves.

Secondly, raising capital through crowdfunding platforms is exceptionally accessible. According to Bechter et al. (2011), crowdfunding platforms “*address the problem that the majority of entrepreneurs fail to raise venture capital for two reasons. Firstly, most entrepreneurs do not qualify for venture capital since they can't grow fast enough, nor do they have the potential for a large public offering. Secondly, there are too few venture capitalists versus the masses of entrepreneurs who need money.*” Sigar (2012) expresses the same ideas – small businesses have very limited financing options. According to her, bank loans are often denied due to a lack of

collateral, operating history and a proven track record. Also, private financing from venture capital firms and angel investors only fund a small number of businesses. Sigar (2012) perceives crowdfunding as an opportunity to fill this capital gap by connecting small businesses, which are marginalized from the traditional sources of funding, to the general public.

What is more, entrepreneurs seeking to raise capital through crowdfunding platforms are awarded with a chance to test marketability. The whole mechanism of crowdfunding is based on attracting a big number of individuals, who find an idea interesting, worth their investment, time and attention. When a funding portal announces a new idea or business model, a deadline for reaching a fundraising goal is usually set - some make and even exceed the goal, some don't. Ramsey (2012) emphasizes that "*they can gauge the potential for a successful start-up of the business based on the public's response to the request for support*". In other words, if so many individuals believe in an idea or a business model and it is crowdfunded, this probably expresses the "*wisdom of the crowd*" – the idea or business model is likely to succeed.

Lastly, crowdfunding provides benefits for communities through both local and global means. Kitchens and Torrence (2012) state that crowdfunding is going to be a tool for people to invest in their own communities and this will help to create sustainable economic health. Ramsey (2012) supports the idea by stating that crowdfunding creates "*opportunities to talented people with limited resources and to investors who want to keep that talent in the community*". According to Blechter et al. (2011), nowadays modern technologies allow to overcome geographical barriers and access money globally. Findings of the research (Blechter et al., 2011), reveal, that most entrepreneurs focus on a project within their geographical community but try to raise funds globally.

Some weaknesses of crowdfunding (named by Gobble (2012), Sullivan & Ma (2012), Galwin (2012), Sigar (2012), Shirky (2012) and others) are of internal origin; they are the characteristics that place crowdfunding at a disadvantage relative to other means of financing, and can be perceived as *weaknesses*.

To start with, entrepreneurs seeking to crowdfund their businesses should consider the administrative and accounting challenges they are going to face. Even though currently crowdfunding is based on donors receiving rewards, the job of recording contributions and sending rewards is time consuming. When a large number of investors become shareholders, business will face even bigger administrative and accounting challenges – "*this would require meticulous and laborious bookkeeping of all investments and shares in the business to determine the share of profits to which each investor is entitled to*" (Sigar, 2012). Kitchens & Torrence (2012) emphasize,

that a large base of unsophisticated investors is a challenge not only to administrate, but also to communicate.

What is more, Sullivan and Ma (2012), Bechter et al. (2011) and Galwin (2012) state that entrepreneurs seeking to crowdfund their businesses face the risk of their idea being stolen by better funded investors or large corporations. Entrepreneurs might lack knowledge to protect their ideas and business plans, and, moreover, in case an idea or business plan is stolen, most entrepreneurs would lack resources to fight for it in court. Such risk in this paper is considered a weakness, because it is a feature of the mechanism of crowdfunding – presenting ideas and business models in public is a must.

Also, the concern for fraud is expressed by Sullivan & Ma (2012), Galwin (2012) & Sigar (2012). In order to foster the development of crowdfunding, various legislative acts are being introduced which loosens regulatory requirements for small businesses in various ways and it can become a precondition for fraud via crowdfunding (Gobble, 2012). As a result of reduced requirements for public disclosures, some businesses can try to conceal their true financial status. Also, some businesses might even be created as fraud – companies can be started in order to take funding, pay it all as salary and then shut down. Sigar (2012) expresses opinion that whilst implementing rules, legislators should carefully consider the ways to protect investors, especially vulnerable ones, who lack “*financial sophistication*”. Weaker investor protection and potential for fraud in this article is considered as a weakness, because, the ongoing legislative changes are solely subject to crowdfunding, they are not applicable to other means of raising capital.

Also, crowdfunding is an internet based approach. Sigar (2012) draws attention to the fact, that “*the internet, which replaces real life encounters with virtual meetings, could make it more difficult for investors to determine whether an issuers business is legitimate*”. Also there arises a problem of choosing a trustworthy crowdfunding platform. It is an issue for both, investors and entrepreneurs. Though huge amounts of information can nowadays be found on the internet, it is difficult for unsophisticated investors to decide on which intermediary and which business can be trusted and worthy. There are no brokers to give an advice.

Some *opportunities* of crowdfunding can also be found listed (Blechter et al., 2011; Sigar,2012; Kitchens & Torrence, 2012 and others) amongst the advantages of crowdfunding. Despite that, an insight is needed here – as crowdfunding is a novelty and emerging very fast, exploring the elements it could exploit to its advantage could enhance the importance of crowdfunding and fasten its development.

First of all, a good look at the crowd, i.e. the contemporary society, needs to be taken. In the knowledge economy, the formation of an information society should be noticed and taken into account. As technology has become more advanced over time, the usage of internet emerged and this triggered the popularity of various social networks and projects based on crowdsourcing to increase. Social networks and crowdsourcing can be employed for the benefit of crowdfunding. Crowdfunding can employ social networks for promotion. Blechter et al. (2011) state, that social networks can serve as a medium in promoting a project to friends and, respectively, their friends. Blechter et al. (2011) present data, suggesting that *“investment accelerates as the entrepreneur gets closer to the required sum whereby outsiders contribute most funds as opposed to the initial phase where friends contribute the most”*. So, after family members and friends contribute in the initial phase, they can recommend the business for their friends through social networks and serve as a trustworthy source. Having such recommendations and seeing that a big part of the amount is already raised, outsiders are more likely to contribute. Also, the possibility to couple crowdfunding with crowdsourcing looks promising. According to Sigar (2012), crowdfunding can serve as a tool for innovators to improve their business models and products or services before they are even offered to public. Blechter et al. (2011) say that an idea being posted online would be evaluated and after consensus has been reached crowdfunded. Blechter et al. (2011) state, that such coupling may not be suitable for commercial projects due to the issue of ownership.

The positive effects crowdfunding is expected to have on economy can also be perceived as an opportunity. Crowdfunding is said to be capable to create of new jobs (Sigar, 2012), to catalyze long-term economic recovery (Gobble, 2012), foster economic development (Kitchens & Torrence, 2012) and innovations (Shirky, 2012; Kitchens & Torrence, 2012). The JOBS Act is designed to increase job creation and economic growth by improving access to public capital markets for emerging growth companies (Kitchens & Torrence, 2012). Similar effect is probably expected in the Russia. Sacks (2012) says, that even if there are entrepreneurs with ideas, there will be no businesses and no jobs unless there is capital. The benefits on innovation ecosystem are also significant. According to Shirky (2012) *“This isn’t the side effect, this is really the main effect of improving the startup economy: getting more people to try more ideas, which inherently means more failure. But it also means more experience, it means more surprises, it means lower cost”*. Kitchens & Torrence (2012) express very similar ideas stating that economic growth is driven by innovation, innovation is driven by experimentation and experimentation is driven by crowdfunding. Also, according to Sigar (2012) small businesses provide consumers with more product and service options. With so many positive effects expected to occur, implementing crowdfunding must be considered of high importance, what means that legislators are supposed to

listen to both supporters and opponents and make decisions fairly fast. Also, the positive effects of crowdfunding might be used as leverage in the discussion between supporters, opponents and legislators.

Also, crowdfunding is designed as a niche investment opportunity / way to raise capital. It is not expected to compete with other ways of raising capital or to invest. On one hand, Shirky (2012) grounds the idea, that crowdfunding is a niche method to raise capital and states that there will probably be no overlap, even in the early days, between the VC traditional targets and crowdfunding. He believes that „*crowdfunding will reveal itself to be a source of all kinds of startups that just weren't part of the current ecosystem*“. On the other hand, Farrell (2012) introduces an infographic on the history of crowdfunding. The infographic grounds the importance of small businesses on economy and overviews the investing public. According to the infographic, crowdfunding should reveal itself as a new investment opportunity, available to those, who don't have enough money to invest in stock. The idea, that crowdfunding is more likely to compete with gambling than other investment opportunities can be retrieved.

	<b>Helpful</b>	<b>Harmful</b>
<b>Internal origin</b> (attributes of the crowdfunding)	<b>STRENGTHS</b>	<b>WEAKNESSES</b>
	Entrepreneurs keep the right to make company's decisions themselves.	Administrative and accounting challenges
	Accessibility of capital	Only internet-based, lack of advise
	A chance to test marketability	Ideas and business models presented on public can be easily stolen
	Benefits community building	Weaker investor protection and potential for fraud
<b>Internal origin</b> (attributes of the crowdfunding)	<b>OPPORTUNITIES</b>	<b>THREATS</b>
	The existence of information society (social networks for promotion, possibility to couple with crowdsourcing)	Current legal restrictions are not suitable for crowdfunding
	Positive effects crowdfunding is expected to have on the economy	The risky nature of small businesses
A niche investment opportunity / way to raise capital		

Table 6. SWOT analysis of crowdfunding. Source: composed from various sources.

Every novelty is very vulnerable due to the lack of experience and existing negative forces in the environment. Finding out and monitoring threats - elements in the environment that could cause trouble for the business or project is especially important for innovative companies or in this case methods, that are expected to foster huge changes.

The risky nature of small businesses might also be considered as a threat towards crowdfunding. Sigar (2012) states that startup companies are traditionally riskier and have a higher rate of failure in comparison with other businesses. Uncertainty about the development of unproven products and services arises. Sullivan and Ma (2012) also express the fear that many crowdfunding investors will be sadly disappointed when business they invest in fails, since many do in the first 5 years. This may cause not only disappointment, but lawsuits might be started as well. Moreover, Gobble (2012) draws attention to the fact, that getting financing through crowdfunding is easier, in comparison to venture capital. Entrepreneurs might misjudge by choosing an easier way, despite venture capitalists offer help - mentorship, advice, useful contacts - in addition to money. Sometimes such help can be crucial for a small company to succeed.

The identified strengths, weaknesses, opportunities and threats of crowdfunding are summarized in the Table 2.

#### **4.2 Crowdfunder as entrepreneur**

In order to answer the second research question: “*What individual characteristics are required for successful crowdfunding?*”, we will take a look at several entrepreneurs who has successfully financed their projects through crowdfunding. The reason behind the stated question is the fact that pretty much everyone can create a campaign and try to collect money on CFPs, however not everyone who’s using this tool can be identified as an entrepreneur. The analysis will be carried out via conduction of a semi-structured interviews. Primary data will be used.

The main goal of this part is to identify the characteristics of an individual crowdfunders, based on which to make more general conclusions. It needs to be mentioned, that even though we investigating into individual entrepreneurial characteristics, the teams behind crowdfunding projects can consist of more than one person. In coordination with research question and previously discussed theoretical framework, the following variables will be analyzed: entrepreneurial characteristics, entrepreneurial skills, and entrepreneurial motivations.

The last thing to mention is that even though the listed variables are separated, all of them are affecting one another and having an impact on the process of opportunity recognition, idea development, and value exploitation.

Existing studies and research suggests that individuals use crowdfunding in order to raise funds from targeting a general public, also called the crowd (Belleflamme et al., 2010). The research findings gathered from multiple case studies and individual interviews justify this statement and also present new evidence and perspectives about other motivational factors influencing creators. Extrinsic and intrinsic motivations are discovered from direct answers to interview questions, and also by observing and interpreting given answers. Extrinsic motivations result in obtaining a reward, recognition or satisfaction for the work done, while intrinsic motivations highlight taking up an activity for fun or one's own sake (Kleemann et al., 2008).

The main extrinsic motivation was identified as *seeking for funding* when running a project on CFP. This finding is confirmed by eight out of eight interviewees, who ran a crowdfunding project on Kickstarter. Interviewees indicated that finding investors who would be interested to invest into creative idea projects is extremely difficult, and the results are rarely positive. As one interviewee notes: "*Having a full time job, a marriage, and two children did not present me with a lot of opportunities to seek professional investors like a record label or whatnot.*" (Scott Cross, fletev). All eight interviewees received successful funding for their project, which confirms the high success rate for campaigns run on CFPs. According to statistics of Kickstarter, 43% of all projects receive successful funding (Kickstarter, 2016).

Another extrinsic motivation observed from majority of the interviews is *seeking for public attention* for presented projects. This motivation proves to bring awareness to projects regardless the success of the funding result on crowdfunding platform. One interviewee noted that he gained public attention for his animation project although his project on Kickstarter did not receive significant overfunding (Boguslavsky). Creator received personal checks, as philanthropic donations from strangers after his project had been successfully funded on Kickstarter. This finding signifies that creators not only gain momentum while their projects are actively running the campaign on Kickstarter, but also *attract attention* and *bring awareness outside the crowdfunding platform*.

With the case of Lightpack, the project gained public attention from various media outside their home country Russia. For instance, US tech internet magazine Engadget acknowledged Lightpack and its project on Kickstarter, and brought awareness to its creators<sup>4</sup>. The CEO of Lightpack approximated that the overall public attention that the project gained due to the success on Kickstarter platform is approximated to a value of at least 100,000 USD in advertising. Therefore, Kickstarter platform is also used for promotion, public attention and awareness

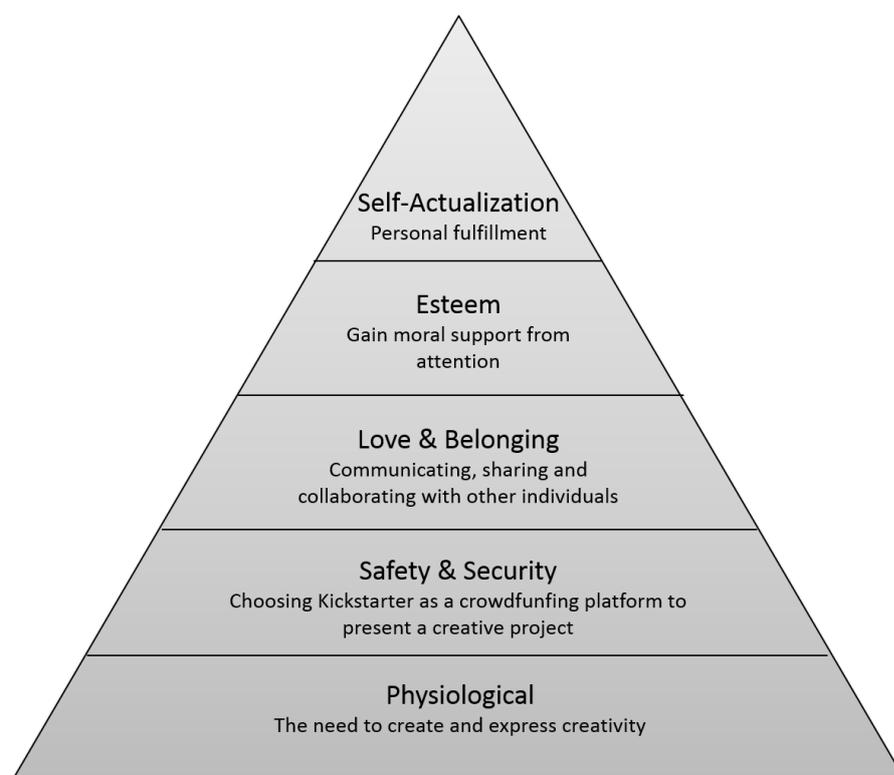
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<sup>4</sup> <http://www.engadget.com/2013/04/25/insert-coin-lightpack/> - Engadget article about Lightpack

generation, and not only for generating funding. Authors Belleflamme et al. (2010), at the time of their study of economic implications of crowdfunding, already acknowledged that crowdfunding could serve as a promotional tool.

Moreover, interviewees noted that once awareness is achieved and a project is successful, the crowd continues to donate money even though the project has already reached its funding goal. This finding suggests that crowdfunding model on Kickstarter has the ability to influence a *self-generating model of bringing attention and awareness to projects and their creators*.

The majority of interviewees also identified that Kickstarter was used to satisfy a *personal needs* of project creators. Five out of eight individuals (Gagne, Peich, Boguslavsky, Babin,



Gaynullin) who ran a creative project on Kickstarter highlighted different personal self-actualization goals that they anticipated to achieve. Therefore, this confirms that individuals are also driven by an intrinsic motivation for self-fulfillment. This finding directly relates to Maslow's (1943) categorization of human needs based on different motivations. *Self-actualization* is part of social needs that are positioned at the top of the pyramid, signifying that individuals realize personal potentials by presenting projects on Kickstarter crowdfunding platform. Figure 8 highlights motivations for using Kickstarter crowdfunding platform explained with Maslow's human needs motivations.

*Figure 8. Crowdfunding motivations, explained using Maslow's (1943) foundation of hierarchy of needs. Source: own creation.*

However, these intrinsic motivations were not interpreted in the remaining 3 cases (ATRI, SNOOZ and Lightpack). The reason for this can be interpreted in the type of these projects. Although these projects fit the category of creativity on Kickstarter, the main aim for them was to receive funding for their startups. Thus, the ending result was not a project or a product.

Therefore, a conclusion is drawn based on these findings. It is suggested that individuals are able to support personal needs when projects are not startup-driven, but focused on a tangible project or product creation. For instance, one interviewee noted that his animation film project was very personal (Boguslavsky). His main goal was not to raise money, but fulfil a personal desire for making something passionate. This project highlights an aim for personal fulfillment depicted in the tangible product intended for the public.

Moreover, two interviewees acknowledged that improving self-esteem was also among the most important motivations. One interviewee confirmed to have gained moral support for the project, even though he did not manage to successfully achieve all the goals on Kickstarter (Gaynullin). Therefore, individuals who create projects on Kickstarter express the need for self-fulfillment.

### **4.3 Specifics of Kickstarter CFP**

In order to gain a clear picture of crowdfunding campaign phases, we first need to clarify the general specifics of crowdfunding on Kickstarter. We will use the secondary data from the Kickstarter site itself, as well as two video interviews with one of the co-founders of this CFP – Perry Chan - who can provide a more detailed overview on the specificities of the Kickstarter work.

Kickstarter is a crowdfunding website founded on April 28, 2009 by Perry Chen, Yancey Strickler and Charles Adler, that facilitates online fundraising. Based in New-York, USA, it started as a platform for filmmakers and artists, today it is one of the largest crowdfunding platforms worldwide for creative projects, such as film, music, design, art, video games, comics, journalism, publishing, fashion, food, photography, technology and theater.

To date, more than 100,000 projects have been successfully funded on Kickstarter since April 2009, with more than 10.9 million backers and \$2,4 billion dollars<sup>5</sup>.

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<sup>5</sup> <https://www.kickstarter.com/help/stats> - Kickstarter Statistics

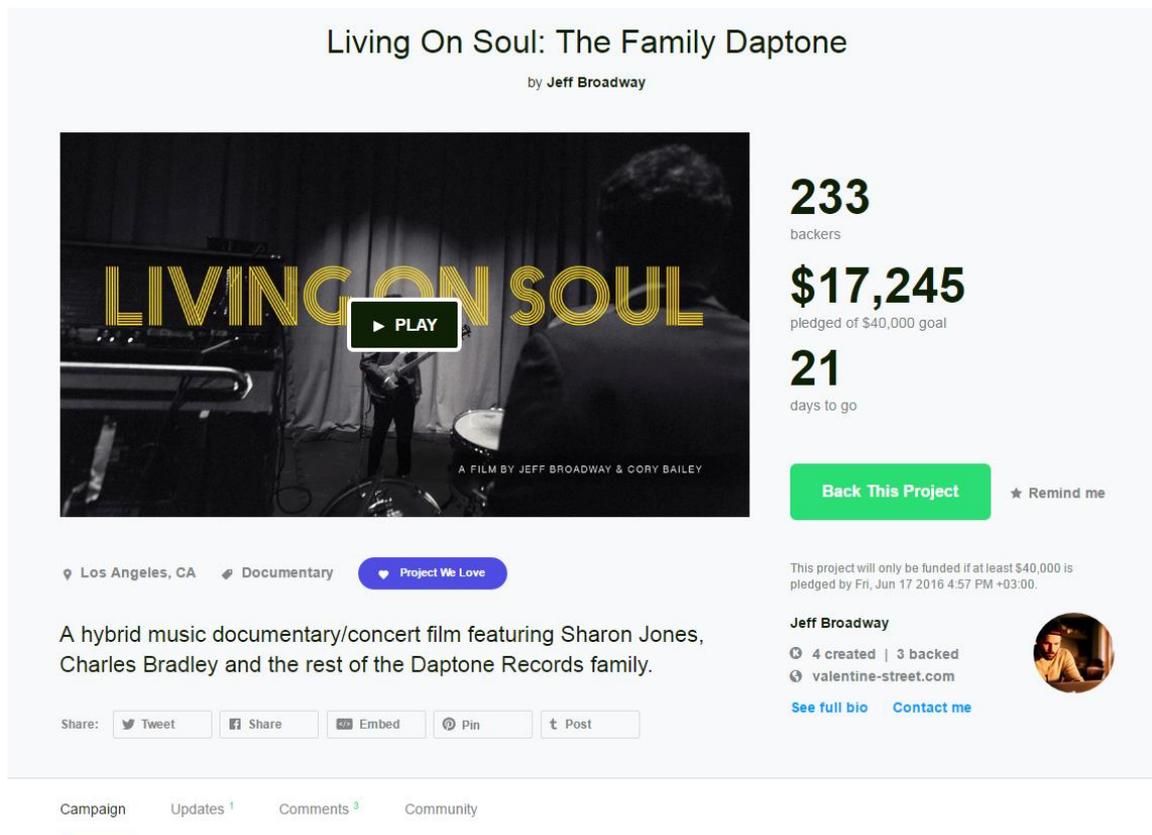


Image 1. Project landing page on Kickstarter. Source: Kickstarter.com

The platform focuses on creative project crowdfunding. According to co-founder Yancey Strickler, creativity can be allotted in many different ways (Ryssdal, 2012). This is why there are 15 creative categories that projects have to fit in. Kickstarter is based on a reward-based crowdfunding model - collecting monetary funding from a general audience of people in exchange for a reward. This facilitation stands as an alternative to traditional methods of investment (Schwienbacher & Larralde, 2010). Instead of specific professional investors providing large sums of money to projects or business start-ups, Kickstarter is a platform where ordinary individuals fund projects of other individuals by donating small sums of money.

On Kickstarter, project owners are called ‘creators’ while individuals who pledge money to projects are referred to as ‘backers’. Every project has a funding goal and a time deadline. Creators have to choose to run their project between one and 60 days, and define the funding goal in dollars to a sum they need to realize the project. According to Kickstarter statistics, the most successful project campaigns run for 30 days or less<sup>6</sup>. After the deadline of a project is reached, it is classified as ‘funding successful’ or ‘funding unsuccessful’ project. Successful projects are those projects that reach their funding goal on time, thus creators receive the pledged money. If projects do not reach their funding goal on time, they are thus unsuccessful. When this occurs, project

<sup>6</sup> <https://www.kickstarter.com/help/faq/kickstarter%20basics> – Kickstarter Basics

creators do not receive any donations pledged prior to the project's deadline as all the money is transferred back to backers' credit cards. This is called an *all-or-nothing* business model.

Furthermore, all proposed projects on Kickstarter platform are closely monitored. Projects have to surpass a quality control evaluation from Kickstarter, examining if criteria and guidelines are met, before they are presented to the public. The platform disregards any projects that favor a personal aim or goal, the so-called '*fund-my-life*' projects (e.g. money for learning a new language, taking a trip, etc.). This curatorial behavior is one of the most significant characteristics differentiating Kickstarter from other crowdfunding platforms alike. Moreover, Kickstarter helps promote projects that are favored by the staff on its blog (Projects We Love section) and on the front page (Staff Picks section, Curated Pages). Kickstarter holds no ownership in the projects. All projects are stored in Kickstarter's data and are open to public view. Kickstarter takes 5% of the money raised for a project, while Amazon withdraws additional 3%-5%, as all the money transfers are carried out by Amazon Payments. Kickstarter appeals to a worldwide audience of individuals. Although, creators of projects have to hold a U.S. bank account, it does not restrict foreign project owners from using the platform. Foreign entrepreneurs usually find friends, family members or acquaintances that are willing to process the U.S. based payment system of a project. Backers of projects, however, are only required to have a credit card, no matter where it is issued.

Perry Chen – one of the co-founders of Kickstarter – states that their main goal was to create a fundraising platform that will allow for creative individuals to share their vision and ideas with the Internet community, and let the 'crowd' to decide whether or not these ideas are worth enough to make it past prototype or concept. Chen specifies that Kickstarter is not just another investment option, because creators do not bear any obligations for the money they receive. However, crowdfunding is not a donation or charity either. It's something different. Chen underlines that they found out that for some reason both entrepreneurs and general public perceives *donations* for non-social causes as something negative. Due to this, Kickstarter founders tried to present a new approach to communication between creator and consumer as something of correlation between patronage and purchasing, which goes in the line with conclusions of Mollick (2014). The final result resembles a merge between pre-sales and exchange – crowdfunders receive money contributions and repay in the form of unique products and services. However, even this definition is not embraces the whole nature of crowdfunding process, because crowdfunders are not obligated to fulfill their *promises*, therefore backers are making their investment decision with certain degree of *risk*.

The funding model of Kickstarter is based on *all-or-nothing* principle. The particular model allows crowdfunders to collect the acquired sum only if it has reached the funding goal that was stated from the very start of the campaign. The sum also needs to be collected in the certain time period, which at average consist of 28-30 days. Otherwise, all donations will be transferred back to investors. The all-or-nothing model was chosen by Kickstarter founders by several reasons. The first and the most important one – it helps to “*mitigate risks associated with limited legal protection of backers*”<sup>7</sup>. We have already highlighted this problem in the valuation of crowdfunding part. However, this approach helps backers to be more confident in that their investments won’t go in vain. On the other side, it also benefits the entrepreneurs because “*nobody wants to end up receiving only a part of the needed financing but still being expected to finish the project*”<sup>8</sup>. The second reason is that all-or-nothing model encourages backers to be more active and beneficial for campaign: if they want to see the project being completed it is in their interest to help spread the word and promote project to others. And finally, it is statistically justified: as we have found out during the literature review “*Of the projects that have reached 20% of their funding goal, 81% were successfully funded. Of the projects that have reached 60% of their funding goal, 98% were successfully funded. Projects either make their goal or find little support. There's little in-between*”<sup>9</sup>.

In addition, Kickstarter has its own rulebook which states certain rules to be followed by individuals or companies willing to participate. Even though Kickstarter administration understands that they can’t cover all the possible nuances of crowdfunding, the goal of the rulebook is to explain Kickstarter’s “*purpose and perspective*”. There exist three main rules<sup>10</sup>:

- **Projects must create something to share with others** – even though Kickstarter allows for all sorts of creative endeavors, the presented projects must have a final outcome that they strive to achieve. Either in a form of product, service or event: the result should be realistic, achievable and shareable.
- **Projects must be honest and clearly presented** – in the mentioned context of limited legal regulation, the Kickstarter community is “*built on trust and communication*”. Therefore, the presented projects must show their trustworthiness by not “*misleading people or misinterpreting facts*”.
- **Projects can’t fundraise for charity, offer financial incentives, or involve prohibited items** – this particular rule just underlines the reward-based nature of crowdfunding by once again

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<sup>7</sup> <https://www.kickstarter.com/help/faq/kickstarter%20basics> – Kickstarter Basics

<sup>8</sup> <https://www.youtube.com/watch?v=3R7mTFHEs1k> – Perry Chen and Walter Isaacson. Kickstarter and the Economics of Creativity.

<sup>9</sup> <https://www.kickstarter.com/help/faq/kickstarter%20basics> – Kickstarter Basics

<sup>10</sup> <https://www.kickstarter.com/rules> – Kickstarter Rulebook

stating that creator are expected to provide something in return for financial support, but “*can’t offer financial incentives like equity or repayment*”. In addition, Kickstarter provides a specified list of prohibited things<sup>11</sup> like political fundraising, medical items, financial services, weapons, drugs, etc.

Moving on to the components of the crowdfunding project itself we can identify the following noteworthy elements. First of all – *comment* section. This is the way for backers to directly communicate with project creators. However, even though everyone can see the comments posted, only the ones who contributed to the campaign can post them. This highlights the exclusivity of communication between project creators and backers. During the campaign period, creators have a set of statistical tools, provided by Kickstarter, for tracking and monitoring all the numbers associated with their project.

The second important element is *updates*. Here project creators can post announcements, share progress or thank the backers. Kickstarter staff emphasizes the necessity of updates, stating that this is the way of “*communicating with backers and keeping them updated on your progress... Being part of this journey is one of the best things about Kickstarter*”<sup>12</sup>. They later identify three main types of updates:

- **Updates that build momentum** – are about informing the backers about new developments and funding milestones;
- **Updates that share the process** – are about keeping backers in the loop after the project is successfully funded;
- **Updates that celebrate success** – after the project is successfully funded become part of a fully customized spotlight page - “*a central hub for news, updates, links to your finished work, and anything else you want people to know*”.

#### 4.4 Specifics of crowdfunding campaign

In order to answer the second question of this research “*What are the specifics of pre-planning and execution of crowdfunding campaign?*”, we’ll focus on what is happening during the actual process of crowdfunding work. To be more specific, we will investigate the different phases of crowdfunding campaign separately. Generally, it can be divided into three main steps: pre-planning, execution and fulfillment. However, in this thesis we are only interested in the first two periods:

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<sup>11</sup> <https://www.kickstarter.com/rules/prohibited> - Kickstarter’s List of Prohibited items

<sup>12</sup> <https://www.kickstarter.com/help/handbook/updates> - Kickstarter’s Creator Handbook

- **Pre-planning** – the period of preparation for the crowdfunding campaign. It roughly starts with the opportunity recognition of a new idea and lasts until the project launches on the CFP. In coordination with the theoretical framework, we can state that this period is similar to the product development phase of the startup, therefore its main characteristic is extreme *uncertainty*.
- **Execution** – the core fundraising period, during which entrepreneur is trying to attract as much backers as possible in order to successfully reach the funding goal during the limited period of time. It starts immediately after pre-planning phase and continues until the campaign clock runs down to zero. In coordination with the theoretical framework, we can state that this period is similar to what Reis stated as the *learning* phase of the build-measure-learn loop.

Everything that goes after the crowdfunding campaign is finished is not the focus of interest in this thesis, but can be viewed on the timeline presented on Figure 3.

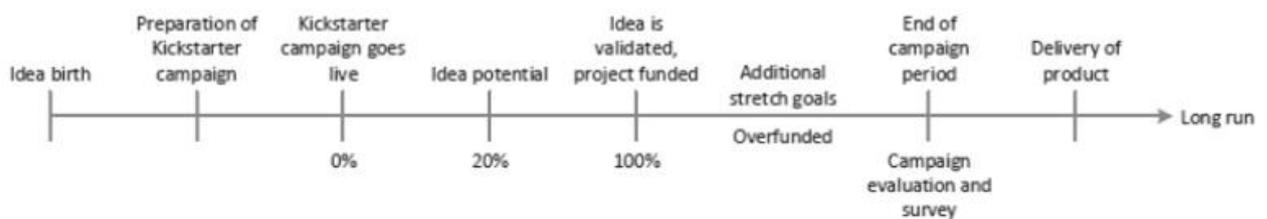


Figure 9. Crowdfunding campaign process. Source: own creation

The following research will be done using data from the selected cases both of secondary and primary nature.

#### 4.4.1 Pre-Planning phase

As it has been discovered during the desk research, the pre-planning phase of the crowdfunding campaign is crucial for its final outcome. It includes everything that entrepreneur undertakes before making a decision to go live. Therefore, this stage is highly specific for each case and amongst other things depends on the *individual characteristics* of crowdfunder. As we have established in theoretical framework, Mollick (2014) stated that one of the key determinants of future success is ability to signal preparedness and assure potential backers of product quality and uniqueness. However, in this period, entrepreneurs are operating in the context of *extreme uncertainty* and do not have a clear understanding of who are their target customer group or how does the final product should look like. Therefore, the whole pre-planning period is characterized by entrepreneurs' attempt to mitigate this uncertainty. Nevertheless, this situation changes when

preparation ends and campaign goes live. After that, the uncertainty is being replaced *learning* in coordination with the ideas of Ries (2011) and Verganti (2009).

Moreover, following the theoretical concepts described earlier, three main elements of entrepreneurs' readiness for campaign launch has been identified:

- Product development
- Value propositions
- Campaign launch preparation

These elements not only characterize the pre-planning phase but also underline the traditional approach to innovation, starting with idea formulation, building of a prototype and future commercialization (Ries, 2011). The last thing to mention is that the financial costs of pre-planning are case-dependent and are not the focus of this research.

### **Product Development**

In this segment, we will take a look at 8 cases of crowdfunding campaigns and how its creators managed to go from idea formulation to building of an MVP, which was later to be presented during the campaign and modified in coordination with the received feedback (Ries, 2011). We will use the product development perspective to understand how entrepreneurs conducted market research, identified potential target customer group and its considerations, designed and prototyped the MVP.

Amongst selected cases, 4 out of 8 has conducted a thorough market research of industry and similar products (Lightpack, SNOOZ, SmartHalo, flatev). In 2 cases (Lightpack, SmartHalo) the companies had previously established customer bases. That way, we can conclude that they have tested their prototypes in advance to launching a crowdfunding campaign. However, the remaining cases also had some sorts of an MVP (in the case of animation projects they were sketches or drafts) and therefore could be accepted by Kickstarter rules. The duration, imputed effort and costs associated with designing of an MVP has varied from case to case and lasted from 1 to 7 months. 6 out of 8 cases ((Lightpack, SNOOZ, SmartHalo, flatev, ATRI, PEGTOP) has decided to patent their products prior to launch, which corresponds with the idea that entrepreneurs fear the public disclosure of the concepts and following intellectual rights thievery. Nevertheless, the other 2 cases were of art nature and the need for patents were not as significant for them. This situation once more emphasizes the problem of insufficient legal protection of crowdfunding participants.

Moving on to customer considerations – 4 cases (The Saga of Rex, Ships of years past, ATRI, PEGTOP) did not run any marketing researches and therefore did not know who are their

customer group. Lightpack and SmartHalo undertake a few market tests and other cases decided to use only secondary sources of data and concentrate on existing customer segments.

## Value Propositions

While the goal of the product development was to build a relevant prototype that will reflect the desired features and show the final vision of the entrepreneur, the way this prototype will be presented to public during the crowdfunding campaign – is the question of how do entrepreneurs manage to formulate their *proposal* (Verganti, 2009). While the CFPs allow for various ways of presenting a project – text, images, sound, etc. – the core of the project pitch is always a *video presentation*. In the video pitch, entrepreneur has to express his vision and convince the potential investors either by making emphasis on *functional benefits* of the product (USP) and/or *emotional benefits* of the product (ESP) (Pelsmacker et al. 2010).

We will investigate into each case by look at the video presentations of each of the 8 cases. In order to assess what elements – USP or ESP – prevail in the video presentations we will evaluate them using the concept of *ethos* (credibility), *logos* (logic), *pathos* (emotion) (Higgins and Walker 2012). The research proposition goes that entrepreneurs will try to establish their credibility (*ethos*) by turning to their reputation, experience and skills, as well as personally appearing in the video in order to present their own products. In case of appealing to backers' logic (*logos*), entrepreneurs will try to emphasize to product useful features and the way it will fill the existing gap. Finally, the emotional component (*pathos*) will concentrate on appealing to backers' feelings.

It is also needs to be mentioned, that according to Kickstarter guidelines, project creators need to manage to tell their story in the format of 3-5 minutes' presentation, which requires a certain level of skill. Therefore, many entrepreneurs turn to professional firms in order to have an attractive and compelling video.

In the selected cases, 5 out of 8 projects turned to outsourced professional studios for help in making their pitches (Lightpack, SNOOZ, SmartHalo, flatev, ATRI). The remaining cases decided to go with their own production. One of the cases (Lightpack) has purposefully shot the video pitch in the way that it will be suitable for both – presentation on Kickstarter as well as on the company's official site.

Considering the video presentations themselves:

- The SmartHalo pitch highly relied on ethos and logos, much more than any other cases, which makes for a conclusion that the goal was to maximize the USP part;

- Considering the value propositions of other cases: 5 cases (Lightpack, SNOOZ, flatev, ATRI, PEGTOP) had an equal mix of both USP and ESP components, while 2 art projects (The Saga of Rex, Ships of years past) concentrated only on emotional benefits.
- The expected findings included all of the video presentation to include significant amount of ESP elements, however only in 2 cases (The Saga of Rex, Ships of years past) they have prevailed over the USP, while others preferred to go with the functional benefits. This can be explained by the artistic nature of 2 of the cases.
- Only in 4 of the cases, the creators emphasized the importance of establishing credibility of the creators (Lightpack, SNOOZ, SmartHalo, flatev). Interestingly enough, this are the cases with the biggest amount of raised funds.

Based on all that, we can state that the importance of presenting the functional benefits of the product over emotional ones seems to have a more positive impact on the resulting outcome of the campaign.

### **Campaign Launch Preparation**

Due to the limitations of this research, we can't identify all peculiarities and aspects of the pre-planning phase. Instead, we will concentrate on the specific aspects that creators prioritize and the way they promote the upcoming campaign. The research proposition goes that the process of advertising and promotion starts way before campaign launch and continues until the last day of fundraising.

All the selected cases and creators has approached the preparation process differently. Judging from the data, all 8 cases started by investigating of Kickstarter rulebook, guidelines and prohibition list, meaning that all of them has at least the basic understanding of the crowdfunding principles. We can judge on the level of their readiness by the fact, that Kickstarter has approved their projects to be presented on the platform.

However, only 3 of the 8 cases has gone further and undertake an in-depth research on crowdfunding specifics and peculiarities (Lightpack, SNOOZ, SmartHalo). The others did very little to almost none. Moreover, its these 3 cases who specifically planned the way their campaign will go, carefully choosing each of the elements to be presented during execution phase. 2 of the art project decided to go with their "*gut instinct*", and the rest thought that they will figure it out on the go. Again, in terms of media coverage and promotion, the selected 3 cases (Lightpack, SNOOZ, SmartHalo) has organized the process way in advance, understanding the importance of this element. However, it's only SmartHalo, who decided to organize the "*snowball effect of information*" by implementing and embargo on publications until the campaign starts.

Additionally, they have emailed a lot of their previous customers and asked for help in spreading the word. The result has vary positively affected the way their campaign started.

#### 4.4.2 Execution phase

In this segment we will focus on what is going on during the actual process of fundraising, which starts after the campaign is officially launches and ends when the stated time period runs out. We will continue answering the question “*What are the specifics of pre-planning and execution of crowdfunding campaign?*”.

As it has been stated earlier, the pre-planning phase of the crowdfunding campaign is characterized by extreme uncertainty. However, when campaign goes love, the uncertainty is being replaced by the process of *learning*. Here, during execution phase, entrepreneurs learn about whether or not their product qualifies to be realized and if not, where is that thin *borderline*, which separates it from being accepted by the public (Verganti, 2009). That way, we perceive crowdfunding campaign as a certain type of product *proposal* – an entrepreneurial vision, which he tries to present to his potential customers. We expect that this *validated learning* is as important and valuable for entrepreneur as fundraising is (Ries, 2011). Even if the campaign turns out to be unsuccessful, the knowledge that entrepreneur acquires is still very beneficial for him. As it has been discovered in the previous chapters – non-financial goals of project creators are prevailing, which contributes to this proposition.

The particular elements of execution phase that will be studied are *customer discovery* and *communication*. We will try to understand what actions do project creators undertake in order to successfully raise the needed sum.

As we have established in theoretical framework, the importance of locating the *early adopters* is crucial for success of the one’s venture. They allow not only to test marketability of the project, but also serve as an extremely valuable sources of feedback provision. As we stated all of the selected 8 cases have come up with some form of an MVP. Here we will try to understand how did they managed to use it in order to locate their customers and receive the needed feedback for further pivoting.

The other studied element is *communication*. As it was stated in Kickstarter Creator Handbook – in order to attract potential investors, entrepreneur needs to communicate with them. Additionally, it emphasizes the importance of honesty and clarity in presentations<sup>13</sup>. The communication side of crowdfunding campaign will be studied from perspective of three elements:

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<sup>13</sup> <https://www.kickstarter.com/rules> - Kickstarter Rules

- Updates and Stretch Goals
- Comments
- Media coverage and promotion

As it has been stated earlier, updates and stretch goals help to maintain connection between creator and backer, keeping them in touch about the current progress of the project or some new interesting offerings and announcements like the stretch goals. Comments allow for backers to directly communicate with the creator and media coverage intensifies the supply of potential investors.

### **Discussion of the results**

As all of the 8 creators has stated, we can conclude that they have tested the marketability of their ideas. All of them agreed that they have successfully located the early adopters of their products and because of them – successfully reached the funding goal.

In the words of Perry Chen, this is one of the major unique benefits of crowdfunding *“Usually, it is extremely hard to test marketability of products... I mean, there are no magic solutions to understand whether or not it’s going to work. However, through crowdfunding these becomes possible...”*<sup>14</sup>.

With the video presentations, it has been concluded that using of the USP and ESP is situational and do not have such a strong impact of the campaign’s outcome. Either way, we can see that all of the cases tried to explain in their pitches the various benefits of their products. They tried to appeal both to logic and emotion

The importance of acquiring of the early adopters has been driven by two main factors: to understand the potential target group for the product and to get access to valuable feedback early in the process of production. 7 out of 8 cases has successfully discovered something new about their target group and utilized that knowledge to improve their products.

The concept of communication and its elements in relation to crowdfunding campaign has also been analyzed. We have identified the positive dependence between the amount of investments and project updates. Even though the exact number of updates varies quite a lot from case to case, the positive effect remains constant. All of the selected cases has also implemented the stretch goals, however the exact effect of their implementation was not measured.

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<sup>14</sup> <https://www.youtube.com/watch?v=3R7mTFHEs1k> – Perry Chen and Walter Isaacson. Kickstarter and the Economics of Creativity.

Nevertheless, it did help to form a loyal community around the project, which has been confirmed by 6 out of 8 cases. Additionally, interviewees emphasized the importance of updated in resolving of confusion and misunderstanding between creators and backers.

All of the creators signaled that the amount of work that was putted into crowdfunding campaign has surpassed their expectations. 5 out of 8 creators called the process “*exhausting*” but “*satisfying*”. The amount of work has proportionally grown in correlation with the amount of attracted backers.

In case of marketing and promotion, we have identified that initially only half of the cases understood the importance of active promotion off-site. However, as the campaign went all of them realized that they should have invested more in preparation of media coverage.

Finally, the answer to the question “*What are the specifics of pre-planning and execution of crowdfunding campaign?*” is based on the what have been discovered during the process of research. As a result, the following elements have been identified:

- **Pre-planning**
  - The through market research
  - The designing of an MVP
  - The protection of intellectual rights
  - The formulation of USP and ESP
  - The preparation of campaign materials
  - The organization of media coverage
- **Execution**
  - Location of early adopters
  - Active communication with backers
  - Acquiring feedback
  - Pivoting the project concept

## CONCLUSION

The main goal of conducted desk research, exploratory case study and qualitative interviews was to observe and define whether there are potentials for entrepreneurs to use crowdfunding for their business. As we have found out, all of the 8 cases has successfully completed their crowdfunding campaigns, raised the needed sum of money and successfully delivered the products in time. Many of the projects finished far above the target goal, showing an extreme signs of overfunding, which in its own way has led for them to expand and grow further. However, as it has been formulated by Kickstarter's co-founder Perry Chan – crowdfunding goes beyond simple concept of alternative fundraising. It incorporates a set of professional tools, organized in a form of a crowdfunding platform, which can significantly assist in the process of entrepreneurial venture creation. Consequently, all of the 8 cases has initially thought only about making enough money to complete their products, but ended up receiving much more than that – by incorporating the process of learning they have followed the startup way.

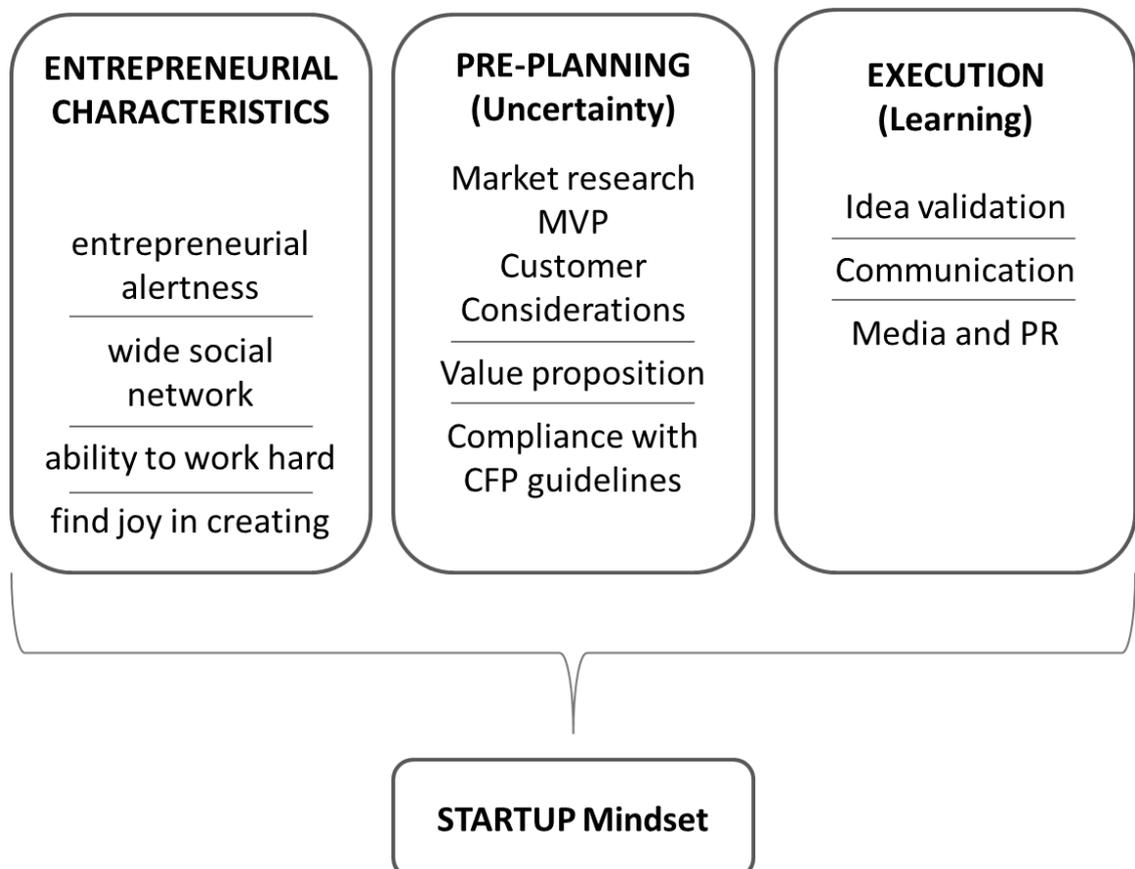


Figure 10. Holistic overview of findings. Source: own creation

As it has been found out during the research, crowdfunding main applications include:

- **Fundraising** – a primary goal and underline basic idea of crowdfunding. All 8 interviewees confirmed that they perceive crowdfunding as a viable option for capital raising. Interestingly enough, all participants stated that if not crowdfunding, they would've

preferred debt financing, which corresponds with the idea that full creative control over the company is important for startup entrepreneurs.

- **Marketing** – as majority of respondents stated, a crowdfunding campaign is an effective way to market a product and enforce community building. Generally, crowdfunding aids in achieve the following marketing goals: a) attraction of early adopters b) organizing media coverage c) forging of multi-dimensional communication on creator-customer level d) viral promotion with the help of supporters.
- **Testing** – crowdfunding to be a suitable way to test markets' need for products - through financing an initiative, supporters (markets) ultimately vote on the projects they find desirable.
- **Customer engagement** – the concept of involvement has surfaced multiple times during interviews. According to interviewees one of the main benefits and reasons to use crowdfunding is its ability to involve and engage supporters with the upcoming product.
- **Real-time feedback** – ability to receive and respond in real-time to feedback from customers was noted by one interviewee as one of the major benefits of crowdfunding. Participant noted that they could observe successes of their online advertising campaign on the crowdfunding initiative almost in real time while they could observe the effects of their own online efforts.

Crowdfunding campaign is eventually an experiment which involves a large number of activities and characterized by lots of learning. In the Figure 6 we provide a holistic overview of the findings and answer the main question of this paper – how can entrepreneurs exploit crowdfunding for their business? The answer is – by obtaining a startup mindset and making a huge emphasis on the pre-planning of the campaign process.

### **Theoretical Contributions**

The main theoretical contributions include deeper understanding of the phenomena of crowdfunding as well as provision of a new perspective on crowdfunding from the position of startup theories.

### **Managerial Implications**

The recommendations for successful utilization and reviewing of relevant theoretical literature will allow for any reader to gain a much clearer picture of crowdfunding phenomena and its possible applications.

### **Limitations of the research**

The particular research concentrates only on reward-based model of crowdfunding and includes only one crowdfunding platform – Kickstarter.

### **Directions for further research**

The particular research can be continued and expanded in the future. The suggestions for further research include three directions. First, is to study the failed crowdfunding campaigns in order to understand what kind of benefits one can extract from this unsuccessful experience. Second, to understand what drives the decision of backers to support certain project and what elements of the campaign have the biggest impact on that decision. And lastly, to study deeper the process of communication between creators and backers and the way the connections between them are formed and maintained.

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## Appendix 1 – Top 10 most funded campaign on Kickstarter

Rank	USD goal	Total USD pledged	Project title	Category	Percentage funded	Number of backers
1	\$500,000	\$20,338,986	Pebble Time - Awesome Smartwatch, No Compromises	Product Design		78,471
2	\$50,000	\$13,285,226	COOLEST COOLER: 21st Century Cooler that's Actually Cooler	Product Design		62,642
3	\$100,000	\$10,266,845	Pebble: E-Paper Watch for iPhone and Android	Product Design		68,929
4	\$20,000	\$9,192,055	The World's Best TRAVEL JACKET with 15 Features    BAUBAX	Product Design		44,949
5	\$10,000	\$8,782,571	Exploding Kittens	Tabletop Games		219,382
6	\$950,000	\$8,596,474	OUYA: A New Kind of Video Game Console	Gaming Hardware		63,416
7	\$1,000,000	\$7,513,523	Pebble 2, Time 2 + All-New Pebble Core	Product Design		40,108
8	\$2,000,000	\$6,333,295	Shenmue 3	Video Games		69,320
9	\$800,000	\$6,225,354	Pono Music - Where Your Soul Rediscovered Music	Sound		18,220

10	\$2,000,000	\$5,764,229	Bring Back MYSTERY SCIENCE THEATER 3000	Television		48,270
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## Appendix 2 – Interview guidelines

1. How did you find out about the phenomena of crowdfunding?
2. What motivated you to use crowdfunding?
3. How did you come up with the idea for your project?
4. Did you have any previous experience in running an entrepreneurial venture?
5. Pre-planning phase
  - a. How did you prepare for your crowdfunding campaign?
  - b. Did you do any market research prior to launching a campaign?
  - c. Did you have an MVP ready to be shown to public?
6. Execution phase
  - a. How did you communicate with backers during the campaign?
7. Do you perceive crowdfunding as a viable option for capital raising?
8. Do you perceive crowdfunding as a marketing instrument?
9. Do you perceive crowdfunding as a testing ground for ideas?
10. What are other applications of crowdfunding for business?
11. What are the main benefits of crowdfunding?
12. What do you think are crowdfunding weak points?
13. What do you think helped you to reach the funding goal?
14. What do you think negatively affected your campaign?
15. Are you planning to continue using crowdfunding in the future?