Choose wisely: Crowdfunding through the stages of the startup life cycle

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Crowdfunding; Startup funding; Crowdsourcing; Crowd capital; Information asymmetry; Crowd communication; Startup strategy

Abstract  Crowdfunding is attractive to startups as an alternative funding source and offers nonmonetary resources through organizational learning. It encompasses the outsourcing of an organizational function, through IT, to a strategically defined network of actors (i.e., the crowd) in the form of an open call—specifically, requesting monetary contributions toward a commercial or social business goal. Nonetheless, many startups are hesitant to consider crowdfunding because little guidance exists on how the various types of crowdfunding add value in different life cycle stages and which type is best suited for which stage. In response to this gap, this article introduces a typology of crowdfunding, the benefits it offers, and how specific benefits relate to the identified crowdfunding types. On this basis, we present a framework for choosing the right crowdfunding type for each stage in the startup life cycle, in addition to providing practical advice on crowdfunding best practices. The best practices outlined have shown demonstrable contributions toward achieving funding goals and are likely to prove valuable for startups.

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1. Startups and crowdfunding

Startups require resources to succeed and one of the most important resources is money. Traditionally, the options for capital formation available to startups were few and comprised primarily of FFF (friends, family, fools), angel investors, venture capitalists, and seed funding (Startup Explore, 2014). More recently, there has been a surge in alternative models. Among these, crowdfunding has emerged as a popular source of capital formation in various fields—from purely for-profit to social causes, technology, performing arts, real estate, and music.

Crowdfunding draws inspiration from the ideas of microfinance (Morduch, 1999) and crowdsourcing. It encompasses the outsourcing of an organizational function (capital formation) to a strategically-defined network of actors (crowd) in the form of an open call (Kietzmann, 2017) via dedicated websites (crowdfunding platforms). And small amounts of money from a large number of people add up. In 2010, crowdfunding was a relatively small industry...
to the tune of $880 million worldwide. In 2015, estimates put the global crowdfunding industry at $34.4 billion (Massolution, 2015).

Crowdfunding is especially suited for startups trying to turn an idea into a viable business and young companies aiming to maintain or grow their venture (Stemler, 2013). Both face challenges when trying to secure funding. Due to lack of credit and operating history, startup founders often have difficulties conveying the value of their proposed venture to investors. Startups, therefore, have difficulty accessing traditional funding options such as bank loans, venture capital, or angel investment. These challenges are exacerbated for social ventures, which are driven by the ambiguous and sometimes dichotomous goal to achieve a double bottom line: to balance social and for-profit goals (Lehner, 2013). In addition, it is often prohibitively expensive for young businesses to access wider traditional capital markets (Tunguz, 2013). These and other factors, such as the shortage of capital provoked by the global financial crisis and the growth in other forms of crowdsourcing, have contributed to the rise of the crowdfunding phenomenon in recent years (Giudici, Guerini, & Lamastra, 2013).

As crowdfunding has been growing in popularity, so has its exposure in academic and practitioner-oriented literature. A number of articles have developed independently of one another but without a unifying framework to understand crowdfunding in the context of the startup life cycle. As a result, startups considering crowdfunding have little guidance on how to decide among the different types of crowdfunding available and the benefits each type can offer in different startup stages. This is an important consideration since funding needs vary significantly across stages, as do the types of returns and assurances offered to a crowd in different crowdfunding variants.

This article closes the research gap by elucidating which crowdfunding type is most appropriate for startups in each life cycle stage. It first lays out a typology of crowdfunding, the benefits crowdfunding offers in terms of financial and nonmonetary resource provision, and how these two aspects intersect. This leads to a framework for decision making, enabling the startup to choose the crowdfunding type best suited for its specific life cycle stage. Once crowdfunding alternatives are considered and a choice has been made, startups face the next problem: how to attract a crowd and its contributions. This article addresses this by outlining best practices for crowdfunding alternatives at each stage.

2. Types of crowdfunding

Crowdfunding as an online distributed funding model suggests that requesting relatively small monetary contributions from a crowd helps startups acquire critical financial resources. In this context, crowdfunding is viewed as a homogenous concept: a general request for money via an open call. However, just as the funding needs for startups vary, crowdfunding varies by the type of rewards offered to supporters. The following section outlines a typology of crowdfunding (see Table 1) by considering if rewards are offered and whether they are tangible or non-tangible (Belleflamme, Lambert, & Schwienbacher, 2014; Canada Media Fund, 2016; NCFA, 2012).

2.1. Donation crowdfunding

In the donation crowdfunding model, the founder receives money from a crowd without any tangible return for that contribution (Canada Media Fund,
In the pure donation model, no rewards at all are offered to contributors. The funds received are essentially a grant given for a specific purpose, but without the expectation of a specific return to the funder. According to a 2015 industry report by Massolutions, donation crowdfunding generates the second-largest funding volume globally (NCFA, 2015) and the idea of donation crowdfunding has been successfully utilized in social marketing for a number of years (Lehner & Nicholls, 2014).

The rewards-based donation model employs an incentive system whereby backers receive nonmonetary rewards that include personal recognition or experiential rewards, such as the opportunity to meet the creators, attend special events, or even to participate in the creation of the product. Donation crowdfunding is more popular for projects with smaller funding goals; globally, 90% of donation crowdfunding campaigns raised less than $10,000 (NCFA, 2012).

2.2. Lending crowdfunding

Lending crowdfunding, often referred to as peer-to-business (P2B) or peer-to-peer (P2P) crowdfunding, raises money with the expectation that founders will repay supporters. Lending crowdfunding is the largest crowdfunding type by funding volume (NCFA, 2015) and takes one of three forms: (1) the pre-sales model, (2) the traditional lending model, and (3) the forgivable loan (NCFA, 2012). The pre-sales model offers the finished product in return for the contributor’s pledge; the contribution amount requested from each crowd member is determined by an assessment of the fair market value of the product. How many pre-sale copies the founder offers depends on the funder’s total contribution amount—larger contributions typically mean a supporter receives more copies (NCFA, 2012). The first-generation Pebble smartwatch is among the most well-known pre-sales campaigns. It raised more than $10 million from nearly 70,000 funders on Kickstarter, more than 100 times its funding goal, and Pebble delivered its first round of watches 10 months after the campaign ended (Schroter, 2014). The traditional lending agreement uses standard terms where loans are repaid with interest determined pre-campaign launch. The forgivable loan repays contributions only if and when the project begins to generate revenue or profit. With both the traditional and forgivable loan, crowdfunding projects are assessed according to their risk levels—either by the platform itself or by a third-party evaluator. Lenders choose the level of risk they are prepared to accept and support projects accordingly.

2.3. Equity crowdfunding

In the equity crowdfunding model, also referred to as investment crowdfunding, the venture raises money from a crowd in exchange for an ownership stake in the firm. That is, investors are offered equity or bond-like shares (Ahlers, Cumming, Guenther, & Schweizer, 2015). Equity crowdfunding is the fastest growing crowdfunding category and the average campaign value is high.1 Investor-led equity crowdfunding typically involves accredited investors, such as venture capitalists, angel investors, or sector specialists who negotiate with the founder on funding terms. These projects are then promoted to accredited investors via platforms that are often subscription-only (Wagner, 2014). In entrepreneur-led equity crowdfunding, campaigns are accessible to all crowd investors and the campaign proponent sets the valuations and determines the terms of the offering.

3. Benefits of crowdfunding for startups

The previous section introduced a typology of crowdfunding considering the type of return or reward to backers. While this is an important first aspect to understand, a startup also needs to consider the specific benefits it aims to achieve in pursuing crowdfunding efforts. First, crowdfunding helps alleviate the capital crunch many startups face. Many campaigns aim to raise a relatively small sum of money for a one-time project or event (Mollick & Kuppuswamy, 2016). Other projects intend to raise a substantial amount of money for more complex and long-term undertakings, providing founders with the funds to turn an idea into a viable business (Mollick, 2014). This method works; nine in 10 successful projects on Kickstarter have turned into ongoing firms and existed up to 3 years later (Painter, 2014). However, crowdfunding in a startup context is not just about funding; it also offers nonmonetary benefits that encompass the following (Belleflamme, Lambert, & Schwienbacher, 2010; Brown, Boon, & Pitt, 2017; Gerber & Hui, 2013; Mollick, 2014):

- Validating the overall business idea—Does the idea actually solve a consumer problem (problem/solution validation)?
- Refining the product or service with potential customers by receiving their feedback, likes,
and dislikes (product validation). In this context, crowdfunding is a means to support user-generated innovation and a way to better understand customer preferences.

- Painting an accurate picture of how a new product will perform before officially going to market (market validation), thus allowing startups to fail early without investing additional time or money if they see little interest from a crowd.

- Marketing, such as promoting a product or a direct sales channel by providing backers with the finished product and ensuring a readily available sales pipeline (market penetration/growth).

Crowdfunding further helps establish a loyal community of engaged customers. The successes of Pebble and Ouya—a video game console—led other developers to write applications for these products even before they were released to the market, helping to build a competitive advantage.

In summary, crowdfunding provides critical organizational resources in the form of money but it also provides non-financial resources, or crowd capital, an organizational-level resource obtained from a crowd (Prpić, Shukla, Kietzmann, & McCarthy, 2015).

4. Selecting the best crowdfunding type for each stage

As previously laid out, crowdfunding provides monetary and non-financial resources. However, in the prevailing view, a startup is often viewed as a single construct: an individual aiming to turn an idea into a viable business that requires resources. The challenge with this view is that it ignores the life cycle a startup undergoes, where each life cycle stage has unique monetary and nonmonetary resource needs. The following section addresses this challenge and suggests that a startup can identify the most suitable crowdfunding method by considering its life cycle stage along with the resource needs at each stage. Adopting the business life cycle framework proposed by Churchill and Lewis (1983), three stages are differentiated. For each stage, key resource requirements are outlined along with the crowdfunding type best suited to meet these requirements.

4.1. Pre-startup stage: Donation crowdfunding

In the pre-startup stage of the crowdfunding life cycle, the founder has an idea and explores the feasibility of building a business based on this idea (Majoran, 2014; MaRS, 2009a). Pre-startup efforts focus on developing a viable offering that solves a significant customer problem as well as identifying the target market, partners, distributors, and competitors. In this formative phase, achieving problem/solution fit and creating a viable business plan are of key importance. Funding needs are primarily for pre-startup R&D, product testing, generating the business plan, and preparing to launch the venture (MaRS, 2009a).

Donation crowdfunding is the most suitable type to meet these needs for three reasons. First, it does not offer a tangible reward to a crowd. At the pre-startup stage, when the venture has not yet generated revenue from the offering, it is still developing the business plan and generally has no financial plan and no track record. The risk of project failure is highest at this stage; therefore, the founder is not in a position to promise tangible or monetary rewards. Second, donation crowdfunding typically allows for more operational flexibility compared to other forms of crowdfunding that have more conditions attached to the financial contributions made by a crowd. Third, the common characteristics of donation-based crowdfunding projects help keep the risk of disappointing crowd members low. Overall funding goals and individual contributions are usually small. For example, a successful Kickstarter project raises an average of $6,000, while the average individual contribution is just $25 (Heyman, 2015). Donation crowdfunding can feasibly provide the necessary capital to move the venture to the next stage in the startup life cycle, at which point founders should reevaluate fundraising approaches.

4.2. Startup stage: Lending crowdfunding

As the venture enters the startup stage, it has ascertained the feasibility of the idea and the credibility of the business model to deliver the offering to an attractive target market (Majoran, 2014; MaRS, 2009b). Efforts now focus on refining the solution or prototype into a minimum viable product and advancing the initial revenue model into a viable business plan (Moogk, 2012). Key concerns in the startup stage are validating product/market fit. Does the product or service deliver on customers’ needs (product validation)? Are prospective customers and distribution partners willing to purchase the product when it is ready for commercial offering and at what price (market validation)? How can the startup expand from that one key customer segment to a broader and sustainable sales base? (Churchill & Lewis, 1983).

Resources in the startup phase are required to build products for prospective customers to test,
hire employees, manage operations, establish the product in the market, and execute the marketing plan for commercial launch (Hofstrand, 2013; MaRS, 2009b). Lending crowdfunding is best suited for ventures in this stage. Having built a viable product that has gone through a few iteration cycles and having generated some initial revenue demonstrates early traction, putting the startup in a stronger position to credibly offer tangible rewards such as monetary interest or a pre-sales product. In addition, a key goal in the startup stage is to validate product/market fit. The lending model helps to achieve this goal by providing a real-life estimate of demand and customers’ willingness to pay, particularly in the case of the pre-sales model. It also builds an initial group of excited early adopters, which creates a competitive advantage for the business. Finally, the startup stage requires substantially more funding than the pre-startup stage (Hofstrand, 2013). P2P or P2B lending platforms often require a higher minimum loan amount from each backer. The minimum loan amount on Lending Club, a P2P platform, is $5,000 and Funding Circle requires an even higher minimum investment of $25,000 (Herrick, 2016). Lending crowdfunding aligns well with this need for higher capital amounts.

4.3. Growth stage: Equity crowdfunding

The growth stage typically begins when the startup has become an efficient, profitable entity. The venture is financially healthy, has sufficient size and market penetration, and has achieved product and market validation. Startup activities focus on scaling operations, processes, and systems to, at a minimum, remain profitable but preferably to grow and earn an above-average economic return on the resources employed (Churchill & Lewis, 1983; Majoran, 2014). As the startup transitions into expansion, it has demonstrated strong growth that is expected to continue. Funds raised at this stage are used to support further growth and may help the startup acquire another company as a way to achieve scale or to provide liquidity and an exit for the founder (MaRS, 2013).

Equity crowdfunding, which offers a financial return to backers, is the most appropriate crowdfunding type for the growth stage. The capital necessary to scale and grow the business is typically high and often unattainable by the donation or lending crowdfunding models. The average funding amount for an equity crowdfunding campaign is higher, making this type more suitable than other models (Sandlund, 2013). At this stage, the venture is able to demonstrate success and can pitch its funding requests to prospective backers with objectively verifiable information, such as financial data or information about its customer base. The risk of failure for the venture is lower than at its beginning and the startup is, in turn, able to offer monetary rewards more credibly. This crowdfunding model fits well at this stage as growth means an opportunity for organizational change and a shift of power. The founder and the business have become reasonably separate; the startup is decentralized and often organized by key functions (Churchill & Lewis, 1983). Thus, the founder is typically more open to the idea of giving up some ownership and control of the business—an inherent requirement of equity crowdfunding—during the growth phase.

5. Best practices on how to attract a crowd and its contributions

As laid out in the previous section, startups are able to identify the most suitable crowdfunding type by considering their specific life cycle stage and resource requirements. Once the choice of crowdfunding type is made, campaign proponents face the next challenge, which is how to attract people and their contributions. Crowdfunding is a transactional relationship between founder and funder. The information asymmetry between these two parties makes this relationship imbalanced and inefficient, likely impeding the outcome (McCarthy, Silvestre, & Kietzmann, 2013). Using cue utilization as a theoretical lens, this section provides practical guidance on how startups can communicate the value of their proposed endeavor to crowd members.

Cue utilization theory (Olson, 1972) posits that, when faced with ambiguity about the quality of an entity (person, product, firm, institution), individuals use surrogate information to make inferences about the entity’s quality (Bahadir, DeKinder, & Kohli, 2014). Firms can influence this assessment process by sending signals or cues that convey the quality desired by the firm. Signals are defined as the information under the direct control of the entity, such as its own published information or certifications to accepted standards. Cues, on the other hand, consist of information that includes signals as well as additional information available through third parties or the general environment. As such, cues are not always directly under the control of the entity. A young firm in an initial public offering (IPO) may staff its board with a diverse group of esteemed directors to convey its legitimacy to investors. This, along with audited and regulated statements that are part of the IPO process, encompasses the signals. If news outlets or social media
picked up on the composition of the board and the past successes of its members, interested parties could receive cues.

5.1. Harnessing cues and signals for donation crowdfunding

5.1.1. Choose a specialized platform and all-or-nothing payout model

The central tenet of donation crowdfunding is that it does not offer tangible rewards to backers. This means the founder needs to communicate the value of the project in nonmonetary terms. Crowd members must be convinced that the cause they are contributing to is worthy of their support. In this context, due to the fact that the venture is in the pre-startup phase, there are few objectively verifiable signals at the founder’s disposal. The choice of platform is one of the strongest, signaling a specialization and addressing a particular crowd that is drawn to the chosen platform. Crowdfunding on Quirky indicates a product focus (e.g., a collapsible yoga mat) and an invitation to participate in the actual development of the product. Using Kickstarter, on the other hand, signals that the project endeavors to contribute toward the social good of society (e.g., a campaign to fund a World Peace and Prayer Day).

In addition, employing the all-or-nothing model signals to a crowd that the startup is committed to the project and will only proceed if the required threshold is met (Cumming, Leboeuf, & Schwienbacher, 2014). In the all-or-nothing (or fixed funding) payout model, the creator only receives funds if the funding goal is met or surpassed during the campaign period (Kickstarter, 2016), while in the keep-what-you-earned (or flexible funding) model, the founder keeps all funds raised. Empirical evidence suggests that campaigns employing the all-or-nothing model are more successful in achieving their funding goal and outperform projects using the flexible funding model with respect to the number of supporters attracted to their campaigns (Kolenda, 2016).

5.1.2. Be transparent and accountable

The second suggested best practice includes a detailed breakdown of what the invested funds will be used for. This reduces the information asymmetry between founders and crowd members by signaling that contributions are indeed making a difference in the project being supported. In the case of pure donation crowdfunding, the necessity of sending a strong signal of accountability has been recognized in scientific literature on charitable giving (Murphy, n.d.). There is a strong consensus that by keeping donors informed about their contribution’s impact, organizations improve their fundraising outcomes (Blackbaud, 2012), especially if they demonstrate that donations go to the core cause rather than toward overhead costs (Prior, 2014). The band Protest the Hero crowdfunded an album via Indiegogo in 2013. Not only did the band include an itemized list of expenses in its pitch, but also members were very explicit about their motivation to do so in their campaign description (Protest the Hero, 2013). The campaign ended with a total of $341,146 raised, exceeding the target by 173%.

5.1.3. Publicize backer information

Another best practice is the publication of supporter details. This practice makes the project appear more relatable (Kolenda, 2016), which has been shown as a success factor in charitable giving and donations (Karlan & List, 2007; Leonhardt, 2008). The charity:water crowdfunding campaign promotes supporters with elaborate editorial content and illustrates the importance of being able to relate. In a prominent example, Rachel Beckwith, a girl from Washington State, set out to raise $300 for charity:water by foregoing gifts for her ninth birthday (Beckwith, 2011). While her initial campaign fell short of her goal, her tragic death in a car accident led to a revival of her campaign that has raised more than $1.2 million to date.

This example also illustrates the opportunity to trigger herd behavior, which is the tendency for individuals to mimic the actions of a larger group (Phung, 2007). Herd behavior may be caused by social pressure of conformity or by the common rationale that it is unlikely such a large group could be wrong. Herd behavior represents an indirectly controllable cue for the startup that is contributing significantly to a crowdfunding campaign’s success. It is estimated that four investors contributing $1 each will trigger another three investors to do the same, for no other reason than having seen others engaged with the project (Estrin & Khavul, 2016).

5.2. Harnessing cues and signals for lending crowdfunding

5.2.1. Offer tangible rewards

Lending crowdfunding requires the startup to signal a reliable ability to compensate an investing crowd. One of the potential reward forms here is monetary interest. This is a slight variation of traditional debt funding where established measures can be brought to bear. The Dutch platform TailWindCrowd, for example, publishes the risk profile score and third-party assessments underlying the fair interest that the founder offers to a crowd (Tailwind Crowd, 2016). The startup founder can use this score and the
associated interest set by the platform to signal the quality of the proposed campaign.

Inherent to the pre-sale model of lending crowdfunding is rewarding crowd members with a tangible product from the project. Pebble has raised record-breaking amounts in both of its product releases by offering pre-sales of smartwatches that were still in the development stages (Dredge, 2015). The reward to the crowd was twofold: (1) assured and preferred access—the first 100 funders contributing $235 or more were guaranteed working prototypes, and (2) a discounted price—anyone contributing $115 was assured a production watch, which compared favorably with the $150 market price tag (Pape & Imbesi, 2014). The extra incentive for early backers was a signal intended to trigger the herd effect mentioned earlier.

5.2.2. Detail the startup founder’s credentials
The second best practice for lending crowdfunding is the publication of details regarding the founder’s background. A funding crowd is not only investing in a product or an idea, but also in the person who is shepherding this idea from the pre-startup phase to success. With proper educational credentials and a successful track record, founders prove their competency. This increases the probability of funding success and is common with more-traditional venture capital funding (Hsu, 2007). This best practice has been widely employed by successful crowdfunding campaigns in ways that are appropriate for their circumstances—ranging from the board members publicized by Elio Motors (2016) as an “impressive roster of industry icons” in their quest to build an affordable, fuel efficient vehicle to the decades of beekeeping experience of the Flow Hive team (Anderson, 2015).

5.2.3. Frequently update a funding crowd
The third best practice involves frequent updates and communication with a funding crowd. One of the key learnings that the founder of the successful Goldieblox campaign remarks on in her final update on Kickstarter is that members of a funding crowd “deserve to hear from us more” (Sterling, 2013). Goldieblox had developed The Engineering Toy for Girls and received funding from many backers who were promised the finished product. When delays occurred, communication to supporters was a key tool used to ensure that the support base remained committed to the project. Comments posted to Goldieblox’s updates indicate that the transparency and accountability were viewed positively, or at least as mitigating factors in negative experiences, thus helping keep the crucial cues of the online community engaged and supporting the project.

5.3. Harnessing cues and signals for equity crowdfunding

5.3.1. Provide third-party verifiable reports
The first best practice for equity crowdfunding is the use of third-party verifiable information. Regulatory requirements for equity crowdfunding, such as implementation guidelines for the U.S. JOBS Act and regulations in Canada, mandate different levels of financial disclosure for companies of different sizes (Rose, 2012; Thompson, 2016). The release of financial and other information reduces information asymmetry between the startup and investors. Startups should be careful, though, not to limit the signals to the government-mandated minimum disclosure standards. Verifiable and digestible information on the company and its key projects has been identified as a contributing factor to equity crowdfunding success (Millard, 2016). One example of success is Mouth (https://angel.co/mouth), an online store for U.S.-made indie food and spirits, which raised $1.1 million in equity funding. It proactively informed supporters of its vision, strategies, team, and even product to clarify its value proposition and mitigate perceived risks for potential investors.

5.3.2. Attract reputable early investors
Incidentally, Mouth has also employed the second best practice that sends a strong signal to potential investors. By publishing data on early, reputable investors, startups benefit from the information cascading to subsequent potential investors. The equity crowdfunding platform Crowdfunder has embraced this idea so thoroughly that it displays a featured investor on the homepage for each campaign. Furthermore, some campaigns provide significantly more information in investor profiles than in the biographies of the startup team. Digitzs, for example, is a facilitator of payment processing for e-commerce companies and its campaign was underway at the time of this writing. Investors are listed with varying levels of detail, but prominent investors, like Kevin Harrington from the ABC show Shark Tank, get visible placement with short biographies detailing their experience (Crowdfunder, n.d.).

5.3.3. Target a crowd that can empathize
The third best practice for equity crowdfunding is to target a crowd that can empathize with the founder’s network, geographical proximity, or business aim. A founder’s individual social capital—their personal and business network—has shown to correlate positively with success in a crowdfunding campaign (Giudici et al., 2013). This finding was supported by a study of approximately 48,500 projects, which found that geographic proximity to the
founder is positively linked to venture capital funding (Mollick, 2014). The closeness to the aim of the project can be seen in a number of ventures that target a specific crowd, such as Farm Hill, a delivery service for healthy lunch food operating in the Silicon Valley area. It raised $1 million in equity crowdfunding, with a number of the investors identified as ‘foodies’ or previous investors in similar ventures (Farm Hill, n.d.). Another example is Plum (2015), which developed a wi-fi-enabled smart light switch and drew funders who had extensive previous experience in successful smart home networking companies. Plum exceeded its $5 million equity crowdfunding goal.

5.4. Best practices mini-summary

In summary, a startup should develop, maintain, and use its personal and professional networks extensively in the lead up to and during an equity crowdfunding campaign. This contributes positively to one of the key success factors for a crowdfunding campaign: achieving and sustaining momentum behind the campaign, especially in the early post-launch days. Evidence shows that once a campaign hits 30% of its funding goal the success rate climbs to 90%, compared to only 50% after a campaign reaches the 5% mark. And the faster the momentum is gained the better; campaigns that reach the 30% mark within the first week are more likely to achieve their funding goals (Canada Media Fund, 2016).

6. Final thoughts on crowdfunding for startups

This article offers contributions to both the practitioner and research communities. For startups, it demonstrates that crowdfunding can generate a valuable organizational resource base, primarily through the acquisition of funds, but also through nonmonetary resources in the form of learning, the formation of crowd capital, and marketing (Brown et al., 2017; McCarthy et al., 2013; Prpić et al., 2015). But not all crowdfunding types are equally suited to support the various resource requirements in different life cycle stages, and neither are all crowdfunding types, a feasible option. When choosing among the different crowdfunding types, a startup needs to consider its specific lifecycle stage, along with intended crowdfunding benefits like resource provision and constraints in terms of the type of reward it is able to offer credibly. This article provides a framework to guide startup decisions in this context, which is illustrated in Figure 1.

In the pre-startup phase, organizational resources focus on validating the idea and a crowd provides

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**Figure 1. Framework for startup crowdfunding**

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<th>Growth</th>
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<td>Market Validation</td>
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<td>Verifiability of Information</td>
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<td>Optimal Type of Crowdfunding</td>
<td>Donation</td>
<td>Lending</td>
<td>Equity</td>
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<td>Reward Offered</td>
<td>No (tangible) return</td>
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<td>Securities, Profit Sharing</td>
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<td>Best Practices</td>
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valuable resources through funding and feedback on a proposed solution. Ventures in this stage neither have a developed product to offer as a reward, nor are they able to offer financial or equity-like returns; donation crowdfunding is optimal to meet their resource needs within these constraints. Similarly, resources in the growth stage are required to market the offering and scale the venture’s operations. Equity crowdfunding is best suited to meet the higher capital needs in this phase, in addition to providing critical nonmonetary resources in the form of product promotion, sales, and marketing.

Once a choice on the type of crowdfunding is made, startups face the next problem: how to convince potential backers to fund their venture. As a solution, this article offers a number of best practices as guidelines that have been shown to have a measurable effect on the success rates of crowdfunding initiatives and are likely to prove valuable for startups (see Figure 1). This leads to another key finding. The circumstances for different crowdfunding endeavors are so diverse that it can be argued that each crowd has to be constructed and addressed in a unique way. Cue utilization theory, an established theory in social sciences, has provided a valuable theoretical lens in this context. Each startup life cycle stage is characterized by different types and levels of information asymmetry between a founder and crowd members. Cues and signals can help reduce the information asymmetry between the two parties and make the outcome more efficient for both.

The findings of this article prompt possible future research. One example would be to dig deeper into the recommendations by empirically validating the proposed best practices. While this article has mainly focused on for-profit startups, this work may also spark research in the field of social enterprise, such as an investigation into the differences between startups with purely for-profit aims and startups focusing on a double-bottom line. In conclusion, I hope that this article convinces startups and scholars that crowdfunding can play a significant role in creating a critical resource base.

References


