CROWDINVESTOR INVESTMENT DECISION-MAKING
A STUDY OF MOTIVATION, INVESTMENT PROCESS AND CRITERIA
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<tr>
<td>ASSOB</td>
<td>Australian Small Scale Offering Board</td>
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<tr>
<td>BA</td>
<td>Business Angel</td>
</tr>
<tr>
<td>BaFin</td>
<td>Bundesanstalt für Finanzdienstleistungsaufsicht</td>
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<tr>
<td>CAGR</td>
<td>Compound Annual Growth Rate</td>
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<td>CAPEX</td>
<td>Capital Expenditure</td>
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<td>CEO</td>
<td>Chief Executive Officer</td>
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<td>CF</td>
<td>Crowdfunding</td>
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<td>COO</td>
<td>Chief Operation Officer</td>
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<td>EUR</td>
<td>EURO</td>
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<tr>
<td>EIS</td>
<td>Enterprise Investment Scheme</td>
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<td>FF</td>
<td>Family, Friends and ‘Fools’</td>
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<td>GBP</td>
<td>British Pound</td>
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<td>IPO</td>
<td>Initial Public Offering</td>
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<tr>
<td>IRR</td>
<td>Internal Rate of Return</td>
</tr>
<tr>
<td>JOBS Act</td>
<td>Jumpstart Our Business Start-ups Act</td>
</tr>
<tr>
<td>MBA</td>
<td>Master of Business Administration</td>
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<tr>
<td>OECD</td>
<td>Organisation for Economic Co-operation and Development</td>
</tr>
<tr>
<td>P&amp;L</td>
<td>Profit &amp; Loss</td>
</tr>
<tr>
<td>PV</td>
<td>Photovoltaic</td>
</tr>
<tr>
<td>ROI</td>
<td>Return On Investment</td>
</tr>
<tr>
<td>SEC</td>
<td>Securities and Exchange Commission</td>
</tr>
<tr>
<td>SEIS</td>
<td>Small Enterprise Investment Scheme</td>
</tr>
<tr>
<td>SEK</td>
<td>Swedish Krona</td>
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<tr>
<td>SME</td>
<td>Small and Medium-sized Enterprises</td>
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<td>UK</td>
<td>United Kingdom</td>
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<tr>
<td>USD</td>
<td>United States Dollar</td>
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<tr>
<td>USP</td>
<td>Unique-selling Proposition</td>
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<td>VC</td>
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Abstract
Crowdinvesting is a new source of entrepreneurial finance allowing the broad public to invest money into start-ups in exchange for an equity stake in the venture. As a consequence crowdinvesting is said to democratize start-up financing. While crowdinvesting as a financing vehicle for early-stage ventures is gaining momentum little remains known about the crowdinvestor who, if not classified as accredited investor, was previously excluded from investing in unlisted companies. This study is an initial attempt to investigate crowdinvestors’ motives and investment decision-making criteria inspired by previous research on business angels. For this purpose a total of twenty interviews were conducted with crowdinvestors from three different platforms: Seedmatch, FundedByMe and Seedrs. All interviews were conducted, transcribed and analysed in March and April 2014.

In the first part of this thesis the concept of crowdinvesting is placed in its broader thematic context of crowdsourcing and crowdfunding. Subsequently, relevant background knowledge on the crowdinvesting process and ecosystem are presented, before moving into the theoretical background on business angel investment decision-making process and criteria as well as motivational aspects. Hereafter, research findings are presented in the analysis chapter followed by a discussion of possible implications of our results.

Our results suggest that crowdinvestors in some characteristics resemble business angels. This is not only true in terms of motivational considerations, but also in crowdinvestors' decision-making criteria. However, we perceive structural differences, i.e. size, stage and context of the investment, as too significant to misconceive crowdinvestors as business angels. Overall, our findings suggest that crowdinvestors are well informed about the risk involved when investing in early-stage ventures. We imply crowdinvestors make conscientious investment choices.

Keywords: Entrepreneurial finance, business angel, investment decision-making, crowdinvestor, crowdinvesting, equity-based crowdfunding, crowdfunding.
1 INTRODUCTION

Entrepreneurship is recognised globally to be a key source of innovation and dynamism in advanced industrialised countries, as well as in emerging and developing economies. Start-ups and small or medium sized companies (SMEs) are responsible for most net job creation in OECD countries and make important contributions to innovation, productivity and economic growth (OECD, 2010). Access to capital and investment is an integral part of translating innovative ideas into sustainable businesses. Despite the clear evidence of their importance for economic prosperity it is widely recognized that entrepreneurs face difficulties in attracting external finance at the early stages of the entrepreneurial lifecycle.

Seed investments are characterized by high risk and are likely to take many years before generating a return to their investors. Additionally, valuation of these businesses is very difficult due to the lack of traction and uncertainty about future cash flows. Therefore, most formal investors, such as venture capital (VCs)\(^1\) firms, are unwilling to make equity investments at the pre-/ seed stage and focus their attention on later-stage ventures with a proven business model. Even business angels (BAs)\(^2\) have reduced their investment activity at the seed stage (Ernst & Young, 2012). According to recent data around 35 per cent of business angel investments were allocated to companies at the pre-/seed stage in 2013, down by 20 per cent from the pre-crisis peak in 2008 (CVR, 2013). Thus, pre-seed and seed financing is mostly provided by the entrepreneurs’ own savings, bootstrapping and the close network of family and friends (Bhidé, 1992; Winborg & Landstrom, 2001; Ebben & Johnson, 2006).

Faced by these constraints an ever increasing number of entrepreneurs is taking advantage of the Internet to obtain financial help directly from large communities of individuals – dubbed as the crowd (Kleemann et al., 2008; Belleflamme & Schwienbacher, 2012b). On the very basis, this new concept, called crowdfunding, involves tapping a large dispersed audience of investors for small sums of money that on an aggregate help to fund a project or a venture. Crowdfunding is typically empowered by the web 2.0 revolutions and the continuing emancipation of the crowd (Lehner, 2013; Reyes & Finken, 2012; Drury & Stott, 2011; Brabham, 2008).

\(^1\) Hereafter venture capital will be referred to as VC.
\(^2\) Hereafter business angel will be referred to as BA.
While in the past transaction costs made it unlikely that investments of such small amounts would be available to the general public, the Internet and crowdinvesting now provide the opportunity to accomplish this (Friedman, 2005; Belleflamme & Schwienbacher, 2012b).

With the introduction of the first platforms in Europe in 2012 crowdinvesting has increasingly gained momentum in the public domain. In brief, crowdinvesting allows start-ups and small businesses to raise capital from their immediate and extended social networks, and at the same time, offers small investors the chance to purchase an equity stake in the business. As a consequence, crowdinvesting has become a viable alternative form of entrepreneurial finance by addressing the funding gap from initial to later stage funding, otherwise known as the “valley of death” (see Figure 1). In the US, President Obama has termed crowdinvesting as a potential game changer by democratizing the sphere of entrepreneurial finance (New York Times, 2012).

Although crowdinvesting markets are nascent, the concept itself is not broadly understood due to a lack of scientific research on the subject matter. Thus, discussions about its applicability and potential often strand in “uninformed narratives that contribute limited value to broadening the understanding of the underlying mechanisms” (Massolution, 2013). A consistent feature in the on-going discussion amongst different stakeholders has been a persistent call for informed regulation and design of crowdinvesting markets, which is a necessary effort to ensure the protection of crowdinvestors and entrepreneurs, as well as to enhance the efficiency and sustainability of the industry. However, while the formulation of policy and regulation surrounding crowdinvesting is beginning to garner greater attention, many aspects of crowdinvesting have yet to receive rigorous examination (Moritz & Block, 2013; Ahlers et al., 2013).

Two of these aspects pertain to the crowd more directly. Firstly, the investment behaviour of crowdinvestors is not yet well understood and secondly, the motives of the crowd to invest in start-ups remain ambiguous (Ahlers et al. 2013; Hagedorn & Pinkwart, 2013; Hornuf & Schwienbacher, 2014). Academic research broadening the understanding of the motives and investment behaviour of crowdinvestors is crucial to design effective ecosystems. Novel insights on this subject will have implications for platform operators, entrepreneurs, and legislators as well as crowdinvestors.
1.1 Thesis Structure

This thesis is composed of ten chapters, beginning with the introduction to the phenomenon of crowdinvesting and problems related to limited academic knowledge on the subject matter in **chapter one**. The **second chapter** presents our literature review of previous academic research on crowdfunding and crowdinvesting and concludes by highlighting the current research gap, which has been pointed out by several researchers. The problem statement presented in **chapter three** is inspired by the research gap illuminated in the literature review. By answering this problem statement we aim to contribute to the existing literature with insights on the crowdinvestors motivation, decision-making process and criteria. Following the problem statement, **chapter four** introduces our methodological considerations, which resulted in the choice of a qualitative approach in the form of semi-structured interviews. Additionally, the chapter accounts for the selection of theory, data collection, data analysis and validity.

**Chapter five** familiarizes the reader with the antecedents of crowdinvesting, namely crowdsourcing and crowdfunding. Following, **chapter six** provides a comprehensive overview of research on BA investment decision-making process and criteria as well as motivational aspects. By using BA theory we build the foundation for our subsequent analysis. **Chapter seven** is dedicated to the first part of our analysis and presents insights on crowdinvestors’ demographics and motives, distinguished in financial and non-financial. The second part of our analysis in **chapter eight** offers in-depth insights on crowdinvestors’ decision-making process and criteria. This chapter’s structure follows the different stages of the process and presents our findings on a diverse set of investment criteria.

Subsequently, **chapter nine** provides a reflection on our research results in comparison to BA research by asking: Are crowdinvestors small BAs? Furthermore, we operationalize our insights by placing them in the context of earlier research and by drawing implications for the crowdinvesting ecosystem. We finish this thesis off in **chapter ten** by concluding on our findings and the problem statement. The final remark is assigned to recommendations for future areas of research.
2 LITERATURE REVIEW

Our Literature review focuses on existing literature in crowdfunding and crowdinvesting to actualise the terms and to present earlier research on the subjects. Further our aim with the literature review is to establish additional awareness of the research gap pointed out by Ahlers et al. (2013), Hagedorn and Pinkwart (2013), as well as Hornuf and Schwienbacher (2014). A crucial stepping-stone to the identification of a relevant and understudied research area within an existing topic is to map the current state of academic work on the subject (Stebbins, 2001). In a primary step academic papers on crowdfunding were collected via relevant search instruments, including ResearchGate, Google scholar and Ebsco by applying keywords such as crowdfunding, crowdsourcing and crowdinvesting. The initial screenings of the catalogues lead to the identification of the most popular articles on the subject. In a subsequent step, bibliographies of these articles were explored to identify additional studies. After ensuring their relevance for this thesis we included them in the literature review. Excluded from this review were academic papers focussing solely on the areas of either donation- or lending-based crowdfunding. Bachelor and Master Thesis as well as term papers were also not considered as part of this study. Caused by the novelty of the subject academic papers are scarce and little work has been published to date. Some of the papers are still work-in-progress or are available for peer review by the scientific community. In short, this important and growing area of entrepreneurial and governmental activity is lacking fundamental research, even as both practice and policy continue to evolve quickly (Mollick, 2013).

2.1 Research on Crowdfunding

The first academic studies on crowdfunding mainly followed a ‘phenomenon-based approach’, by providing a definition, description and delimitation of crowdfunding from related topics and concepts, often with the help of case studies (Schwienbacher & Larralde, 2010; Belleflamme et al. 2012a; 2012b; Hemer, 2011; Mitra, 2012). The use of crowdfunding to fund entrepreneurial or project-based businesses started to engage academic interest in 2010. The widely adopted definition of the crowdfunding term is coined by contributions of Belleflamme et al. (2012a) and Schwienbacher and Larralde (2012). In many of the first studies market data is compiled and combined with qualitative data gathered through interviews (Aitamurto, 2011; Hemer et al., 2011; Röthler & Wenzlaff, 2011). Academic papers focussing on the analysis of empirical data began to emerge when crowdfunding platforms,
which are the intermediaries between entrepreneurs and investors, were more established in the market by facilitating sufficient transaction volumes.

Within the collected literature on crowdfunding many authors tend to focus on the role and motivations of backers or investors in crowdfunding (Mollick, 2013). Gerber and Hui (2012) and Gerber et al. (2014) study the motivation and deterrents to participation of investors in crowdfunding markets by conducting a total of 87 one-to-one semi-structured interviews. Their findings suggest that investor motivations include the desire to collect rewards, to help others, to support good causes and to be part of a community. Belleflamme et al. (2012a) also highlight the importance of building a community experience to make crowdfunding a viable alternative to traditional investors and Agrawal et al. (2013:15) state investors “derive consumption value from the feeling of being part of the entrepreneurial initiative and among a select group of early adopters”. In addition, a brief interview study by the Australian Council of the Arts reveals that backers pledge because they expect to be recognized as an early identifier of a cool product within their social network, which they termed as social kudos (Klaebe, 2012).

Furthermore, Gerber et al. (2014) and Agrawal et al. (2013) find that distrust in the entrepreneur’s use of funds or fraud, the concerns about waiting for or not receiving rewards caused by the entrepreneurs incompetence, and the general project risk involved are strong deterrents to solicit resources and contribute. Insights from Mollick (2013) connote that these concerns are not ungrounded. His spot check of 247 Kickstarter projects states that over 50 per cent failed to deliver the promised product on time, with the average delay being 2.5 month. This finding is supported by a recent experimental study conducted by Wash and Salomon (2014) on the pledging behaviour of investors compared between two different operational models: the return rule and the direct donation\(^3\). The results suggest that under the return rule backers are more willing to contribute money to projects, and in particular high-risk projects, leading to an overall increase in pledges, which may be driven by the investors’ concern that the entrepreneur may not be capable of delivering the promised result if the funding target is not achieved.

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\(^3\) Some crowdfunding sites operate under an all-or-nothing return rule in which donations are returned to donors if the project doesn’t meet its goal. Other sites use a direct donation structure where the project owner keeps all donations even if the total funding remains below the target (Wash & Salomon, 2014).
Consequently, the results support previous studies indicating that investors in crowdfunding are not solely motivated by the prospect of financial returns. Factors such as social reputation and intrinsic motives play a central role depending on the context in which the fundraising takes place (Belleflamme et al., 2012c; Ordanini et al., 2011). Ordanini et al. (2011) identified common characteristics of investors from three crowdfunding platforms operating with differing business models: Investors enjoy engaging in innovative behaviour, they show a high level of identification with the entrepreneur or the product, they are interested in a financial return and like to engage in a community of like-minded individuals. Additionally, Hemer et al. (2011) show that investors are motivated by a personal need for the product or service being offered and to attain self-affirmation and joy. Not surprisingly, these findings imply that motivational factors involved in crowdfunding are similar to motives identified in the context of crowdsourcing (Füller, 2010).

In his study of the impact of crowdfunding on journalism, Aitamurto (2011) discovers that the act of participating in crowdfunding seems to be more important than the actual journalistic product. The reasons for contributing to a pitch are more altruistic than instrumental in nature: rather than getting a good story to read, the backer pledges for a common societal goal, which is a democratically healthy society. This may not be surprising since online journalism is a form of public good. Burtch et al. (2012) conducted a related study on crowdfunding in the context of online journalism identifying the predominant influences in this marketplace: altruism and warm-glow.

Giudici et al. (2012) come to the conclusion that at the moment crowdfunding has mainly a social and emotional value. People who are familiar with the Internet may choose to fund an entrepreneurial project if the amount of money to be invested is negligible, the project has a strong emotional appeal or if the returns create an exclusive non-monetary benefit enhancing the social and emotional nature of the deal.

All these studies on the motivation of investors in crowdfunding offer valuable contributions to a better understanding of the underlying mechanism of crowdfunding success, but they fail to provide more actionable insights into the signals that trigger investments. The studies presented in the following paragraph encompass the first attempts of academia to shed light on this area.
One of the first working papers investigating a specific factor of crowdfunding is a study by Agrawal et al. (2011) on the geography of crowdfunding in the setting of financing musical projects. Their goal is to understand whether crowdfunding relaxes geographic constraints on fundraising that are characteristic for investments by VCs and BAs (Mollick, 2013). The results imply a reduced role of spatial proximity between entrepreneurs and investors in the context of funding creative work. The data indicates an average distance of 3,000 miles between artists and investors. Distance, however, still plays a role – within a single round of financing, local investors invest relatively early and appear to be less responsive to decisions by others. The authors show that investors with a personal connection to the entrepreneur – defined as family and friends – drive this geography effect (Agrawal et al., 2011). The findings are consistent with prior research on online activity showing many, but not all, distance-related frictions are reduced in an online setting (Blum & Goldfarb, 2006; Hortacsu et al., 2009). Furthermore the results emphasize the important role of family and friends in generating early investments in entrepreneurial ventures. In alignment with Conti et al. (2011) this may indicate early investments to serve as a signal of entrepreneurial commitment prompting later investors to supply additional resources.

Building on these findings Mollick (2013) studied a data sample of 2,101 high-technology projects from Kickstarter to understand the decision-making processes of what he calls amateur investors. He argues that although amateurs and the experts (VCs) differ in many ways, they are ultimately assessing whether early stage entrepreneurial ventures have the ability to succeed at their goals by looking at signals of quality. Despite the radical differences in selection environments, the outcome shows that both VCs and amateur investors assess entrepreneurial quality in similar ways. The insights imply that entrepreneurs with past evidence of success are more likely to successfully run a crowdfunding campaign and that outside endorsements significantly increase the chance of being supported by the crowd. Additionally, entrepreneurs signalling a high level of preparedness by having a working prototype ready and/or a quality video presentation tend to be more successful in raising capital. From this perspective, funders act like VCs and evaluate the quality of the product, the team and the likelihood of success (Mason, 2008; Hall & Hofer, 1993). Finally, the results suggest crowdfunding to be a more democratically distributed source of capital compared to traditional sources of funding by avoiding some of the biases that are pervasive in VC selection, namely gender and geographic biases.
Lastly, Kim and Viswanathan (2013) examine the role of experts in online crowdfunding markets, particularly the influence of early investors on later investors, based on data derived from a crowdfunding market for mobile applications. Contrary to popular perceptions of crowdfunding markets as means for democratizing expertise and as substitutes for traditional expert-driven mechanisms, their findings reveal that despite the choice provided by these crowd-based markets, the crowd’s decisions are strongly influenced by experts participating in these markets. Concluding, early investments by experts serve as credible quality signals for later investors, especially for those who are less experienced.

Despite providing valuable insights into the motivations and investment decision making criteria of investors in the setting of non-equity based crowdfunding models, it is important to keep in mind the structural differences between non-equity and equity-based crowdfunding (see Chapter 5.2.1). In general, the most critical distinction is grounded on the amplification of information asymmetries. Whereas the asymmetry problem currently concerns the feasibility of and the creator's ability to deliver the product, in the equity setting the asymmetry problem includes the above as well as the creator's ability to generate equity value by building a company rather than just delivering a product. In the absence of strict governance, reporting, accounting, and other requirements common in publicly traded securities markets, crowdinvestors are subject to an unusually high degree of risk (Agrawal et al., 2013). Although Agrawal et al. (2013) notice the applicability of findings from earlier studies to the context of crowdinvesting, it is important to bear in mind potential limitations. To date, studies dealing solely with crowdinvesting are still scarce. In the next part of this thesis we will present the findings of the few studies currently available.

2.2 Research on Crowdinvesting

As a succeeding phenomenon originating from crowdfunding, crowdinvesting is portrayed as a more serious form of entrepreneurial engagement than reward-based crowdfunding. While some basic commonalities exist, the two terms have differences, which has inspired two distinct research areas.

Similar to the evolution of studies considering crowdfunding in general, the first academic attempts to grasp the infant market of crowdinvesting are providing a broad introduction to the topic and a discussion on its relevance for entrepreneurial finance. The delimitation of crowdinvesting to traditional sources of risk capital, particularly VCs and BAs, is a common theme within the selected literature (Mäschle, 2012; Kortleben & Vollmer, 2012; Agrawal et
Besides, several authors focus their attention on the legal aspects of crowdinvesting driven by the long lasting public debate on whether crowdinvesting should be legalized or not in the US and followed by the recent implementation of the JOBS Act in 2013 (Klöhn & Hornuf, 2012; Griffin, 2012; Cohn, 2012; Fink, 2012; Hazen, 2012).

Kortleben and Vollmer (2012) deliver one of the most compelling introductions to the field of crowdinvesting and its relevance for entrepreneurial finance by comparing its mechanisms with alternative forms of risk capital. In alignment with other studies, the authors’ position crowdinvesting as an intermediary source of capital bridging the gap from funding provided by family and friends to traditional sources of risk capital, such as BAs and VCs (see Figure 1). Moreover, they discuss the crowdinvesting investment process to the well-studied stage process applied by VCs (Maxwell et al., 2011; Paul et al., 2007; Fried & Hisrich, 1994; Wells, 1974). Kortleben and Vollmer (2012) highlight the problem of information asymmetries between entrepreneur and investor(s) and consequent need of due diligence to reduce risk.

With their working paper on the German crowdinvesting market, Hagedorn & Pinkwart (2013) provided an equivalent introduction to crowdinvesting.

In his working paper on the information disclosure policy of German crowdinvesting platforms, Mäschle (2012) argues that current policy is not optimal in the presence of competition among platforms. As part of the solution to solve the information disclosure problem, he proposes a three-staged theoretical model to demonstrate that increasing competition among platforms should enforce a race-to-the-top strategy for disclosure requirements. Additionally, a list of information to be disclosed to the investor community by the entrepreneur are identified due to their empirically verified effect on the risk-return-profile of a company. Featured on this list are among others: balance sheet data to allow for an assessment of the financial standing, detailed information on the firm’s human capital such as education and working experience of the entrepreneurial team as well as firm specific characteristics such as the company’s size, legal form, industry- and ownership structure (see Appendix 4).

Another noteworthy contribution to a deepened understanding of crowdinvesting is Ahlers et al. (2013) work that can be regarded as the first attempt to empirically examine factors

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4 Hazen (2012) argues that it does not make sense to sacrifice investor protection simply because there are dollar limits on the investments solicited via crowdfunding. The new crowdfunding exemption as implemented by the SEC has to provide sufficiently meaningful disclosure to protect investors.
affecting success of projects in the context of crowdinvesting. Their analysis is based on a sample of 104 offerings taken from ASSOB, an Australian crowdinvesting platform operating since 2006 and investigates the impact of a firm’s financial roadmap (pre-planned IPOs or acquisitions), human capital (networks, board structure), venture risk (awards, government grants and patents), and level of uncertainty (amount of equity offered, retaining equity and financial forecasts) on fundraising success. The analysis shows that entrepreneurs retaining equity and providing extensive information about risks can be interpreted as effective signals. Statistically, these variables have the strongest impact on funding success and raising capital over a shorter time period. Companies that, prior to seeking crowdinvesting, have been in business longer are also more likely to raise the desired level of capital more quickly. Furthermore, companies with more board members, higher levels of education (as measured by the percentage of board members holding an MBA degree), and better networks, which are interpreted as positive attributes of quality, are more likely to attract a higher number of investors. Interestingly, variables such as the presence of a financial roadmap including the type of proposed exit channel have at most a limited impact on funding success. These may be regarded as “cheap talk” by investors, because the statements are not legally binding (Ahlers et al., 2013). Finally, Agrawal et al. (2013) point out that access to investment opportunities is a key incentive for investors to engage in crowdinvesting.

Our literature review on crowdfunding in general and crowdinvesting in particular, reveals that whilst a growing stream of academic literature has been published since 2010 many important aspects of crowdfunding require further studies to explore the dynamic factors shaping the crowdfunding ecosystem. More particularly several authors emphasized the need for additional studies investigating the motivations and investment decision-making criteria of investors in the quickly evolving market of crowdinvesting (Hagedorn & Pinkwart, 2013; Moritz & Block, 2013; Kortleben & Vollmer, 2013; Ahlers et al., 2013). We must learn more about the investor in order to find good solutions to support entrepreneurs and investors in saving their interests (Hagedorn & Pinkwart, 2013). Kortleben and Vollmer (2013) raise questions regarding the selection criteria of investors in crowdinvesting. Do these investors apply similar investment criteria as traditional investors or do gut-feeling and/or emotional aspects in the pitch trigger their investments? Additionally they regard a systematic analysis of investors’ demographics as an essential step towards efficiently designed crowdinvesting ecosystems.
Moritz and Block (2013) conclude that the study of crowdinvestors’ investment criteria remains incomplete. The authors inspire research based on VC decision-making criteria to provide rudiments of whether these “inexperienced” investors apply similar criteria as sophisticated investors. If the crowd applies these rational investment criteria or if the investment decision is rather driven by emotional aspects, herding behaviour or altruistic motives, has yet to be explored.

3 PROBLEM STATEMENT

While crowdinvesting as a new phenomenon in entrepreneurial finance has increasingly received attention from media as well as academic research, our literature review indicates a significant research gap exists for studies on crowdinvestors’ motivation as well as investment decision-making criteria and process. Hagedorn and Pinkwart (2013), Moritz and Block (2013) as well as Ahlers et al. (2013) illuminate this gap by calling for more research on these aspects. This sparked our interest to explore the field within our thesis by following the tradition of exploratory studies of new phenomena within entrepreneurship (Rice, 2002; Roure & Maidique, 1986; Tan et al., 2013; Zahra, 1991). We aim to contribute fundamental exploratory research on crowdinvesting to bridge the identified research gap and to provide practical insights on crowdinvestors and their investment decision-making, by asking:

**How are crowdinvestors informing their investment decision?**

To answer this question adequately several related sub-questions must be considered. Thus, in addition to our primary research question we set out to explore:

3.1 Guiding Questions

1. Who are the crowdinvestors?
2. What motivates crowdinvestors to participate?
3. How is the investment process structured?
4. How are crowdinvestors using information provided in the campaign?

3.2 Significance of Research

To our best knowledge this study can be considered the first of its kind and insights gathered by exploring the before stated research questions will be valuable to different actors in the
crowdinvesting ecosystem. A broadened understanding of crowdinvestors, their motives and especially their investment decision-making is crucial in designing efficient crowdinvesting ecosystems. The benefits for the different actors in the ecosystem can be summarized as follows:

Platform operators: Understanding crowdinvestors’ motivation and investment behaviour will allow platform operators to design effective investment infrastructures and to attract new investors.

Entrepreneurs: This study is particularly interesting for entrepreneurs considering crowdinvesting as a means to raise funding for their start-up. Comprehending crowdinvestors’ motives and decision-making criteria will support entrepreneurs in creating compelling and interesting investment proposals.

Legislators: Traditionally, the concern of legislation is to protect entrepreneurs and especially investors. New insights on how crowdinvestors inform their investment decisions are important to draft and implement suitable legislation.

Crowdinvestors: Finally, understanding how peers inform their investment decision can be useful for crowdinvestors in making well-informed investment choices.

3.3 Terms and Definitions

As a clarification to the problem statement and our research intentions, we will shortly define our understanding of the terms: crowdinvestor, informing and investment decision.

We define crowdinvestor as an individual, who acts alone or in an informal syndicate and invests his or her own money via a crowdinvesting platform into an unquoted business where there is no family or friend connection.

Informing is defined as the degree to which the crowdinvestor utilizes available information to make his investment decision.

We understand investment decision as a process that entails several steps, from screening the opportunities to the actual investment (see Chapter 8.1).
4 METHODOLOGY

The methodology chapter commences with a brief review of earlier research methods in entrepreneurial finance. These methods include questionnaires, statistical data analysis, and verbal protocol analysis. Following this review we decided to conduct a qualitative study based on semi-structured interviews as the method for data collection. Further the methodology chapter will present our data collection and analysis, and finally discuss the thesis’ validity.

4.1 Research Methods in Entrepreneurial Finance

Traditionally, research in VCs and BAs has often adopted a quantitative approach based on questionnaires (see Appendix 2 & 3). These studies attempt to test the prevalence of certain investment criteria found in earlier studies. Quantitative research and statistical evidence are often considered a scientific requirement for generalizations (Silverman, 2006). However, research on BAs is often constrained by limitations in generalizing findings. The informal nature of the BA networks is a problem making it difficult to locate BAs and to obtain representative samples (Wetzel, 1981; Mason, 2008). This and other limitations have inspired researchers to state their criticism of the popularity of questionnaires in BA research.

Landström (1998) states that research based on questionnaires reflects “desirable” criteria rather than “true” criteria used. Further, he points out that respondents tend to overestimate the significance of the different decision-making criteria and if the respondent does not have a clear understanding of decision-making model, the results of the analyses are often of limited value. Shepherd and Zacharakis (1999) add to this view by critiquing the use of post-hoc methods such as questionnaires, surveys and interviews. Their criticism of post-hoc methods inspires Mason and Stark (2004) to undertake a verbal protocol analysis, which overcomes the bias of post-hoc methods. Verbal protocols are real-time experiments where the interviewee “thinks aloud” while examining an investment proposal. Using verbal protocol analysis, interviewees are not required to introspect, which removes recall and post-hoc rationalization biases (Sandberg et al. 1988). The method is also used by Hall & Hofer (1993). Nonetheless, verbal protocol analysis has its unique limitations, as it is based on a simulated scenario created by the researcher (Hall & Hofer, 1993). Additionally, the method is preoccupied with counting “thought units”, e.g. how many times a certain thought is articulated. Yet, thought units are not necessarily an indicator of the factor’s importance on in the decision (Zacharakis & Meyer, 1995). Riquelme and Rickards (1992) point out that
subjectivity is involved in coding, analyzing and interpreting verbal protocol transcripts. Finally, some respondents may be uncomfortable about thinking and speaking out loud, which may distort thoughts or the way they are presented (Shepherd & Zacharakis, 1999). Due to the potential bias of generating and interpreting verbal protocols, Ericsson and Simon (1985) suggest that observation is an integral part of verbal protocol analysis, which is only guaranteed if the researcher is face-to-face with the interviewee.

The online nature of crowdfunding has allowed for a new type of method in entrepreneurial research based on the use of online analytics and the platforms’ own data management systems. Our literature review (see Appendix 1) reveals that the majority of current crowdfunding research is of quantitative nature working with statistical data derived from crowdfunding platforms and funding campaigns (Ahlers et al., 2013; Bayus & Kuppuswamy, 2013; Giudici et al. 2013; Mollick, 2013). These studies help to build a general understanding of metrics in crowdfunding, but are limited in providing in-depth knowledge about crowdfunders’ motives and investment decision-making. Ahlers et al. (2013) use a data set of 104 crowdinvesting opportunities from the crowdinvesting platform ASSOB. While the study points out common features of successful and unsuccessful crowdinvesting campaigns, the authors note that the method is limited in the discovery of insights on crowdfunders as individuals, including their motivation and investment decision.

Only a few crowdfunding studies apply qualitative methods (see Appendix 1). Ordanini et al. (2011) employ a grounded theory approach performing an in-depth qualitative analysis of three cases involving crowd-funding initiatives. They argue that given the novelty of the phenomenon, employing a qualitative approach facilitates the exploration of a phenomenon within its context. The study provides fundamental understanding of crowdfunders’ and entrepreneurs’ reasons to participate in crowdfunding. Gerber and Hui (2012) investigate motivations and deterrents for crowdfunding participation by using a qualitative approach with semi-structured interviews as data collection method. They argue that the advantage of semi-structured interviews is the ability to collect data in situ, not just reflective data.

In contrast, quantitative studies aim at testing or verifying existing theories and generalizable findings on the basis of statistical evidence. This seems to be the case in ample research on BAs and VCs where the findings of earlier studies are often tested in new settings. There are clear explorative limitations in quantitative studies (Stebbins, 2001) and as indicated earlier Ahlers et al. (2013) have experienced limitations by using a quantitative method.
Table 1: Overview of Research Methods and Limitations

<table>
<thead>
<tr>
<th>Method</th>
<th>Limitations</th>
</tr>
</thead>
</table>
| Verbal Protocol Analysis      | • Limited to insights on one or very few simulated scenarios e.g. investment opportunities (Hall & Hofer, 1993).  
                                | • The value of thought units is questionable (Zacharakis & Meyer, 1995).  
                                | • Preferably conducted with researchers being physically present (Ericsson & Simon, 1985).                                           |
| Questionnaire                 | • Difficult to obtain satisfactory response rates (Wetzel, 1983).  
                                | • Hypothesis testing with limited room to explore a new phenomenon (Stebbins, 2001).  
                                | • Focus on statistical measurement and generalization (Corbin & Strauss, 2008).                                                          |
| Statistical Data Analysis     | • Evolving interpretation is precluded in statistical data analysis (Silverman, 2006).                                                   
                                | • Using this method, Ahlers et al. (2013) do not provide insights on the individual crowdinvestors.                                   |

4.2 A Qualitative Study

The selection of a qualitative study relates to some of the limitations, which are associated with quantitative research, namely the inability to explore new phenomena in detail. The point of departure in this study is the knowledge gap illuminated by our literature review and operationalized by our problem statement. When addressing a research field where little prior knowledge exits and where the research question is based on “why or how” it is recommended by Stebbins (2001) to follow a qualitative approach. Moreover, Eisenhardt (1989) emphasises that qualitative studies can make significant contributions to theory development when key themes within a research field are weakly developed. This is supported by research on crowdfunding of Ordanini et al. (2011) and Gerber and Hui (2012). Further, Corbin and Strauss (2008) elaborate that the aim of working with qualitative methods is to explore complex social phenomena.

Our literature review revealed two dominant approaches to qualitative research in the field of entrepreneurial finance: Verbal protocol analysis and semi-structured interviews. While both methods are used to conduct inspiring studies they are subject to unique advantages and limitations. The advantage of verbal protocol analysis is that it helps to overcome post-hoc
biases. However, given our limitations as student researchers and with regard to Ericsson and Simon's (1985) argument that verbal protocol analysis is best performed in situ, we decided against this approach. Interviews are a useful method if the aim is to understand and explore human behaviour (Kvale, 2007). Further, semi-structured interviews proposed by Kvale (2007) are well suited to our exploratory study. The semi-structured interview method encourages the researcher to focus on evolving interpretation, which means breaking with the interview protocol if the conversation reveals topics, which could not be expected a priori (Kvale, 1997; Isabella, 1990).

### 4.3 Selection of Theory

In this chapter we will briefly argue for the selection of business angel theory as a central theoretical concept. The theory itself will be presented and operationalized in chapter 6. While our research approach is inspired by a tradition of exploratory research and driven by empirical data, Suddaby (2006) and Kvale (2007) argue that qualitative researchers must have a basic understanding of the research field prior to data collection. Theory has a pivotal role in establishing that understanding.

As the problem statement and the literature review on crowdfunding and crowdinvesting highlight there is a need for more research and more theory in the research field of crowdinvesting. In the lack of theoretical inspiration from the research field in concern, we investigated comparable phenomena, which could help to explain how crowdinvestors are informing their investment decision. Through an extensive literature review of entrepreneurial finance including both VC and BA theory, we found that existing research on business angels can provide a foundation for our research and the preparation of the interview protocol (see Chapter 6.1). BAs are usually characterized as informal investors who are investing their own money into new ventures (Mason, 2008). Crowdinvestors share this characteristic, even if their investment amounts are smaller. BAs investment decision has been studied for decades and entails a rich literature (see Appendix 2; e.g. Mason & Harrison, 1996b; Feeney et al., 1999; Van Osnabrugge, 2000; Mason & Stark, 2004). Previous studies have followed a similar approach by comparing crowdinvestors and crowdfunders to BAs or VCs, thus we consider this selection to be fully justified (see Mollick, 2013; Ahlers et al., 2013; Schwienbacher & Larralde, 2010; Hornuf & Schwienbacher, 2014).
4.4 Semi-Structured Interview Method

The point of departure for the interviews was our interview guide (see Appendix 6). Following a semi-structured interview approach, we have intentionally avoided to follow the interview guide meticulously.

The semi-structured interview is first and foremost a specific conversation technique, where in opposition to daily life dialogues and philosophical conversations it is the interviewer as a professional researcher who asks the questions and the interviewee responding (Kvale, 1997). Applying the semi-structured form means that we compiled an interview guide prior to the interview, but allowed the interview to take turns around interesting subjects as they emerged. As an example, we have often asked the interviewee to elaborate on their feelings and thoughts when remarking on interesting topics.

We divided the interview guide into three sections. In the first section interviewees were asked about their professional and educational background. In the second section we addressed their crowdinvesting activity, their motivation and experience with investing. In the third section we asked our interviewees about their investment process from finding an interesting crowdinvesting project to the actual investment. We assumed that talking about personal investments could be a sensitive topic to some of the interviewees and thus started every interview by asking the interviewee to introduce him- or herself, including education and profession. This way we are able to draw implications from their experiences with entrepreneurship and finance, but most importantly it built trust needed to discuss more confidential and sensitive topics (Kvale, 1997; Appendix 6). Further, considerations of building trust and removing potential communication barriers encouraged us to offer Danish and German interviewees the option of interview in their native language. As a result we conducted one Danish and seven German interviews. These were translated into English before the coding.

4.5 Data Collection

As a point of departure, we contacted the crowdinvesting platforms FundedByMe and Seedrs, and conducted two preliminary unstructured interviews with management representatives. They informed us about the current state of crowdinvesting, the overall business situation and their understanding of the investor crowd. Both platforms offered their support for our data collection.
As preparation to interviewee recruitment we set up an online blog\(^5\) to provide relevant stakeholders with a brief introduction to our research. Besides introducing our research the blog served well in establishing trust in our research and to demonstrate a professional approach to the study.

We conducted a total of 20 interviews with crowdinvestors via Skype and by phone ranging from 20 minutes to 2 hours in duration. All interviews were recorded and transcribed. The transcription was carried out within two days after the interview. Interviewing through Skype entails the option of video call and whenever possible this feature was utilized. In cases where Skype was not an option or the interviewee preferred a phone call, interviews were conducted via phone.

4.5.1 Crowdinvesting Platforms
In order to obtain a diverse sample of investors and to allow research on different aspects of crowdinvesting we decided to recruit investors from three platforms: Seedmatch from Germany, Seedrs from the U.K. and FundedByMe from Sweden.

4.5.1.1 Seedmatch
The Seedmatch model is based on a so-called ‘partiarisches Darlehen’ or a profit participating loan. In human language: “It is debt that talks, walks and quacks like equity”, according to Tim Reinsch, COO of Seedmatch (Weverbergh, 2013). It gives the investor rights to participate in the profits of the company, either through dividends or other forms of capital gains. To this date Seedmatch only accepts investments from Germany-based individuals. We were aware of the differences prior to selecting Seedmatch, but we presume that investors’ selection process is similar to that from investors on FundedByMe and Seedrs.

4.5.1.2 Seedrs
With their office in London, Seedrs is allowing investors from throughout the EU to invest in start-ups listed on the platform. The UK legislation is offering eligible investors a tax relief of up to 50 per cent of their investment back in income tax through the Seed Enterprise Investments Scheme (SEIS) and 30 per cent through the Enterprise Investment Scheme (EIS) (Seedrs, 2013). Among others, this was an interesting aspect to interview investors from Seedrs to get a better understanding of how the tax incentives may trigger investments on the platform.

\(^5\) Our blog can be accessed via the following link: http://cbsequitycrowdfunding.wordpress.com/.
4.5.1.3 FundedByMe

Beginning in Stockholm, the Swedish platform expanded its base during 2013, by opening offices in Helsinki, Oslo, Copenhagen, Berlin, Madrid and Milan. The latest opening in Singapore started operating in January 2014. FundedByMe operates a multi-purpose platform, including reward-based, equity-based and lending-based crowdfunding. Being based in Copenhagen we assumed that including a Scandinavian based platform would increase our chance of recruiting interviewees.

4.5.2 Interviewees

Out of the 20 interviews, 4 interviewees invested on Seedrs, 8 on FundedByMe and 8 on Seedmatch (see Table 1). A few investors had additional investment experience from other platforms. For our recruiting process the sole requirement was that investors made at least one investment. Therefore, our sample initially included 4 interviewees who turned out to be family and friends investors (RC, MTH, SG and PLS). It was not until we conducted and analysed all interviews that we realized FF investors should not be included in our overall analysis (see Chapter 7.1).

We took a proactive approach to interviewee recruitment, contacting interviewees directly through emails or social media such as LinkedIn and Xing. On Seedrs and Seedmatch anonymity is optional for the investor. A minority show their identity and sometimes link to their social media profiles. We used this option to find investors and collected contact information in a database. Afterwards we sent out an invitation to join our study as an interview partner. The invitation was linked to our blog where they would be introduced to our research. The blog also featured a sign up form where investors could sign up to participate. However in most cases the interview was scheduled directly by correspondence via E-mail or LinkedIn and Xing. We contacted a total of 37 crowdinvestors from Seedrs and Seedmatch, yielding 11 interviews (30 per cent).

In the case of FundedByMe, we were provided help by the platform to identify crowdinvestors who were subsequently contacted via email. Two interviewees were identified through FundedByMe’s blog. In total 20 investors on FundedByMe were contacted yielding 8 interviews (40 per cent). We also included one investor from the German platform Innovestment. This interview was scheduled through personal contacts.

6 See Table 2 for an overview of interviewees.
In agreement with our interview partners we decided to secure our interviewees’ anonymity and assigned random codes instead of using their real names. On the next page an overview of name codes and other investor details is provided in Table 2.

Table 2: Overview of Interviewees

<table>
<thead>
<tr>
<th>Initials</th>
<th>Gender</th>
<th>Number of Investments</th>
<th>Platforms</th>
<th>Profession</th>
<th>Education</th>
</tr>
</thead>
<tbody>
<tr>
<td>OGG</td>
<td>Male</td>
<td>1</td>
<td>Innovestment</td>
<td>Entrepreneur</td>
<td>MBA</td>
</tr>
<tr>
<td>AN</td>
<td>Female</td>
<td>10</td>
<td>FundedByMe</td>
<td>Entrepreneur</td>
<td>Informal</td>
</tr>
<tr>
<td>CI</td>
<td>Male</td>
<td>11</td>
<td>Seedrs</td>
<td>Finance</td>
<td>MBA</td>
</tr>
<tr>
<td>FP</td>
<td>Male</td>
<td>9</td>
<td>Seedmatch</td>
<td>Entrepreneur</td>
<td>Technology Engineer</td>
</tr>
<tr>
<td>KNZ</td>
<td>Male</td>
<td>48</td>
<td>Seedrs</td>
<td>Marketing</td>
<td>MBA</td>
</tr>
<tr>
<td>NH</td>
<td>Male</td>
<td>5</td>
<td>FundedByMe</td>
<td>Finance</td>
<td>Engineer</td>
</tr>
<tr>
<td>PS</td>
<td>Male</td>
<td>40</td>
<td>FundedByMe</td>
<td>Entrepreneur/Management Consulting</td>
<td>MBA</td>
</tr>
<tr>
<td>RC</td>
<td>Female</td>
<td>1</td>
<td>FundedByMe</td>
<td>Public Sector Finance</td>
<td>M.Sc. in Economics</td>
</tr>
<tr>
<td>TL</td>
<td>Male</td>
<td>15</td>
<td>Seedrs</td>
<td>Software Developer</td>
<td>Computer Science Engineer</td>
</tr>
<tr>
<td>JD</td>
<td>Male</td>
<td>1</td>
<td>Seedmatch</td>
<td>Sales Manager for software company</td>
<td>Electrical engineering</td>
</tr>
<tr>
<td>KG</td>
<td>Male</td>
<td>35</td>
<td>Seedmatch</td>
<td>Private Equity</td>
<td>M.Sc. in Maths</td>
</tr>
<tr>
<td>LH</td>
<td>Male</td>
<td>9</td>
<td>Seedmatch</td>
<td>Works at BITS University with focus on Entrepreneurship</td>
<td>M.Sc. in Accounting and Finance/ PhD in HR Management</td>
</tr>
<tr>
<td>MW</td>
<td>Male</td>
<td>3</td>
<td>Seedmatch</td>
<td>Start-up Coach. Background in Project management</td>
<td>M.Sc. in Economics</td>
</tr>
<tr>
<td>PE</td>
<td>Male</td>
<td>6</td>
<td>Seedrs</td>
<td>Entrepreneur</td>
<td>BA Business Studies</td>
</tr>
<tr>
<td>PLS</td>
<td>Male</td>
<td>1</td>
<td>FundedByMe</td>
<td>Project Manager</td>
<td>M.Sc. Computer Science</td>
</tr>
<tr>
<td>RN</td>
<td>Male</td>
<td>10</td>
<td>Seedmatch</td>
<td>Start-up consultant</td>
<td>N/A</td>
</tr>
<tr>
<td>SD</td>
<td>Male</td>
<td>4</td>
<td>Seedmatch</td>
<td>Master Student/Entrepreneur</td>
<td>M.Sc. in Management and Finance</td>
</tr>
<tr>
<td>SG</td>
<td>Male</td>
<td>1</td>
<td>FundedByMe</td>
<td>Researcher</td>
<td>M.Sc. in Pedagogy</td>
</tr>
<tr>
<td>TK</td>
<td>Male</td>
<td>5</td>
<td>FundedByMe</td>
<td>Entrepreneur</td>
<td>M.Sc. Design, Communication &amp; Media</td>
</tr>
<tr>
<td>MTH</td>
<td>Female</td>
<td>1</td>
<td>FundedByMe</td>
<td>Primary School Teacher</td>
<td>M.Sc. in English</td>
</tr>
</tbody>
</table>
4.6 Data Analysis

As qualitative researchers we were subject to the predicaments that often characterise qualitative research, such as the insecurity with methodological questions regarding sample appropriateness. How do we ensure to capture evolving topics we did not expect a priori? And how do we derive relevant meaning from the collected data? (Corbin & Strauss, 2008).

The first instrument applied was a continuous evaluation of emerging data. During the interview we took notes to capture emerging topics and after each interview we evaluated and discussed the data. In this way we grew more experienced with every interview and started to recognize patterns emerging from the data.

In total almost 12 hours of interview were collected, which is ample to manage for inexperienced researchers. In order to derive meaning from the data and to make it manageable, interviews were transcribe shortly after the interview. We strived to transcribe interviews meticulously, reflecting the way they were conducted. This second engagement with the data material was used for interpretation as recommended by Kvale (2007), who states that transcription is not a simple clerical task but an interpretive process.

The transcription process resulted in 218 pages of interview transcripts. To manage the large amount of data we decided to use the computer software NVivo, which is a useful program to organize coded data. We undertook a coding process of methodically reading through the transcripts with the objective of developing categories to assort the interviews into a more manageable form. By doing so, we ensured to conduct a substantial analysis where the data is presented in a meaningful way (Corbin & Strauss, 2008). The first step in the process was to assign relevant text to broad categories, which were inspired by our interview topics (Silverman, 2006). This initial coding resulted in a large number of broad categories helping to organize basic ideas. The categories can be understood as theoretical concepts. In a subsequent step data was examined in detail to identify and reflect on sub-categories underpinning the concepts. An overview of our coding is provided in Table 3 on the next page. Sources represent the number of how many respondents mentioned the category and codes the number of text pieces related to the category.
### Table 3: Overview of Coding

<table>
<thead>
<tr>
<th>Category</th>
<th>Sources</th>
<th>Codes</th>
<th>Sub-category</th>
</tr>
</thead>
<tbody>
<tr>
<td>Investor Profile</td>
<td>20</td>
<td>49</td>
<td>Professional background, Education, Investment experience, Activity in crowdfunding</td>
</tr>
<tr>
<td>Motivation</td>
<td>20</td>
<td>95</td>
<td>Return on Investment, Tax benefits, Playing a role in the company, Extending network, Crowdsourcing, Portfolio diversification</td>
</tr>
<tr>
<td>Screening</td>
<td>15</td>
<td>30</td>
<td>Personal Interest, Innovation, Traction</td>
</tr>
<tr>
<td>Evaluation</td>
<td>20</td>
<td>154</td>
<td>Business Plan, Team characteristics, Entrepreneur, Market characteristics, Financial characteristics, Business Idea, Geography, Investor fit</td>
</tr>
<tr>
<td>Investment</td>
<td>15</td>
<td>40</td>
<td>Sizing of investment, Play money, Time spent</td>
</tr>
<tr>
<td>Post-investment</td>
<td>18</td>
<td>46</td>
<td>Active engagement in venture, Reading updates, Networking</td>
</tr>
<tr>
<td>Miscellaneous</td>
<td>16</td>
<td>56</td>
<td>Legislation, Platform details, Personal outlook</td>
</tr>
</tbody>
</table>
4.7 Validity

Traditionally, validity in qualitative research involves determining the degrees to which researchers' claims about knowledge correspond to reality (or the interviewee's construction of reality) being studied (Eisner & Peshkin, 1990). Given the informal nature of the BA market, studies on this investor type have traditionally suffered from difficulties of identifying BAs and have struggled to create random samples (Wetzel, 1983; Feeney, 1999; Mason & Harrison, 2002a; Wiltbank, 2009). Although this study focuses on crowdinvestors and their decision-making processes it is subject to similar limitations previously faced by researchers studying BAs. The vast majority of crowdinvestors is investing anonymously. Since our initial attempt of getting access to the crowdinvestors with the help of the platform operators failed, we had to rely on inviting crowdinvestors with public profiles on Seedrs and Seedmatch to join for an interview. There is a risk that these individuals represent a certain type of investor and our sample can therefore not be considered random. Consequently, we must be aware of the potential impact of this bias on our analysis and the findings we present in this thesis. Thus, any insights presented in the context of this thesis are only a reflection of insights gathered from our sample and should therefore not be generalized.

Another potential limitation in our study is that our interviews were performed retrospectively. This means we asked our interviewees to think back to their last investment and the actions they performed during the process. Self-reported, retrospective data is subject to conscious or unconscious errors associated with post-hoc rationalization and recall biases (Zacharakis & Meyer, 1995). Further, it must be assumed that cognitive perceptual limitations exist and that crowdinvestors might have limited insights into their decision processes, especially since many are inexperienced in this form of investing. It is possible our interviewees were influenced by such biases and over- or understated certain aspects of their investment process and criteria.

Despite the possibilities of the before mentioned biases, it is our belief that our sample and the presented findings are reliable and provide valuable insights and inspirations for future research on the subject.
5 THEMATIC CONTEXT: FROM CROWDSOURCING TO CROWDINVESTING

In this chapter crowdsourcing and crowdfunding are presented as the antecedents of crowdinvesting. It is important to understand these concepts and their interdependence in order to obtain a fundamental understanding of the phenomenon of crowdinvesting.

After establishing the foundation to comprehending crowdinvesting as a unique concept, we introduce a detailed presentation of its potential to bridge the financial gap in venture funding. This is followed by an introduction of the crowdinvesting eco-system and the key actors. Finally, an exemplary crowdinvesting process consisting of different phases is presented.

5.1 Crowdsourcing

Crowdsourcing leverages the creative abilities of the “crowd” to obtain ideas, feedback and solutions in order to develop corporate activities. In 2004, Surowiecki’s work "The Wisdom of Crowds" received a lot of attention and contributed to the popular notion of using the Internet community to help with problem-solving and other decision-making, both in the private and public domain. Jeff Howe (2006) introduced the term crowdsourcing in the June 2006 issue of Wired Magazine. Academia started publishing research on the subject since 2008. After an extensive survey of literature Estellés-Arolas and González-Ladrónde-Guevara (2012) came up with the following comprehensive definition of crowdsourcing:

“Crowdsourcing is a type of participative online activity in which an individual, an institution, a non-profit organization, or a company proposes to a group of individuals of varying knowledge, heterogeneity, and number, via a flexible open call, the voluntary undertaking of a task. The undertaking of the task, of variable complexity and modularity, and in which the crowd should participate bringing their work, money, knowledge, and/or experience, always entails mutual benefit. The user will receive the satisfaction of a given type of need, be it economic, social recognition, self-esteem, or the development of individual skills, while the crowdsourcer will obtain and utilize to their advantage what the user has brought to the venture, whose form will depend on the type of activity undertaken” (Estellés-Arolas & González-Ladrónde, 2012:9f.).

This definition is wordy and complex, but it is highlighting the key ingredients of the concept (Brabham, 2013). Several authors, including Brabham (2008) and Kleeman et al. (2008)
identify the development of Web 2.0 as a prerequisite to the development of crowdsourcing. The author’s point out that its structure is mandatory for companies to be able to reach large networks of dispersed consumers more easily. Sang-Heui et al. (2008) define three main characteristics for the Web 2.0. First, collaboration allows combining each other’s knowledge and resources. Second, openness allows people to contribute freely to different projects. And third, participation is increased thanks to the ease of access and use of computers and Internet. According to Granovetter (1973) the most efficient networks are those that link to the broadest range of information, knowledge and experience. Benkler’s (2006) seminal analysis of networks highlights their influence in our rapidly changing world. Benkler perceives a transition towards a decentralized industrial information economy where human capacity is the primary source of scarcity. To this end, Benkler posits the possible reversal of two trends that defined the last century of economic development: centralization and commercialization. Eric von Hippel also describes this shift towards a more democratized and decentralized economy in his influential work on the democratization of innovation, where he argues that consumers become active co-workers in open innovation practices (Hippel, 2005; Kleeman et al., 2008, Brabham, 2013). The word democratization appears in both the popular and scholarly discourse on crowdsourcing and more recently in the context of crowdfunding, for example when President Obama named crowdfunding as a potential game changer by “democratizing the sphere of entrepreneurial finance” (New York Times, 2012).

### 5.2 Crowdfunding

Although crowdsourcing is regarded as the antecedent of crowdfunding, several caveats and clarifications need to be made in order to transform the definition of crowdsourcing to the context of crowdfunding. Essentially, “crowdfunding describes an innovative funding model whereby individuals use the Internet – via an open call⁷ – to contribute relatively small amounts of money to support the creation of a specific product or the investment in a specific business idea either in form of donation or in exchange for some form of reward and/ or voting rights” (Belleflamme et al., 2012b:5; Brabham, 2013). This definition highlights the interdisciplinary nature of crowdfunding (Lehner, 2013). A definition of the phenomenon requires a combined assessment of different disciplines, such as business administration,

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⁷ An open call is understood as a call-to-action; e.g. a call for capital or support, where the message is not targeted at any specific intended recipient (Massolution, 2013:18).
Kickstarter is a well-known illustration of the crowdfunding idea. At Kickstarter, particularly people from the arts can post an idea for a creative project or business and ask members in the online community to support the idea with money contributions in return for previously specified rewards. For example, a musician wants to record his independent new album by seeking funding from the crowd to finance the cost related to the task. This musician may offer a variety of rewards for different levels of support, or *pledges* as labelled by Kickstarter, all of which will be delivered to the supporters in case the project reaches its full funding goal.

Despite, crowdfunding does not fit the strict definition of crowdsourcing. Crowdsourcing is a blend of top-down managed processes, with the locus of control over production residing with both, the organization and the crowd in a shared, give-and-take relationship. Crowdfunding does not resemble this structure. In crowdfunding an artist or an entrepreneur develops and idea and seeks financial help from the crowd to develop his or her idea into a viable business. There is no engagement with the crowd on what the artistic endeavour will look like or how the start-up business will be managed. Crowdfunding uses the proven mechanisms of crowdsourcing with the distinguishing factor of pooling capital from the crowd instead of creative capabilities. Consequently, crowdfunding is distributed financing, not crowdsourcing (Brabham, 2008).

Collecting small amounts of money from a large number of people has a long history in many domains (Ordanini, et al. 2011). For example, Mozart and Beethoven financed concerts and new music compositions with money from interested patrons, the Statue of Liberty in New York was funded by small donations from the American and French people, and President Barack Obama’s 2008 election campaign raised most of its funds from small donations over the web (Hemer, 2011).

As regard to the underlying factors of the recent success of crowdfunding, researchers have highlighted three main elements (Agrawal et al., 2011; Agrawal et al., 2013):

- The shortage of capital caused by the current global financial climate, that has rendered difficulties in raising risk capital for entrepreneurial companies (see Chapter 5.3.1).
- The evolution of the Web 2.0 technologies.
- Matching funders with creators is now more efficient and effective due to lower search costs online.
- Risk exposure is reduced because funding in small increments is economically feasible online.
- Low communication costs facilitate improved information gathering and progress monitoring for distant funders.

- The success of the related crowdsourcing phenomenon.

5.2.1 Forms of Crowdfunding
Crowdfunding facilitates funding for a diverse set of purposes by applying numerous business models. Massolution (2013) distinguishes four different models of crowdfunding as illustrated below. The majority of platforms can be categorized under these four typologies, but it is important to keep in mind that several variations and hybrid forms of the different models exist.

5.2.1.1 Donation Model
The donation-based model of crowdfunding is a means for charities, or those who raise money for social and/or charitable projects, to engage a community online and to enable them to donate to a project. The key difference to the other crowdfunding models hereby is the absence of financial or material rewards for donors. This model is particularly attractive to small organisations and charities or private people raising money for a specific charitable cause. Popular platforms include Crowdrise and Causes.

5.2.1.2 Reward/Pre-purchase Model
As stated previously, the reward-based model is by far the most popular form of crowdfunding, especially within the creative, social and entrepreneurial sphere. This model allows people to contribute small amounts of money – often referred to as pledges – in return for previously specified non-financial rewards, often operated as a tiered system where the value of rewards increases with the contribution. The reward-based model often resembles philanthropy with contributions in most cases exceeding the value of rewards. Some projects are run on a pre-sales basis, where supporters pre-purchase a prototyped product, a movie or a record to finance the initial production, filming or recording (Belleflamme et al., 2012a; Kortleben & Vollmar, 2012). If these projects achieve their funding targets the fundraiser promises to produce the product and deliver it to the backers, who benefit from being among the first group to receive the final outcome. Based on these features it is often assumed that backers in pre-selling agreements resemble lead user characteristics. Kickstarter and Indiegogo are among the most well known reward-based platforms.
5.2.1.3 Lending Model
Crowdfunded lending is largely an evolution of the peer-to-peer model of lending, pioneered by companies such as LendingClub and Zopa (Hemer et al., 2011; Röthler & Wenzlaff, 2011). Private people or businesses seeking a loan apply through the platform via a pitch and members of the crowd cover a micro stake of the overall loan in return for a specified interest rate, as utilized by the UK-based FundingCircle. Some platforms focused on social causes offer interest-free loans such as Kiva, a micro-lending site, which has risen more than USD 500 million since its introduction in 2005. Astonishingly, the overall default rate is barely above one percent (Kiva, 2013).

5.2.1.4 Equity Model (Crowdinvesting)
The remaining crowdfunding model is the application of the concept to investing for equity, or profit/revenue sharing in businesses or projects (Klöhn & Hornuf, 2012; Beck, 2012; Moritz & Block, 2013). The equity-based model – here referred to as crowdinvesting - has only shown modest growth during the last years due to regulatory restrictions imposed on this type of activity. In many countries the public offering of securities requires the publication of a sales prospectus, which must be accepted by a supervisory authority, e.g. the SEC in the US or the BaFin in Germany. The respective procedures are complicated, time-consuming and costly, prohibiting many businesses from following this path (Hemer, 2011).

Some European platforms have pioneered the equity-based model, allowing non-accredited investors to take a small stake in an unlisted or private business, while the US legislation has been critical towards easing the regulatory hurdles for crowdinvesting until last year, when the JOBS Act was passed (Schwienbacher & Larralde, 2010). CrowdCube and Seedrs in the UK, Fundedbyme in Sweden, and Seedmatch in Germany, are among the platforms with good traction.

5.3 Crowdinvesting
In the context of this project we adopt the following definition of crowdinvesting coined by Hagedorn and Pinkwart (2013:17):

“Crowdinvesting is a financing method for young ventures and other commercial projects that supports the acquisition of equity by coordinating the submission of different forms of shares to an undefined group of possible investors through social virtual communities.”
5.3.1 Crowdinvesting and the Financing Gap

Crowdinvesting, as illustrated in Figure 1, can be regarded as a means to bridge the financing gap – often referred to as valley of death – from initial investments provided by the entrepreneur(s) own funds and family and friends to more formal sources of funding supplied by BAs and VCs. This hypothesis is based on the assumption that profit-seeking investors only invest in businesses with a suitable risk-return profile. Moreover, in recent years traditional sources of risk capital have increasingly been moving their investment activity upstream by making bigger investments into more established companies (Collins & Pierrakis, 2012).

This shift in focus has created a significant “funding gap” for early stage start-up ventures and has renewed both academic and practitioner interest in potential methods of promoting the aggregated pool of capital available to early-stage start-up enterprises that are pre-revenue and yet to reach commercialisation stages (Ley & Weaven, 2011; Cassar 2004; Cumming 2007).

The financing gap is best defined as, “the absence of small amounts of risk capital from institutional sources for companies at the seed, start-up and early-growth stages, which arises because the fixed costs of investment appraisal and monitoring make it uneconomic for venture capital funds to make small investments, and because of the reluctance of banks to make unsecured lending” (Mason, 1996:4). According to a survey of 1,001 entrepreneurs conducted by Ernst & Young in 2012, almost two-thirds of respondents reported that getting access to funding is their most pressing problem. The challenge faced by many entrepreneurs to receive access to funding, especially in the early phases of the entrepreneurial lifecycle – the pre-seed and seed phase – is one of today’s major obstacles to the creation, survival and growth of enterprises (Kraemer-Eis et al., 2012; Ernst & Young, 2012).

An effective funding ecosystem requires that entrepreneurial companies must be able to access finance at every stage of their development. Traditional approaches to financing these businesses envisage series of funding stages, whereby companies move from pre-seed and seed, through to start-up, emerging growth and expansion (see Figure 1). At each stage, there should be sources of finance available, and at least in theory, a smooth transition should be possible between the different forms of finance. Nonetheless, there is clear evidence that large gaps have appeared along the funding channel, not at last in the
course and aftermath of the financial crisis. These gaps make it difficult for entrepreneurial companies to start up and grow, meaning that they are unable to play their potential role of enabling a sustained economic recovery.

![Figure 1: Sources of Financing in the Entrepreneurial Lifecycle (Own illustration based on Ernst & Young (2012))](image)

At the pre-seed and seed stage of growth, the entrepreneurial venture is just being established. These phases are often dominated by tasks related to research and development to determine the product or service, to develop a working prototype model to assess the venture’s viability, to conduct a proof-of-concept and to write a compelling business plan (Ernst & Young, 2012; Beck, 2012). In many cases, financing needs are still reasonably small and are possibly even lower than they were a few years ago, thanks to the advancements of technology and innovations, such as cloud computing, significantly reducing the cost to start-up (Miller & Bound, 2011; Suster, 2012).

As mentioned, most formal investors are unwilling to make equity investments at the seed stage. Seed investments entail high risk and are likely to take many years before generating a return to the investors, if they do so at all. Another problem is that early-stage companies are very difficult to value because the revenue potential remains uncertain. According to recent data, around 35 per cent of business angel investments were allocated to companies at the pre-/seed stage in 2013, down by 20 per cent from the pre-crisis peak in 2008 (CVR,
At the start-up stage, business angels are filling some of the gap left by traditional VC, which more recently tends to focus on later-stage companies.

As VC firms, banks and even BAs focus their attention on later-stage ventures with lower risk profile, seed-stage companies face a shortage of viable funding options. Governments can play an important role in filling gaps in seed funding, through grants and other forms of public aid, but their scope is not sufficient to remove barriers to funding.

The emergence of crowdinvesting can be seen as a promising alternative source of early-stage entrepreneurial finance under two scenarios. One is the initial seed money to start a business, where family and friends funding may be unavailable, insufficient or amounts required are too small making an investment unattractive to BAs. Early-stage investments are very risky due to high levels of uncertainty surrounding the business and the presence of information asymmetry between the entrepreneur and the investor. Thus, an investor will have to invest considerable time and money to conduct a thorough due diligence to inform his investment decision. Given these costs, investments have to be above a certain threshold to be economically viable (Hagedorn & Pinkwart, 2013). Second, there is a gap above the level where business angels are usually active, but where the capital required is too small for VCs to involve. Although the majority of funds raised via crowdinvesting are located in the lower gap, the model has the potential to incorporate larger amounts, especially if it can entice more sophisticated investors to get involved (Collins & Pierrakis, 2012).

In 2012, around 79 per cent of all crowdinvesting rounds were of a total volume smaller than USD 250 thousand, with funding volume of successful campaigns averaging at USD 190 thousand (Massolution, 2013; Figure 2). Compared to this the average value of BA or BA-syndicate deals at the seed stage averaged USD 590 thousand during 2013 (Halo Report, 2013).

![Figure 2: Median Campaign Size in USD Across Crowdfunding Models (own illustration based on Massolution (2013:34))](image-url)
This shows that financing rounds through crowdinvesting platforms are yet smaller than those of traditional early-stage financing forms. Given the industry’s infancy and easing of regulatory burdens this gap is likely to be bridged. However, the comparison of the average size of successful crowdinvesting campaigns with alternative crowdfunding models illustrates the importance of crowdinvesting for the financing of early-stage businesses with larger capital requirements. As Figure 2 illustrates average funding rounds via crowdinvesting are by far the largest compared to the three alternative crowdfunding models. Nonetheless, it is important to point out that significant funding rounds are feasible via lending or reward-based models. A good example is the Pebble smartwatch, which collected more than USD 10 million in 2012 on Kickstarter (Kickstarter, 2012).

Overall the market of crowdinvesting is comparably small with a global volume of USD 116 million in 2012\(^8\). The JOBS-Act turning into effect in the US may trigger an unprecedented growth in funds raised via this channel and signs from the European market indicate crowdinvesting platforms are gaining momentum. In 2013, entrepreneurs raised a total of EUR 7.42 million via Seedmatch, up 166 per cent compared to 2012. In the UK, Seedrs collected more than GBP 1 million per month during the period of December 2013 to May 2014 (Seedmatch, 2014; Seedrs, 2014a).

\[^8\text{Due to legal restrictions in the US, the majority of this amount was raised through crowdfunding platforms operating in Europe (Massolution, 2013).}\]
5.3.2 Crowdinvesting Ecosystem

The crowdinvesting ecosystem essentially consists of three parties, namely the platform, entrepreneur and investors, interacting with each other in a highly regulated environment determined by the country or state involved. The securities commission is charged to implement laws providing oversight on how the interaction between the three parties is governed. This involves regulation on who can become an investor and how much they may invest through this channel, the jurisdictions companies need to comply with to be allowed offering securities and how platforms have to assist in facilitating a straight forward marketplace that as a primary goal has to protect investors (Jofre, 2014).

5.3.2.1 Crowdinvestors

The investor crowd consists of two types of investors, the accredited and non-accredited investor. The securities commissions categorize an accredited investor as a high net worth individual, who can “afford” to lose some of their investments if a company fails and who are experienced in this form of investing. Each country has its own parameters for categorization, but in essence just around 3-5 per cent of a country’s population can be assigned to this group (Van Osnabrugge & Robinson, 2000). The remainder of the population that does not meet these requirements are categorized as non-accredited investors and legislation limits their investment to protect them from losing some or all of their money. The natural worry from a regulatory point of view is that a lack of experience of non-accredited investors may lead to uninformed investments in start-ups without understanding the risks involved. Based on the information presented by the entrepreneur in the investment pitch, the investor decides on whether to invest or not and how much to invest.
5.3.2.2 Entrepreneur (Issuer)

The entrepreneur (or issuer) offers equity in exchange for investors’ money via a selected crowdinvesting platform. This involves pitching the business idea to potential investors in a compelling campaign, which usually presents the key information of the business. This includes information on the ventures team, a short business plan and how proceeds will be used. In most cases a video pitch accompanies the campaign. Campaigns usually run between 30-60 days and if the entrepreneur manages to collect his target amount within that timeframe the deal will be carried out.

5.3.2.3 Platform

The final party of the crowdinvesting ecosystem is the platform, which function as intermediary between entrepreneurs and investors. Platforms operate with different business models, but generally make revenue by charging a percentage fee of the amounts raised by the entrepreneur. As an example, Seedrs charge a fee of 7.5 per cent of the money successfully raised through the platform (Seedrs, 2014b). Platforms can be considered gatekeepers by conducting some basic due diligence in order to prevent fraud and ensure that only genuine ventures can pitch to investors.

5.3.3 Crowdinvesting Process

The process illustrated and further explained below is a simplified representation of a diverse set of processes and individual procedures. It is important to bear in mind that the steps depend on the individual platform and more importantly on the jurisdiction the respective platform operates under. The information provided is a summary of insights taken from Collins and Pierrakis (2012) and Beck (2012) in combination with the crowdinvesting process of the UK-based platform Seedrs (Seedrs, 2013).

![Figure 4: Crowdinvesting Process (own illustration based on Collins & Pierrakis (2012), Beck (2012) and Seedrs (2013).]
**Listing of investment proposal:** In the initial step the entrepreneur is asked to disclose certain information, documents and verifications to the platform he has chosen for his fundraising campaign.\(^9\) Among others, the entrepreneur has to determine how much money he is aspiring to raise and the equity amount he is offering in return, submit a business plan and a video pitch, which is often compulsory.

**Review of proposal:** Afterwards the platform performs some level of vetting by reviewing the disclosures provided by the entrepreneur to ensure they are fair, clear and not misleading, whereas the exact disclosure requirements are dependent on the standards applied by the respective platform. Once the platform is satisfied with the proposal relevant contractual agreements are signed. When contracts are in place the campaign goes live.

**Investment process:** During the investment process the campaign documents are open for review by crowdinvestors, who within a pre-defined timeframe have the option to apply for the purchase of an equity stake via the platform. An important part of this step is the entrepreneur’s interaction with potential investors by answering questions throughout the funding window.

**Closing of funding window:** If the campaign manages to reach the funding target the funds are transferred to the entrepreneur, who in exchange provides the shares. This procedure is facilitated by the platform which buys the start-up share on the investor’s behalf after conducting additional legal due diligence. In cases of Seedrs and Seedmatch the platform holds the shares on behalf of the investors to streamline the communication between the entrepreneur and the investor crowd. If the campaign does not receive the full amount money is returned to the investors.

**Post-investment process:** Following to the successful funding the entrepreneur can use the money to build his business. During the post-investment process investors are updated on relevant progress on a regular basis via mail or other channels. The entrepreneur may also decide to engage the crowd in decision-making.

\(^9\) Disclosure requirements differ between platforms and are dependent on the legislation applied in the country the platform operates in. Please see Appendix 4 for a recommended list of information to disclose (Mäschle, 2012)
**Dividends and Exit:** Whenever the entrepreneur pays dividends, floats or sells the company, the platform passes the proceeds along to the underlying investors. If the entrepreneur does not succeed with his business investors lose their investment without further prospect to earn a return.

Crowdinvesting is a part of the web 2.0 evolutions, which has its origin in the concepts of crowdsourcing and crowdfunding. Remembering this circumstance is important when studying crowdinvesting as it allows placing findings in its broader context. Subsequent to the introduction of the two antecedents, we have moved attention on crowdinvesting by highlighting the relevance of the concept as a source of early-stage entrepreneurial finance. We conclude chapter 5 by providing the reader with a comprehensive overview of the crowdinvesting ecosystem and process. This knowledge will be essential in comprehending the remaining chapters and particularly our analysis and discussion in chapters 7 and 8.

### 6 BUSINESS ANGEL THEORY

In the following chapter research on investment decision-making criteria and process as well as motivational aspects of BAs are introduced. The lack of research on crowdinvestors investment decision-making, process and motivation triggered a need to find an appropriate reference point to studying crowdinvestors. Following an extensive literature review we decided to inspire our research by BA theory (see Appendix 2&3). Previous studies on crowdfunding follow a similar approach and we consider this selection to be fully justified (see Mollick, 2013; Ahlers et al., 2013; Schwienbacher & Larralde, 2010; Hornuf & Schwienbacher, 2014).

Before moving into BA theory introduction we briefly outline our reasoning to deselect VC theory as a reference point for this study.

#### 6.1 Delimitation

The decision-making criteria and process applied by informal (BA) and institutional (VC) investors in their assessment of new investments have attracted interest in earlier research
Due to the informal nature of the market, research on BAs is less available than on VCs, partly because efforts to gather data on BAs began later than those on VCs – nineties vs. seventies (Appendix 2 & 3; Benjamin & Margulis, 1986; Kraemer-Eis et al., 2012). While many studies conclude that BAs arrive at their investment decisions in a similar manner as VCs, understanding the fundamental differences prompted by scale and stage of investment and by the nature of agency relationships between investors and the entrepreneur is paramount (Feeney et al., 1999; MacMillan et al., 1985).

BAs, i.e. private individuals who invest their own money in unlisted small and medium-sized ventures, to which they do not have any family connection, play a pivotal role in the risk capital cycle (Harrison et al., 2010). BAs are usually wealthy individuals with experience in entrepreneurship investing in young businesses with the aim of utilizing their personal network and experience to help the start-up succeed. They are frequently the first source of external finance for start-ups in the early-stages of the company life cycle and can serve as a bridge to later-stage sources of funding such as formal VCs or private equity (see Figure 1; OECD, 2006).

Prior research shows that investment criteria and motives are different for BAs and VCs (Van Osnabrugge & Robinson, 2000). They tend to invest more on a “gut feeling” rather than based on the accurate valuation of the term sheet of the company. This can be explained by the fact that BAs invest in earlier stages of the lifecycle, when the entrepreneur does not have a well-articulated business plan and financial data is scarce. BAs tend to base their decision on highly intangible assets of the company, such as the experience and track record of the entrepreneur or of the management team. Since they invest their own money, BAs invest preferably in companies, which they can maintain close contacts with. BAs seek to be consulted regarding any major decision and frequently take on managerial roles within the venture to reduce agency risk. Therefore, BAs often invest in companies in close proximity (Berchicci et al., 2011). Compared to VCs, investments provided by BAs tend to be of

10 For an extensive list of studies included in our review of prior research on BA and VC please see Appendix 2 & 3.
smaller size and to occur at earlier stages in the life cycle of the firm (see Figure 1; Van Osnabrugge & Robinson, 2000).

Contrary, VCs collect financing from outside investors\(^\text{11}\) on a competitive basis and then re-invest those funds in entrepreneurial ventures (Van Osnabrugge & Robinson, 2000). The VC firm is compensated on the basis of the performance of the fund’s portfolio and their investment decision is primarily based on economic considerations (Mason & Harrison, 2002a). Because of the agency concerns of their fund providers, VCs are obliged to demonstrate competent behaviour to them from the beginning of their investment process. This involves thorough screening of proposals, stringent due diligence and contract formulation before investing – a very costly exercise. Consequently, VCs tend to avoid small-scale investments, because the administrative burdens are too high when matched against likely returns. The fixed deal costs render such deals unprofitable and are simply not attractive to VCs (Coveney & Moore, 1998).

Based on the relationship with fund providers VCs are forced to manage a two-tiered investment system and contend with both the supplier (fund) and the user (entrepreneur) of finance in the volatile environment of entrepreneurial finance. This additional agency relationship has implications on the VC investment process and explains why VCs apply different investment practices compared to less-restricted and less-accountable BAs (Van Osnabrugge & Robinson, 2000). Benjamin and Margulis (1986:216) make this distinction clear:

“Professional venture capitalists are essentially portfolio managers with a unique set of pressures. They have to raise their next fund; they have to invest the money under their management; they are responsible to overseers. None of this applies to the private investor (BA).”

Empirical results suggest that for each of the multiple variables used to measure the due diligence processes of BAs and VCs, VCs conduct significantly more due diligence than BAs. Compared to BAs, VCs: have more sector experience, invest in larger firms, conduct more market research, meet the entrepreneur more often before investing, take more independent references on the entrepreneur, analyse the financials more carefully, demand a more

\(^{11}\) For example pension funds and other institutional investors.
comprehensive business plan from the entrepreneur and incur more research costs\textsuperscript{12},
document their investment process more, consult more people before investment, and
overall take longer to invest (Van Osnabrugge & Robinson, 2000; Van Osnabrugge, 2000).

Following our extensive review of studies published on BAs and VCs investment criteria we
concluded to focus our attention exclusively on BA research. According to our interpretation
of prior research BAs resemble the closest reference point to study and understand the
investment behaviour of crowdinvestors. The structural differences between crowdinvesting
and VC investments are considered too significant to justify a comparison.

6.2 Business Angel Profile

As mentioned by Osnabrugge and Robinson (2000) profiling of BAs has been the objective
of multiple studies. We do not attempt to replicate their efforts, but instead follow the
approach of Feeney et al. (1999) and Mason (2008) to present an overall profile of BAs.
Although BAs share common traits they are a heterogeneous group of individuals.

We start by presenting a definition of BAs adopted from Mason (2008:2):

\textit{“Business angels can be defined as high net worth individuals who invest their own money,
along with their time and expertise, directly in unquoted companies in which they have no
family connection, in the hope of financial gain. They are a distinctive source of finance,
distinguishable from both ‘love money’ (family and friends) and venture capital funds and
from other forms of personal investing.”}

Feeney et al. (1999) build an investor profile based on demographic data from a multitude of
studies. They describe BAs as well-educated, wealthy individuals, typically with experience
from starting new business ventures and the preference to invest close to home. Mason
(2008) adds that they derive satisfaction or psychic income from this involvement and for
many this constitutes an important reason to invest. However, as strong as their hedonistic
satisfaction might be, their overall ambition is to capitalize their investment. They are
expecting to hold an investment for 4 to 7 years and anticipate a capital gain on exit that
provides the equivalent of an after-tax annualized rate of return between 20 to 40 per cent
(Feeney et al. 1999). According to Mason and Harrison (2007) there is a clear overweight of

\textsuperscript{12} Defined as a percentage of amount invested.
male BAs, constituting 95 per cent of all BAs in Western Europe and 90 per cent in the United States.

6.3 Business Angel Motivation

Prior studies such as Sullivan and Miller (1996) used social psychological factors to empirically formalize a scheme that identified three categories of motivations for BAs: economic, altruistic and hedonistic. Van Osnabrugge and Robinson (2000) also group motives of informal investors into three categories: Opportunity for financial gain, playing a role in the entrepreneurial process and other non-financial factors.

Previous studies conclude that in making their investment decisions, BAs are motivated first and foremost by the opportunity for high capital gains (Van Osnabrugge & Robinson, 2000; Mason & Harrison, 1994; Mason & Harrison, 1996b; Wetzel, 1981; Stedler & Peters, 2010). Mason and Harrison (1994) show that UK-based BAs seek an average return on investment of at least 30 per cent for start-ups and early-stage investments and around 20 per cent for investments in established businesses. A recent study by Wiltbank (2009) suggests that these numbers still hold true today. Compared to US-based BAs those rates are slightly higher (Wetzel, 1981; Tymes & Krasner, 1983; Gaston, 1989). While the return on investment is non-arguably the primary motivation for BAs to engage in entrepreneurial finance it is by no means the sole factor. According to prior research non-financial motives play an important role in BAs decision to invest (Wetzel, 1981; Mason & Harrison, 1994; Lumme et al. 1998; Van Osnabrugge & Robinson, 2000).

Wetzel (1981), Sullivan (1994) and Tymes and Kramer (1983) report that BAs are willing to make a trade-off between financial and various non-financial returns. Next to making money, BAs also want to have fun (Benjamin & Margulis, 1986). Landström (1992) shows that several of the investment motives of informal investors have an entrepreneurial significance. For example, the motives “the satisfaction of playing an active role in a small firm” and “having a certain influence on an investment” are often ranked high in importance to informal investors (Landström, 1992; Van Osnabrugge & Robinson, 2000). On a related note, Benjamin and Margulis (2000:93) use the terms “business creators” and “co-creator” to characterise BA intention to participate in the development process and support the venture on the way.
Baty (1991) notes that BAs are sufficiently wealthy to not depend on making a return on their investment and thus potential losses will not affect their lifestyle. However, they gain personal satisfaction and excitement from being involved with an entrepreneurial venture and helping it to get started and grow. Being involved in the process of building a company is something BAs have done successfully before and now that they have the time and money they want to do it again (Van Osnabrugge & Robinson, 2000). In this context, Wetzel (1981) and Baty (1991) mention the entrepreneur’s sense of obligation to give back to the system that allowed their businesses to prosper.

Baty (1991) suggests that the typical BA is best described as a „recreational investor“, investing what one BA described as „casino money“ in a study published by Mason and Harrison (1996b). Other studies have noted that some investors actively look for businesses, which will produce socially valuable products and/or will bring economic prosperity to their geographical region (Van Osnabrugge and Robinson, 2000).

Despite the term angel conveying the impression that altruism may be a major investment motivation, van Osnabrugge and Robinson (2000) highlight the importance of not confusing the angel moniker with any altruistic or charitable impulse. The BA investment is primarily a financial transaction.

6.4 Business Angel Investment Decision-Making Process and Criteria

In the nineties, many of what Mason and Harrison (2000) term as “second generation studies”, shifted focus on studying the investment decision-making process and investment criteria of BAs (e.g. Mason & Rogers (1997), Riding et al. (1993), Harrison & Mason (1990), Mason & Harrison (1996b), Sudek (2006)). While these studies certainly contribute to an enhanced understanding of the investment process and criteria applied by BAs, ambiguity remains. What most studies agree on is that criteria weigh more or less heavily at various stages of the investment process (Riding et al., 1993; Mason & Rogers, 1996; Van Osnabrugge & Robinson, 2000).

The following chapter will be dedicated to the investment process applied by BAs, with the objective to provide the reader with a thorough understanding of the distinct stages of the process and the criteria assessed by BAs to accept or reject an investment opportunity (Mason & Harrison, 2000). For this purpose we will use an exemplary investment process
based on Riding et al. (1993) and Haines et al. (2003) as illustrated below. Although the process is portrayed linear, in practice feedback-loops and skipping or merging of stages are common (Van Osnabrugge, 2000).

![Figure 5: Business Angel Investment Process in Reference to Riding et al. (1993) and Haines et al. (2003).]

### 6.4.1 Deal Origination

There is consensus amongst researchers that BAs apply a rather pragmatic approach in their search for investment opportunities and that it relies on fortunate encounters more than structured search (Atkin & Eseri, 1993; Osnabrugge & Robinson, 2000; Mason, 2008). Mason (2008) states that the BA market is invisible and fragmented, making it difficult for entrepreneurs to search for BAs. Osnabrugge and Robinson (2000) list some of the reasons why BAs are difficult to find: The inexistence of a BA directory, their preference for anonymity to avoid being overloaded with proposals and the private nature of BA investments.

Instead of being publicly known, BAs prefer locating investment opportunities by referrals from individual and institutional sources in their personal networks (Freear et al., 1994; Kelly & Hay, 2003; BAND, 2014). This approach is rather inefficient and has been characterized as a "giant game of hide and seek with everyone blindfolded" (Gaston, 1989:4). Obviously there have been developments in the way BAs are searching for deals since Gaston (1989) and Wetzel (1987) made aware of the market inefficiencies. Osnabrugge and Robinson (2000) list a number of websites where BAs and entrepreneurs can connect with one another. Today, BAs are increasingly using the potential of the Web 2.0 to identify investment opportunities. The rise of websites such as AngelList, which are specializing on connecting BAs and start-ups, bear witness to such developments and can be seen as evidence of a new generation of angel investing.

Often BAs ally in syndicates allowing them to co-invest with other notable investors. This enables them to fund larger deals closer to the type of small venture capital funds (Van Osnabrugge & Robinson, 2000). A syndicate leverages each members experience and
network and thus has better access to investment opportunities and enhanced possibilities to evaluate them compared to an individual BA (AngelList, 2014).

6.4.2 Initial Screening

The initial screening stage is one of the two distinct stages in the evaluation process (Riding et al., 1993). Statistics indicate that this is the most difficult hurdle to leap for a money-seeking venture, with up to 72.6 per cent of investment opportunities rejected after the first quick review (Riding et al. 1997). Usually, BAs have to go through numerous proposals to identify a promising investment opportunity. Therefore, BAs apply a systematic approach to the screening process where they consider factors like the geographic location, the amount needed, the nature of the business and any other personal investment criteria to decide if the opportunity is of interest to them (Mason & Rogers, 1997).

BAs tend to invest in sectors where they have a generic understanding of the business opportunity (Freear et al., 1997). Understanding the business allows BAs to assess how they might contribute to developing the business with their own knowledge and experiences. If the BA does not have the generic understanding of the business or see potential to add value, the opportunity will most likely be rejected (Mason, 2008).

The BA performs his initial screening with the aim to assess whether the opportunity has enough merit to justify a detailed examination. Mason and Rogers (1997) find that BAs approach this stage with a negative mindset, expecting the opportunity to be poor and looking for reasons to reject it. BAs main concerns are the market and the entrepreneur. Product and finance is less important at this stage. They expect a business plan to be available but will only skim it before conducting a more detailed investigation. BAs also want to know how the money will be spent and secure that the entrepreneur is financially committed to the business (Mason, 2008). The larger the proportion of personal wealth invested by the entrepreneur, the higher probability of securing BA investment (Prasad et al., 2000).

As presented in ‘Deal Origination’, BAs rely on their immediate networks for investment opportunities (see Chapter 6.4.1). Riding et al. (1995) suggest that referred deals may be more likely to pass the initial screening if the investor has confidence in the referrer, explaining why BAs focus their attention towards immediate networks. This is consistent with findings of Freear et al. (1994). The logic is that deal referrers are putting their own credibility
and reputation on the line, thus referrals from friends and business associates yield higher acceptance rate than referrals from accountants, lawyers and banks (Freear et al., 1994).

Mason (2008) remarks, that the screening process can take place in the form of oral pitches by the entrepreneur to an audience of BAs. Studies by Mason and Harrison (2003) and Clark (2008) point out that the quality of the presentation affect the screening decision, a poor presentation is deteriorating the BAs confidence in the entrepreneur’s capabilities.

The initial screening is the BAs way of filtering out unpromising investment opportunities and allow them to concentrate on attractive opportunities. As Riding et al. (1993) show the vast majority of opportunities (72.6 per cent) are rejected at the outset simply because they aren’t interesting for the entrepreneur. The next 15.9 per cent are eliminated at a more detailed examination and finally an additional 6 per cent is rejected before the negotiation stage where only 5 per cent of the initial investment opportunities remain.

6.4.3 Detailed Investigation
The 22 per cent of proposals passing the initial screening stage will be subject to a more rigorous assessment during the detailed investigation. An essential component of this stage is referred to as the due diligence process. Due diligence emphasizes understanding and quantifying the risk of the investment proposal, rather than looking at the potential upside (Van Osnabrugge & Robinson, 2000). Studies indicate that the median amount of time spent on due diligence is around 20 hours, though around one quarter of BAs spent less than one day (Wiltbank, 2009). Results from Wiltbank’s (2009) study on UK-based BAs indicate that accurate due diligence can increase the likelihood of making a successful investment. Wiltbank (2009) concludes that those investments where BAs spent at least 20 hours on due diligence are considerably less likely to fail.

Studies on BAs investment criteria find with considerable unanimity that the quality of the entrepreneur/management team is the most critical factor in the decision-making, underpinned by criteria related to the product and market (Haar et al., 1988; KPMG, 1992; Mason & Harrison, 1994; Mason & Harrison, 1996b; Shepherd & Zacharakis, 1999). Although financial criteria are only of secondary importance in the beginning, they become more relevant at later stages of the investment process (Van Osnabrugge & Robinson, 2000). Overall, the list of criteria mentioned in various studies is very broad, illustrating the high level of idiosyncrasy in the BA investment process (Mason & Harrison, 1996b; Feeney et al., 1999).
The following chapter presents insights from various studies on the decision-making processes of BA categorized in criteria related to the entrepreneur or entrepreneurial team, product or service, market, financial and miscellaneous.

6.4.3.1 Entrepreneur or Entrepreneurial Team

For the majority of BAs the entrepreneur is the most critical decision-making criteria at this detailed evaluation stage (Riding et al., 1995). The emphasis on the entrepreneur reflects BAs perception that agency risk is more prevalent than market risk. On that notion, Fiet (1995) argues that BAs lack information, tools and resources to evaluate market risks appropriately. Consequently, they concentrate on evaluating agency risk by assessing attributes related to the entrepreneur.

In this context many BAs emphasize management abilities, market and sales capabilities, track record of lead entrepreneur and more subjective criteria such as a strong work ethic, integrity, trust, openness, passion or enthusiasm as well as personal fit (Smith et al., 2010; Landström, 1998; Van Osnabrugge & Robinson, 2000; Mason & Stark, 2004). Whilst numerous of these factors are highly intangible getting to know the entrepreneur personally by a series of formal and informal meetings is a vital part of the process (May & Simmons, 2001; Mason & Harrison, 1996b). This emphasis on the people reflects the long and personal nature of the angel-entrepreneur relationship (Smith et al. 2010; Mason, 2008). Therefore, it is does not come as a surprise that the lack of “personal fit” – the lack of congruence between entrepreneur’s and investor’s interests and vision – is one of the major reasons to reject an investment opportunity (Feeney et al., 1999).

In their study on private investor decision-making criteria Feeney et al. (1999) list three desirable attributes regarding the entrepreneur: management track record, realism and integrity together with openness. Similarly, Mason and Rogers (1997) find that BAs place considerable emphasis on the experience and track record of the entrepreneur and his or her commitment. Mason and Harrison (1996a) arrive at similar results indicating that most BAs evaluate the entrepreneur’s expertise next to personal qualities such as honesty, trustworthiness and enthusiasm. Some BAs note that an important consideration in their investment decision is simply that they liked the entrepreneur (Mason & Harrison, 1996a).

13 Hereafter the term entrepreneur will be used as a synonym for both a one-man start-up as well as an entrepreneurial team.
Feeney et al. (1999) list some of the most common shortcomings causing them to reject an investment opportunity. A perceived lack of management knowledge, i.e. the entrepreneur lacks the capabilities to transform the idea into a viable business, and a poor management team lacking balance, experience, discipline or teamwork, almost always leads to a rejection of the opportunity. Additionally, Feeney et al. (1999) point out the adverse effect of unrealistic expectations. When entrepreneur's expectations were overly optimistic or their forecasts unsubstantiated, BAs were discouraged from investing (Feeney et al., 1999; Riding et al., 1995).

When reviewing prior research on decision-making criteria of BAs, two personal qualities of the entrepreneur, namely trustworthiness and passion, appear to be of particular importance to the investor (Mason & Harrison, 1996a; Van Osnabrugge & Robinson, 2000; Sudek, 2006; Coveney, 1996; Benjamin & Margulis, 2000; Mason, 2008). In fact, Sudek (2006) indicate that passion and trustworthiness of the entrepreneur are amongst the most important criteria when evaluating the qualities of the entrepreneur. An entrepreneur who demonstrates passion or enthusiasm typically receives more interest by investors than ventures with better business model or product, but lacking a passionate lead entrepreneur. According to Cardon et al. (2009), entrepreneurial passion is often associated with greater planning, preparation and commitment to one’s venture and BAs may translate these qualities into a higher likelihood of business success (Sudek, 2006). Next to passion, trustworthiness is a crucial attribute for any entrepreneur who wants to raise money from informal investors. A lack of trust would often negate any potential upsides of the investment opportunity. Sudek (2006:95) concludes, “The entrepreneur has to be trustworthy”.

We notice what MacMillan et al. (1985:119) mention in their study on VC decision-making criteria holds true for the majority of BAs as well, “There is no question that irrespective of the horse (product), horse race (market), or odds (financial criteria), it is the jockey (entrepreneur) who fundamentally determines whether the venture capitalists will place a bet at all”.

6.4.3.2 Business Idea and Market
The second most frequently listed criteria are attributes concerning the product or service that the entrepreneur intends to commercialize. From an academic perspective, several researchers suggest that BAs attach significant value to the uniqueness, innovativeness and the quality of the product or service (Landström, 1998; Lindsay, 2004; Mason & Harrison,
2003; Mason & Stark, 2004; Van Osnabrugge & Robinson, 2000). Accordingly, Parhankangas and Ehrlich (2013) connote that by promoting the innovativeness of their ventures, entrepreneurs may put themselves in a favourable position to attract informal investors, who are not interested in me-too products or products lacking a unique selling proposition (USP) (Van Osnabrugge & Robinson, 2000).

To be attracted to invest, BAs need to understand how the product or service is distinctive or superior to that of the competition and how any competitive advantage can be sustained (Mason & Harrison, 2004). Clearly, the competitive environment directly impacts the size, growth and accessibility of the market (Feeney et al., 1999). Interestingly, BAs seem to place little importance to proprietary rights or the industry sector. Mason and Harrison (1996b) suggest that the industry sector in which the venture operates is relevant to investors in 24 per cent of the cases studied. Thus the authors find only around one third of investments (35 per cent) is made in ventures operating in sectors familiar to the investor (Mason and Harrison, 1996b). Rather, BAs place much more emphasis on the growth and sales potential (Van Osnabrugge & Robinson, 2000). Market and product potential are certainly vital to the BAs evaluation, and identifying a growth market is of great importance since “early birds are not always winners in product markets, but late comers are almost always losers” (Sahlman & Stevenson, 1985:97). In their study of deals rejected by an investment syndicate, Mason and Harrison (1996b) find that market-related issues are the most frequent deal killers, accounting for the rejection of 47 per cent of investment opportunities.

6.4.3.3 Financial and Investment

In chapter 6.3 we have shown how the outlook for a high financial return on investment primarily motivates BAs. However, short-term economic returns are only of minor importance for the BAs assessment. BAs are well aware that by investing in early-stage ventures their money will be committed for the next 4-7 years, if not lost in the meanwhile (Landström, 1998; Mason & Harrison, 2002b). Feeney et al. (1999) imply that the majority of BAs expect a ROI of between 20-40 per cent depending on the stage the venture is currently in and the size of the investment. Being able to sell their equity stake at some point in time is important to BAs and they usually expect the entrepreneur to have a reasonable exit strategy at hand. Given the legislation-based difficulties with liquefying shares in closely held companies, a convincing investment proposal needs to identify means by which the investor can realize potential gains (Feeney et al., 1999).
Notwithstanding, BAs are putting little effort on the financials and are unlikely to make any return calculations based on the projected statements provided by the entrepreneur (Mason & Rogers, 1997). Instead, BAs rely more on subjective factors and gut instinct that if the investment succeeds, it will succeed very well (Van Osnabrugge & Robinson, 2000).

Prior studies predominantly find that BAs are deterred from investing if they identify the financial projections to be flawed or unrealistic (Mason & Harrison, 1996b; Van Osnabrugge & Robinson, 2000; Mason, 2008). Additionally, Feeney et al. (1999) note that undercapitalized ventures and a lack of owner’s equity as problematic. BAs are attracted by ventures with low initial capital expenditures (CAPEX) and the ability to break even without obtaining additional funding (Van Osnabrugge & Robinson, 2000). In most of the ventures typically funded by BAs the lack of financial controls and accurate accounts is one of the great weaknesses. A lack of trust in the entrepreneur’s ability to manage the day-to-day financial planning is commonly accepted to be a major concern for the investor (Van Osnabrugge, 1998). Following Mason and Harrison (1996a), investors request information on the financial structure of the venture, notably cash flow and profit and loss (P&L) forecasts. Furthermore, research by Van Osnabrugge (1998) suggests that BAs are concerned about the size of the investment sought by an entrepreneur, with 55 per cent agreeing that this was important to them. Factors related to valuation and equity stake offered are only of limited significance as reasons to reject a deal (Mason & Harrison, 1996b).

6.4.3.4 Miscellaneous: Business Plan
Business plans play a central role in raising capital from BAs. More than 75 per cent of investors require seeing a business plan before making an investment decision and only a small fraction of BAs places little or no emphasis on it (Mason & Harrison, 1996b). While many studies agree that a comprehensive and realistic business plan is essential to attract funds from informal investors, it must be highlighted that many investor are sceptical about the value of business projections based on prior negative experiences with business plans presenting overly optimistic and naïve projections (Mason & Harrison, 1996b; Van Osnabrugge & Robinson, 2000). On this notion, Feeney et al. (1999) add that business plans which are: providing insufficient information, poorly written, incomplete or vague are seen as major weakness by BAs. In alignment to this Van Osnabrugge and Robinson (2000:134) advocate for short and concise business plans that are, “getting straight to the point, as briefly as possible summarizing the product, credentials of the management team, the financing sought and reasons why, the achievements of the venture to date, expected
milestones, and exit strategies.” For many BAs the business plan acts as a reflection of the entrepreneur and his attributes and thus has a direct influence on the evaluation of his entrepreneurial capabilities.

It is widely recognised that no more than 5 per cent of investment proposals make it through the detailed investigation stage to proceed to the negotiation and contracting phase (Mason, 2008).

6.4.4 Negotiation and Contracting

Once the BA has performed the evaluation and decided – at least in principle – to invest into a venture both the entrepreneur and the investor need to negotiate the terms of the investment. During this step three main subjects need to be discussed, namely valuation, deal structure and terms and conditions of the investment (Mason, 2008). Whilst negotiating the valuation of the venture is a vital part of this process BAs tend to be less rigorous than venture capitalists. In many cases, BAs prefer to manage potential risks by getting involved in the entrepreneurial process and building a long-term relationship with the entrepreneur (Van Osnabrugge & Robinson, 2000; Mason, 2008). Despite, in a study by Riding et al. (1993) 50 per cent of the investment opportunities entering the negotiation and contracting stage are not executed.

According to Mason and Harrison (2002b) the most frequently cited reason to terminate negotiations is the difficulty in agreeing on a fair valuation of the venture that is acceptable for both parties. This is often reflected in the unrealistic projections entrepreneurs present in their business plans (see Chapter 6.4.3.4). The underlying problem is the challenge of valuing new and early-stage businesses that may only have intangible assets (e.g. intellectual property) and lack historic financial data to make grounded projections on future earnings (Mason, 2008; Van Osnabrugge & Robinson, 2000). Thus, methods of pricing and calculating the size of shareholdings in start-ups and early-stage ventures are remarkably imprecise and subjective (Mason and Harrison, 1996b).

14 Please note that the information presented on the negotiation and contracting stage is on a rather superficial level as this stage is of minor relevance for the crowdfunder (see Chapter 8.1). For more detailed information on contracting and negotiation please see Mason (2008:21ff.) and Van Osnabrugge and Robinson (2000:17ff.).
Taken as a whole, BAs rarely spend more than three months on the investment process, from meeting the entrepreneur for the first time until the decision to invest. In fact, according to a study by Mason and Harrison (1996b) in almost 50 per cent of the studied cases the elapsed time was less than one month.

In their recent research report on UK-based BA investing, Wiltbank (2009) quantify the typical equity-share acquired by BAs at 8 per cent. Only 10 per cent of the investments acquired 20 per cent of the ventures equity. Pre-money valuation was less than 2.5 million pounds in 85 per cent of the cases and 82 per cent had a post-money valuation of less than 3 million pounds. More than 50 per cent of the investments had no revenues at the time of the investment, so they can be categorized as very early-stage investments. Given the informality of the BA market, data on the investment behaviour of BAs is not generalizable and has to be treated with caution. Several studies have quantified similar data and although the results indicate that BAs prefer minority shareholding, discrepancies can be significant (Ehrlich et al., 1994; Mason & Harrison, 2006a; Haar et al., 2008; Van Osnabrugge, 1998; Coveney, 1996).

6.4.5 Post Investment

Next to providing capital one of the distinguishing features of BAs is the “value-added” component they bring to the investee ventures (Coveney & Moore, 1998). BAs are generally actively involved with the businesses they invest in by offering their skills, knowledge and experience in the form of post-investment involvement (Mason & Harrison, 1996a; Politis & Landström, 2002; Ardichvili et al., 2003). Their motivation is to nurture their personal interest in entrepreneurship and to protect their investment through active involvement (Kelly & Hay, 2003; Sætre, 2003). Based on results from Coveney and Moore (1998) in 48 per cent of the studied cases BAs indicate that their experience and expertise was the primary non-financial resource they bring to the ventures and in around 30 per cent of the cases BAs take on managerial roles. This suggests that nearly 80 per cent of investors get involved actively in the ventures they invested in, which is also confirmed by a study conducted by Macht (2007). For BAs who are highly active in the investee company Sætre (2003) coined the term “financial entrepreneurs” describing that some BAs become so engaged in the venture that they act as entrepreneurs.

15 Wiltbank’s study (2009) is based on data derived from 158 angel investors, who had cumulatively invested GBP 134 million into 1,080 angel investments and experienced 406 exits from those investments.
Active BAs can be beneficial to the venture in several ways. In the case the BA has relevant experiences from the industry, the new venture can leverage these experiences in the form of networks, strategic advice, market and business intelligence, as part of the board of directors and above all leveraging the endorsement as a signal of quality to customers and later-stage investors (Van Osnabrugge & Robinson, 2000; Mason, 2008). Madill et al. (2005) show that the involvement of active BAs improves the chance of raising venture capital at a later stage. In their sample 57 per cent of companies backed by BAs had also received funding from institutional venture capitalists. In contrast, only 10 per cent of companies that had not been received angel investments qualified for venture capital (Madill et al., 2005).

According to Harrison and Mason (1996a), BAs and entrepreneurs should be aware that conflicts could arise as part of the relationship. According to Coveney and Moore (1998) in 83 per cent of all studied cases the BA-entrepreneur relationship was described as positive with only a minority of 11 per cent confiding their relationship was negative. BAs and entrepreneurs can benefit from each other in several ways and create mutually valuable relationships. The entrepreneur by getting advice, networks and finance and the BA the opportunity of prolonging his career in the entrepreneurial space and by having a chance of financial reward (Madill et al., 2005; Politis & Landström, 2002). Mason (2008) argues that most business have angels derived fun and enjoyment from their investments, but only in the cases when an investment was successful. The feeling of helping someone, fun and enjoyment is not a compensation for financial loss.

6.4.6 Harvesting

Previous research reveals that BAs usually do not have concrete exit plans at the time they commit to an investment (Harrison & Mason, 1992a; Mason & Harrison, 1996a; Atkin & Esiri, 1993; Landström, 1993). Van Osnabrugge and Robinson (2000) explain this lack of focus by referring to the highly insecure nature of early-stage investments and by pointing out that exit routes become a concern a few years down the road when exit scenarios become more realistic.

For their study on German BAs, Stedler and Peters (2010) indicate that trade sales (54 per cent), flotation (45 per cent) and sale to founder (24 per cent) are the three preferred exit routes. To our best knowledge only four studies have aimed to capture the investment returns of BAs: A small-scale Finnish study (Lumme et al, 1998), two larger UK-based studies (Mason & Harrison, 2002b; Wiltbank, 2009) and a US-based study (Wiltbank &
Boeker, 2007). The findings clearly indicate the highly skewed distribution of returns. For Mason and Harrison's (2002b) UK-based study 40 per cent of investments make a loss (34 per cent a total loss), and another 13 per cent only achieve break-even or bank-level returns. Nonetheless, there is a significant subset of investments, around 23 per cent in total, which generates internal rates of return (IRRs) exceeding 50 per cent. Similar results are found by Wiltbank (2009), indicating that the majority of investment suffers a loss or total loss (56 per cent), while 44 per cent of exits are at substantial yields with an mean multiple of 2.2 or 22 per cent IRR for a holding period of 3.6 years.

7 ANALYSIS VOL. I: INSIGHTS ON CROWDINVESTORS

We begin this chapter by shedding some light on the investor profiles in our sample. This provides the reader with a good understanding of whom we interviewed and of the implications for our findings. Next we present our insights on the crowdinvestors' financial and non-financial motives. The two chapters form a seamless foundation to enter into the detailed presentation of the actual investment process and criteria presented in chapter 8.

7.1 Investor Profile

In the following chapter we present our findings on the characteristics of crowdinvestors included in our sample. This is not an attempt to construct a typology of crowdinvestors. Through our analysis it became clear that friends and family investors are not crowdinvestors. Arguments explicating this delimitation are provided in chapter 7.1.1.

The crowdinvestor can be characterized as a venturesome individual who knowingly bears very high risk when investing in start-ups. Contrary to BAs, a well-studied source of informal capital, we find that crowdinvestors are not primarily investing to earn a high return on their invested capital (Van Osnabrugge & Robinson, 2000). Similar to BAs the majority of investors are well educated (Stedler & Peters, 2010; Feeney & Riding, 1998). Our sample covers a plethora of individuals holding MBAs, technical and financial university degrees. Many of the interviewed crowdinvestors are either entrepreneurs themselves or are in one way or another affiliated with entrepreneurship. The remaining investors are mostly employed in the private sector within finance, marketing or technology. Only one of the interviewees was a student.
The vast majority has experience with investments on the stock market. In total four
interviewees have been involved in large-scale informal investments in the past and can be
classified as professional or accredited investors. In alignment with statistics provided by
different platforms the typical crowdinvestor in our study is male (85 per cent). Seedrs, for
example, published numbers on their investor crowd indicating that only one out of four
investors are female (25 per cent) (Seedrs, 2014a). This does not come as a surprise
bearing in mind other sources of informal capital have traditionally been dominated by men.
This disparity is often explained by the different risk profiles of the different genders (e.g.
Bajtelsmit et al., 1996; Borghans et al., 2009). A consistent finding across studies on BAs is
that typically less than 20 per cent of all investors are female (Becker-Blease & Sohl, 2005;
CVR, 2013; Mason & Harrison, 1994).

The investment behavior among crowdinvestors is quite heterogeneous. While the larger part
of our sample invests in the range of EUR 200-500 per investment, it also covers individuals
investing up to EUR 7500 on a single investment. A similar picture can be drawn when
reviewing the information received on investment portfolios. While the smallest portfolio
consisted of one investment only, some crowdinvestors manage portfolios with up to 48
investments with the median portfolio of 6 investments.

7.1.1 Why Family and Friend Investors Are Not Crowdinvestors
Our analysis revealed that FF investors engage in crowdinvesting due to their personal
affiliation with the entrepreneur. Hence, their investment process and motivation differs
significantly from what we define as crowdinvestors in our study. Uniformly, FF investors
confide that their investment is a one-time experience and none of the investors intends to
engage with concept of crowdinvesting going forward. Contrary to crowdinvestors, FF
investors are not driven by an interest in entrepreneurship. Their involvement in
crowdinvesting is a result of a call – direct or indirect communication from a person that they
are familiar with and whom they trust based on a pre-existing relation. Their primary
motivation is to help the friend, which makes their contribution resemble a donation more
than an actual investment.
7.2 Investor Motives

For entrepreneurs preparing their ventures for the funding process on a crowdinvesting platform an understanding of what motivates crowdinvestors to invest is vital. We know from prior research on BA investment theory that the investors’ motivation to invest in entrepreneurial ventures ultimately influences his/her particular investment criteria (see Figure 5; Van Osnabrugge & Robinson, 2000:116).

The following chapter presents our findings divided in two categories: financial and non-financial motives. Our results on the motives of crowdinvestors exhibit a remarkable consistency across the sample suggesting that non-financial motives are at least as important as the opportunity of financial gain and hence can be seen as a strong motivation to invest. In fact, many of the interviewed crowdinvestors state that given the high-risk nature of the investment they do not expect to make a profit from their investment, although all share the hope of doing so. For instance, FP (l. 772) summarized his motivation as an investor in the following way, “50/50 I would say. The chance of making a return on investment accounts for 50 per cent of my motivation and the other 50 per cent is the chance of supporting an interesting business and to get to know new products and ideas”.

7.2.1 Financial Motives

Our insights on financial motives are structured in two main items: Return on investment and tax-related benefits.

7.2.1.1 Return on Investment

Considering the high-risk nature of the investment one would assume that the prospect of above-average financial returns is the primary driving force behind the phenomenon of crowdinvesting similar to VCs and BAs (Feeney et al., 1999). Our insights on crowdinvestors’ motives and principles to invest draw a slightly different picture. For the majority of investors the idea of investing in a start-up in order to make a profit by reselling the shares at a later stage is not the primary reason to invest. A return on investment is certainly part of it, but it is lower down the list of reasons of why they invest than many entrepreneurs might suspect.

In fact, many of our interviewees state that they tend to write off the money channelled into this investment vehicle. This is not to say crowdinvestors are not intending to earn money

\[16\] Please note that the order of items listed under financial and non-financial motives is not a representation of descending importance.
from their investment. For them profiting financially would be regarded as a welcomed side effect rather than an expected outcome. The majority states that they were not planning to earn money, but neither do they want to make a loss, which clearly distinguishes the investment from a donation. Although they disconnect from the invested money crowdinvestors still expect the utmost from the entrepreneur to build a successful business.

Crowdinvestors do understand the risks involved in investing in early-stage ventures and they have realistic assumptions in terms of prospective financial return on their investment, especially given the circumstances of the comparably low investment sums. We are implying that crowdinvestors make conscious investment decisions. For instance, NH stated, “I have a long-term expectation. I mean for me mentally the money is gone in the sense that it is out of reach [i.e. illiquid, added by authors]. I do not expect to get it. I would really like to help see it grow, but it is written out of my books” and KG summarized his expectation as follows, “If in the end I break even I am more than happy with my investments” (NH, l. 2296; KG, l. 3390). An interesting observation is that crowdinvestors spread their investment across several start-ups to diversify their portfolios.

7.2.1.2 Tax-relief
Next to return on investment, potential tax-benefits must be considered as a financial motive. Based on current legislation only UK-based crowdinvestors investing on UK-based platforms, e.g. Seedrs and Crowdcube, are eligible to receive a tax relief based on two tax relief schemes named EIS and SEIS if they invest in eligible start-ups (see Chapter 4.3.1). Given these circumstances we only interviewed three UK-based investors on this particular subject. All three investors are delighted by the fact that their investments are tax deductible. According to their feedback the tax relief scheme does not only have a positive impact on the overall amount invested - it also incentivizes them to invest more often and to continuously seek out for suitable investment opportunities.

Two investors acknowledge tax benefits to be one of the initial factors drawing their interest to crowdinvesting. Uniformly, tax benefits are considered to reduce the riskiness of the investment, while the upsides at the same time remain with the investor. PE (l.1711) told us, “I mean I love it to be SEISed to be honest – because it gives me 50 per cent back and if the business flops I can claim back the other 50 per cent. So this gives me a lot of security for the investment. The EIS is less, but you still get some kick-back on the tax front.”
Remarkably all crowdinvestors stated that tax-reliefs do not influence their investment decision as long as the investment is eligible for either of the two tax-relief schemes. This is interesting because SEIS offers a tax deduction of up to 50 per cent from income tax, compared to EIS offering a tax-relief of 30 per cent. However, the interviewees pointed out that they would only invest into a start-up not providing tax relief if the investment opportunity is perceived as exceptionally attractive. This suggests that tax benefits are an important incentive to make crowd investment.

7.2.2 Non-Financial Motives

The following chapter presents our insights on the non-financial motives of crowdinvestors. Similar to BAs, the non-financial component of the motivation is essential to explain why crowdinvestors invest in highly risky early-stage ventures. The inventory of non-financial motives is fairly diverse and the list below aims at capturing the essence of factors mentioned during the interviews.

7.2.2.1 Fun and Satisfaction of Supporting Entrepreneurs

The bulk of crowdinvestors invest in early-stage ventures because for them it is fun and satisfying to engage in the entrepreneurial sphere. Crowdinvestors want to support passionate entrepreneurs to build their ventures, strengthen the economic profile of a region or to empower minorities to receive funding.

Though differences exist in the way crowdinvestors define fun, the “fun factor” is inseparable from the investment experience. For KG, fun is meeting with entrepreneurs personally, “For me it’s mainly about the fun of engaging in the entrepreneurial community […]” (KG, l.3386). For AN, fun is a feeling of support, “I feel that I sort of fulfill someone else’s dream” (AN, l.294). And finally, fun can also be the excitement of following the investment with the vision to yield a return as exemplified by PE, “It is exciting I am a gambler of nature so I like to gamble on everything […] and I am satisfied that I have invested my money in something that might give me a long time return” (PE, l.4602).

On an ideological level, some crowdinvestors told us it is a privilege to be an investor working at the disruptive edge of ideas that could change the world. Many of the interviewees believe that entrepreneurism is the embodiment of creating a newer, better world for future generations and a great way to disrupt the way long-established industries, such as banking, have been operating. With crowdinvesting they are given the chance to invest in young start-ups matching their own preferences and personal values. The majority of investors are well aware of the importance of entrepreneurism for economic development and growth and the
advancement of society. This means those investors see the broad impact of their investment and the idea of potentially contributing to this development in itself is perceived as a valuable reward.

TL told us, “It makes me happy to help a project. I am not necessarily looking for profits in the short term or not even in the long term. What I am enjoying in this thing is more the creation of an alliance with some people I trust and some ideas I like and getting a chance to be part of an adventure, like a very tiny part of it, but at least a part of it. So it is more, like fun, because the right way to think about it is me investing in my future, meaning that it will be fun for me to look at it maybe 10 years in the future and see what came out of that. I am putting a tiny piece of myself in the bottle that I will be able to open ten years from now and that’s exciting. It may have disappeared, it may be big and very successful and I will remember the time I made the decision and I think that’s what I am true to when investing in those companies.” (TL, l. 3172) and PS concluded by saying, “[...] here I expect a higher return on fun” (PS, l. 2762).

7.2.2.2 Playing a Role in the Entrepreneurial Process

Next to supporting entrepreneurs to build their businesses, playing an active role in the entrepreneurial process was mentioned as a highly influential motivation by many investors. Being involved in the creation of a business is something a few investors have done successfully as entrepreneurs themselves, or have always envisioned to do at some point in their lives. For many investors fun of entrepreneurial activity is a motive to engage with the ventures they fund. Many crowdinvestors underlined their inherent problem-solving attitude and the pleasure they derive from making things better.

The majority of crowdinvestors are willing to contribute their expertise and actively engage with the venture by advising, mentoring and/or providing access to valuable contacts in their network. Enjoying involvement in the entrepreneurial process is a common element among investors and something that excites them greatly. NH mentioned, “And I was sort of on the look-out for opportunities to get more active in the company and to be a part of it”, and AN highlighted, “ [...] the main goal for the entrepreneur is to understand that I can help them grow their company and this is like being a part of something that will be very big [...]” (NH, l. 2020; AN l. 242). This is not solely to support the entrepreneur to build a successful business, but also an appreciated opportunity to stay connected to the entrepreneurial sphere, to learn from challenges entrepreneurs face during business development, to get a deeper understanding of how successful start-ups are managed and in general to get
introduced to new and exciting ideas and technologies. What a large share of investors seeks is the participation in an exciting adventure of building a start-up and it is the challenge and experience that is appealing to them. The following quote recapitulates our findings accurately, “You get a bit more involved with the company and you get a little bit more the feel of […] it’s pretty much like nurturing a kid. Everyone needs to start from somewhere and life is not all about making money and profit. Sometimes, it is really just about enjoying a journey together, see more new things, investigate new things, to be curious. And I think crowdinvesting allows that – really allows that.” (KNZ, l.1867). And on his LinkedIn profile KNZ uses his crowdinvesting activity to promote himself as a start-up advisor, “Avid technology start up supporter. I am involved in a multitude of start-ups and enjoy an advisory role in helping entrepreneurs troubleshoot and bounce ideas.” This relates to the following non-financial motive.

7.2.2.3 Extending the Professional Network

Finally, a few investors brought up the chance of extending ones social and professional network as an additional motivation. Indeed, since many individuals are gathered around the same project, it is a great possibility to establish relationships. This insight may not be surprising since all crowdinvestors from the platforms Seedmatch and Seedrs (11 of 20 interviews) have their professional profiles linked to their investor account. This can be interpreted as an indication for the motivation of extending one’s professional network. This may have implications for our analysis and the potential bias has been stated in chapter 4.7. However, we must note that investors contacted by other means than social media also mentioned the intention of extending their personal network. KNZ, confided, “And then the second [motivation; added by authors] is that I only invest in start-ups where I also think it will enhance my network – so businesses very close to digital strategies.” (KNZ, l.1304). This motive plays a central role in explaining the community aspect of crowdinvesting as well as the post-investment engagement of investors. The intellectual exchange of ideas between entrepreneur and investors is regarded as a key element of the experience. For some crowdinvestors in our sample this includes calling the entrepreneur(s) on a regular basis, to meet with the entrepreneur(s) for lunch or visiting the start-up at their office. The importance of personal relationships was explained by CI (l.479) as follows, “I think that’s actually the best part, the CEO of the solar tile manufacturer I just met him last week. He was in London so I met him there and it was just really cool to hear first hand. Those entrepreneurs are

17 Uk-based crowdinvestors were contacted via the business network LinkedIn and the German crowdinvestors via the equivalent in Germany, named Xing.
always super excited about their products and happy to tell anything like the difficulties they are having, the next big thing coming up.”

7.2.2.4 Summary
Crowdinvestors’ motives to actively participate on crowdinvesting platforms are diverse and eclectic. Our results suggest that financial and non-financial motives are inextricable when explaining crowdinvestors’ decision-making. We suggest that for the vast majority crowdinvesting entails more than money – for them it is a gratifying experience.

Being equipped with a thorough understanding of investor motives we are prepared to enter into the analysis of the actual investment process starting with ‘screening’ and ending with the stage called ‘harvesting’.

8 ANALYSIS VOL. II: CROWDINVESTORS’ DECISION-MAKING PROCESS AND CRITERIA
To provide a sound foundation for the subsequent analysis chapters, we start by introducing a model of crowdinvestors decision-making process. The following chapters are structured in accordance to the process introduced in chapter 8.1.

8.1 Decision-Making Process
Crowdinvestors’ investment process, as illustrated below, can be systemized into five distinctive stages: Screening, Evaluation, Investment, Post-investment and Harvesting. This process is grounded on feedback from the majority of our interviewees. Nonetheless, the linearity of the illustration should not be misconceived. Occasionally, the process includes feedback-loops, the jumping of a particular stage or adding-on of a new stage. The boundaries between the stages are rather fluid caused by the generally quick decision-making. In chapter 5.3.3, we introduced the overall crowdinvesting process and this chapter can be comprehended as a detailed study of “Investment” and “Post-Investment” (stages three and five) from a crowdinvestor’s perspective.

Figure 6: Crowdinvestors’ Decision-Making Process (Own illustration based on insights gathered through our analysis and with inspiration from von Osnabrugge & Robinson (2000:116))
The **screening phase** is defined as the process of locating interesting investment opportunities on a platform. By clicking on a particular campaign the investors signal interest in the opportunity and moves into the evaluation stage. During the **evaluation stage** the investor accesses the information provided in the proposal, performs some form of due diligence, asks questions in the forum and watches the video. Investors appear to conduct this phase with varying levels of thoroughness.

If the proposal passes the individual evaluation process and the investor decides to invest he will have to decide on the **investment size** and agree to the terms & conditions of the deal. From an investors’ point of view the post-investment phase starts right after the investment has taken place. **Post-investment** is defined as the contractual relationship between the entrepreneur and investor over the lifespan of the investment (i.e. the time until exit or insolvency). **Harvesting or exit** takes place when the investors liquidate their investment by earning dividends or by reselling their shares to a third party.

The final stage in the process, harvesting or exit, has been blurred out in Figure 6. To our best knowledge none of the ventures funded via crowdinvesting has had a successful exit to the time of this writing\(^\text{15}\). With the background knowledge that BAs normally hold their investments for more than 4 years before exiting and considering the infancy of the industry, this circumstance is not surprising. Specific scenarios in which the investor will be able to liquidate the investment exist: Either another company is acquiring the venture, or it floats on a stock exchange. On rare occasions the crowdinvestor may be able to sell his/her shares to a private buyer. In addition, any dividends paid by the venture are being allocated to the investors (Seedrs, 2014a).

When comparing this process to the commonly applied process by BAs (see Chapter 6.4) some key differences are evident: The ease of crowdinvesting is achieved by “outsourcing” the time consuming and costly procedures, which BAs normally have to master, to the platform operators. Throughout the subsequent chapters we will learn more about these fundamental iterations in the process and the crowdinvestors’ decision-making in depth. The key differences in the processes are as follows:

\(^{15}\) 15th of March 2014.
1. **No Deal Origination:** Platform providers are in charge of the initial step of the process by attracting interesting and high-quality start-ups to run a crowdinvesting campaign on their platform. The responsibility of platforms is to review all information provided by the start-up to ensure it is reasonable and not misleading. After approval by the platform the campaign goes live for a limited funding period (usually between 30-60 days). For platforms the challenge is to provide crowdinvestors with a steady deal-flow without compromising their quality standards of ventures to be featured on the site.

2. **No Negotiation and Contracting:** Probably the most significant distinction of crowdinvesting to BA-investing is the absence of negotiation and contracting between the investee and investor. This assignment is handled by the platforms and involves more or less standardized contracts. Before starting their campaign, each start-up decides on how much money to raise and determine the share of equity offered in return. Logically, the investor’s acquires an equity percentage in proportion to the size of his/her investment. Thus, the valuation of the company is set and non-negotiable – i.e. the investment opportunity is presented on a “take-it-or-leave-it” basis.

3. **Platforms as intermediaries:** Unlike in BA-investing, crowdinvesting transactions rely on crowdinvesting portals as intermediaries. Among other things, the crowdinvesting portals offer standardized financial contracts to the issuer, provide marketing and business guidance to the entrepreneur, and offer an investor network by advertising the securities on the portal’s website and by regularly sending out newsletters. And they also perform some basic due diligence to ensure the entrepreneur is credible (Hornuf & Schwienbacher, 2014).

4. **Online-based investment:** We identify the online-based nature of crowdinvesting as an overarching distinction to BA investment decision-making. This has a bearing on all stages of the process and plays a vital role throughout the analysis.
8.2 Screening Investment Opportunities

In this chapter, insights on how investors locate and screen investment opportunities are presented. Investors normally locate investment opportunities via three channels: by actively accessing the platform(s) (the most common approach), reading platforms’ regular newsletter updates or other Internet media and referrals.

The ‘screening phase’ describes how investors identify the interesting projects among a multitude of investment opportunities. During the screening phase crowdfunders quickly scan the investment opportunities featured on a crowdfunding platform and based on the basic information accessible without clicking on the campaign the investor decides whether or not to look at an opportunity in more detail. This process is usually performed very quickly. The majority of investors is selective in their approach and has implemented personal screening systems, which they utilize to select the interesting campaigns.

Increasing popularity of crowdfunding has led to a constantly growing number of entrepreneurs deciding to run a funding round via crowdfunding. The result is that platforms are featuring many investment opportunities at the same time, which challenges the investor to get an overview of the current investment opportunities. As a preparation to our interview, PS looked at his preferred platform CrowdCube and counted a total of 42 active campaigns at that point in time. As a consequence he has applies a screening system where he focuses on “cleantech, ecology or good, crazy ideas” (PS, l.2613). Our analysis suggests that several investors have similar screening methods, which they utilize when browsing through the campaigns. The screening system can be described as a practical tool that crowdfunders utilize to structure their search and to safe time. TK (l.5643) explained, “[…] I go for the things that I feel are interesting and I would probably go for tech or media, because that’s just where my interests are, but I also go after other projects“.

CI told us that he avoids businesses he does not know anything about or where he does not immediately see the potential. In his case this implies staying away from fashion, new social networks or retail products such as soft drinks where barriers to market entry are high. Contrary, PE applies a very different approach. Instead of looking for products that he finds interesting the first filter he applies is to search for campaigns that are funding quickly. His logic is that other people who have already invested did their groundwork and he just needs to jump on the bandwagon. This is often referred to as relying on the ‘wisdom of the crowd’ (see Chapter 8.3.4.2). He described his screening process as follows, “[…] I will look for
businesses that are funding quickly [trending], and if they are raising money quickly and getting towards overfunding then I will have a look at them […]. So I say other people have done their groundwork and I will just jump on the back of it.” (PE, l.4669).

Overall, the way crowdinvestors locate investment opportunities is fundamentally different to deal sourcing processes by BAs (see Chapter 6.4.1). However, during recent years BAs have also moved more of these activities online (Nesta, 2013).

8.2.1 Summary
Crowdinvestors are selective when deciding which of the investment opportunities they will examine in more detail. Similar to BAs investors tend to pre-select investment opportunities, which will be examined in more detail afterwards. Despite the screening process being very quick it is based on conscious decisions guided by personal preferences for business ideas and sectors of interest to the investor.

8.3 Evaluation Stage
In the evaluation stage investors assess the investment opportunity in more detail. This may include watching the video pitch, reading the business plan, looking at the financial details and performing very basic due diligence. The thoroughness displayed by investors during this stage varies significantly between individual cases. For some this may include 10 minutes to scan the information and for others this can take up to 3 weeks. However, during our analysis it became clear that crowdinvestors' barely perform due diligence. This is a sharp contrast to what we know from BA theory (see Chapter 6.1). AN (l.168) for example stated, “I do not do any due diligence almost”, TL (l.3143) pointed out, “But I did not do my due diligence” alike TK who said, “I did not go into any kind of due diligence”. JD (l.3301) confided, “it [the evaluation] has nothing to do with due diligence, it’s based on pure gut feeling”, and KG (l.3301) was of the opinion that, “doing some kind of due diligence does not make any sense if you only invest below EUR 1000” and PS (l.2655) concluded, “so it is really that the threshold is so much lower now because I don't have to worry about due diligence that much”.

In one of their recent infographics on investment criteria of their investor pool, Seedrs quantifies that 89 per cent examine the idea, whereas 59 per cent of investors study the team before investing (Seedrs, 2014a). Although we did not statistically assess the weight of the different criteria in the crowdinvestors’ decision-making we come to a similar conclusion.
The list of investment criteria mentioned by the interviewees will be presented in the following order: First, criteria concerning the business idea and market characteristics, second criteria related to the entrepreneur and/or entrepreneurial team and last financial characteristics including exit strategy. Obviously, we draw inspiration from our insights on BA decision-making criteria presented in chapter 6.4.

8.3.1 The Business Idea and Market

The business idea is usually the first filter in the validation process. This is not overly surprising since the crowdinvesting happens in a digital space and the business idea is the first point of contact for the investor when reviewing investment opportunities. Crowdfunders have a tendency to invest in ventures they quickly understand and in products or services where they see the use case. In addition, it is important that they comprehend the problem the idea is solving. Furthermore, investors are trying to get a rough idea of the market potential.

Despite our interviews being conducted on a retrospect our interviewees were capable of defining their investment approach in considerable detail. Most notably the interviewees remembered the specific attributes of the product or service in-depth. In almost all cases the interviewee was clear about the problem the business idea was solving, its unique selling proposition (USP), its benefits and if it has been validated (proof-of-concept). From this we infer that despite the rather quick decision-making process, the majority of investors make sure they are well acquainted with the business idea before making an investment decision.

The following chapter is organized in two chapters, unique selling proposition and market. This reflects the themes, which occurred during our analysis.

8.3.1.1 Unique Selling Proposition

A unique selling proposition is an important consideration in crowdfunders' evaluation of the business idea. A clear and understandable USP catches investors’ attention and triggers interest for further review of the business. The lack of a compelling USP correspondingly decreases investor interest and most likely translates into cancellation of the investment process.

PS and NH both invested in a venture building an online community for female adventurers. Both evaluated this specific investment on its uniqueness in terms of selling and promoting experiences for women. PS strategically invested in female leadership, “The thing is we try to keep a profile on either clean-tech or something that has to do with female leadership –
women entrepreneurs. And whenever there is an opportunity like this on FundedByMe then for me it is about making a statement ‘I can choose were my money goes’ [...] I can pinpoint it to female entrepreneurship in Sweden and that’s really a surgical position” (PS, l.2438). NH added on to this preference by pointing out the ventures USP as a primary reasons to why he fell “in love with” the project “[...] that project just fit with so many other things I work for – gender equality and equal opportunities for women. I have a young daughter and she is also a little power girl and I felt this is exactly what she wanted to do with tough women driving motorbikes and snowboard and so. So I said this is ideal it combines: business, idea and fun and doing good for women – thinking about my daughter and getting some role models for her. So for me it was just immediately a pet project.” (NH, l. 2025; NH, l.2034).

While PS and NH evaluation of the ventures USP relies on emotional factors and the ventures ability to create social change, other crowdinvestors are more interested in the product innovation and the ability to disrupt existing markets. LH guides his investment decision by asking, “what prevents competitors to pass you in the first few months or first years in business?” (LH, l.3523). In this approach the main importance is that investors understand the product/service and the problem it solves. CI works with financial modeling of large scale energy investments (e.g. funding for new windmill or solar parks) and got excited when he came across an investment opportunity in a company producing unique solar PV rooftop tiles19, “[...] first thing I thought was – there is no way this has not been invented before [...]. And then I looked into it and their competitors [...] they did all have some substantial difference and no solution was as easy to implement and as easy to adapt to. That caught my interest” (CI, l.469). CI’s testimony gives evidence to the importance of the USP. Products lacking clear differentiation from competitors are exposed to competition and cannot be expected to perform well as an investment. Contrary, businesses creating a new market or occupying a niche are – at least in theory – more likely to succeed.

In contrast, a handful or our interviewees provided examples of investment opportunities they rejected due to the lack of a clear unique selling point. On two occasions, FP decided against participating in a funding round due to the product/service not being differentiated sufficiently from its competitors. His statement also underlines the importance of innovativeness to attract his interest as an investor, “I have not invested in the two companies, because for the

19 Solar PVs that are integrated into roof tiles eliminating the need for traditional solar panel modules, which is placed on top of a roof.
one company there is way too much competition and there is no real unique selling point for it. And in the payment service I simply did not invest, because I've seen that in the past many services of this kind failed in the first year. So that means I invest only if it really is something innovative, something that does not yet exist and where there are, in theory, high chances of positive customer feedback." (FP, l.681). On this notion LH (l.3521) mentioned two opportunities he rejected given a perceived lack of a USP, “So a nice example - on Seedmatch - were X and X [the two companies], where even the idea was not clear and what their unique selling proposition was.” These statements indicate that a consideration of the competitive landscape a venture taps into is important to many investors.

8.3.1.2 Market Characteristics and Scalability

Some crowdinvestors mentioned scalability and the market potential as an integral part of the business idea evaluation. Scalability is understood as the growth potential of the investment opportunity and is assessed as the ability to accommodate growth of the business idea.

KNZ repeatedly stated that scalability was the primary criteria for his investment decision. When encountered with a very scalable business model he spent only a few minutes deciding to invest GBP 2300, his largest single investment out of a total of 48 investments (KNZ, l.1497). He generally spent less time on evaluating the business and invested higher amounts in investment opportunities with a scalable business model, “the scalability – that’s always when I invest above 1000 pounds.” (KNZ, l.1374).

Next to scalability, competitive considerations were highlighted by some of our interviewees. AN, KNZ, FP and CI, mentioned that they pay attention to the competitive landscape of the business when they are evaluating investment opportunities. They have all dismissed investment opportunities where they perceived the competitive landscape to be challenging. CI told us that he prevents investments in businesses he does not understand and where the competition is fierce and barriers to entry high: “I stay away from retail products like drinks and such because there are companies out there spending millions and millions of dollars trying to find the next big drink, be that alcoholic drink or soda drink. And most of the products simply fail and I just feel that one startup trying to push one product out there with a little bit of capital probably has a lot lower of being successful” (CI, l.457).

Instead many investors prefer to invest into niche markets where customer acquisition cost is low and preferably where the business has good prospects for growth. FP pointed out that he is only looking for highly innovative products where there are high chances of positive
customer feedback and where there is a large target audience (FP, I.977). LH informed us that he had undertaken his own market analysis by asking his family, friends and colleagues if they needed a specific product that he was considering to invest in (LH, I.3565). KNZ explained that when the data provided in the business plan is not transparent, he would access market research databases like Euromonitor to get an idea on the market size.

8.3.2 Entrepreneur or Entrepreneurial Team Characteristics

After taking a closer look at the idea many crowdinvestors move into the assessment of the entrepreneur’s characteristics or attributes. Placing this criterion second certainly does not mean that the entrepreneurial team is less important than the idea. It just appears to be of lower importance in the very early stage of the process, where the majority of investors’ objective is to familiarize themselves with the idea. While this is a common characteristic across our sample, a minority unmistakably stated to foremost invest into the people behind the venture.

Our findings show that the investment decision is guided by the investors’ confidence in the entrepreneur or entrepreneurial team. For this purpose the campaign video must be highlighted as a critical ingredient to running a successful funding round. The following chapter commences by clarifying the importance of the video. Subsequently, we elaborate on the main findings organized in three categories: firstly management experience and track record, secondly trustworthiness and openness, and lastly personal motivation, passion and commitment.

8.3.2.1 The Overarching Importance of the Video

Throughout our interviews several investors have stated to watch the campaign video as the first entry point to the evaluation stage, as exemplified by MW (I. 3849), "first I watched the video and afterwards I looked at the other information provided in the campaign". Normally, the video summarizes the main points of the business plan. Optimally the entrepreneur (and his team) presents the information in an engaging way. This allows the investor to get a basic introduction to the business, but more importantly helps him/her to make sense of the people behind the project. A few investors made that point clear. For example OGG (I.4316) stated, "When you look at the video […] I think it is also about emotion, it is not only about the money. Its emotions that you believe in the team and decide “this guy will make it!” and PE highlighted, "[…] the one thing I will do is always to watch the video if I like the look of the person, the entrepreneur. You know it does not really give you much details about the entrepreneur, but it can generally generate an appeal for somebody who are watching them and the way they present.” Sometimes, making an investment decision is solely based on
watching the video. PE, a very unique investor within our sample, confided to invest impetuously meaning that he normally views the video and if he likes it the investment is transacted immediately. He outlined his investment process, "I normally just watch the video, download my money and that's it." (PE, l.4543). In many ways the video can be seen as a virtual pitch to potential investors, similar to an investor pitch an entrepreneur would go through when seeking money from BAs or VCs (Mason & Harrison, 2000). Therefore, entrepreneurs need to be aware of their target audience and how they convey their business idea comprehensively and in an engaging, passionate manner.

8.3.2.2 Management Experience and Track Record

Normally, the entry point to build confidence in the entrepreneurial team is to assess if the venture has a team in place encompassing the right capabilities and experiences to build and manage a successful business. The entrepreneur is not expected to be able to do everything, but crowdinvestors expect the entrepreneur to know what the shortcomings of the current team are, and what team members need to be added. Gaps in the management team are considered as problematic since hiring of adequate personnel is difficult and costly. On his evaluation of the entrepreneurial team LH noted, "Who is the team behind the project? That's always my second step and second most important criteria. Which know-how does the team encompass? From my experience as an entrepreneur I can say that next to a good idea you need a strong team. And there it is important to have the right capabilities in place without major gaps. If a young company has to hire a marketing or sales person to get business going that's very costly. And in this particular case the company had the right people on the team, a good developer, strong research team and an experienced sales guy. That was very convincing to me." (LH, l.3529).

In particular many crowdinvestors try to get an understanding if the team has previous experience in building a start-up or know-how within the business field. On this notion, SD put forward that he is often questioning if the entrepreneur has the capabilities and experiences of managing a fast growing business. Being an entrepreneur himself, SD understands the obstacles waiting along the way of scaling a business. Based on his prior experiences many entrepreneurs lack the managerial skills to professionalize their business operations in adaption to growth. In his opinion this represents the highest risk. He states, "There is a huge difference if you are managing a small business or a big one. I am often not sure if the entrepreneur has the required skills. But I honestly do not know how investors can be informed about it adequately. In my opinion, this is currently still the greatest risk whether the entrepreneur has what it needs to manage a company with increasing sales and
increasing complexity” (SD, I.5290). Likewise, LH highlighted that he needs to be confident that the entrepreneur is capable of managing a fast growing business without losing sight of the overall vision (LH, I.3522).

When we asked NH to share his top three investment criteria with us he listed them in the following order: idea, team and financials. Moreover, he elaborated on his assessment of the entrepreneurial team. His comprehensive explication is characteristic for the majority of investors, “Secondly the impression of the team, because in my mind if it is a strong team it will also be able to adapt an idea that needs to be revised […] If you have a strong team who know the vision they want to achieve, then it can adapt their product. If I can feel this is a team that want to work with investors, want to work with the markets, who are open for – let’s say – who know their own limitations and strength. That is a very important criterion – because then I am less worried if the idea is spot on at the first time. If the team is good they can make a bad idea into a good idea. The opposite is not true.” (NH, I.2130).

Regardless of the potential of the idea, crowdinvestors understand that it is the team who will be responsible to transform the idea into a viable business by constantly adapting the business model to changing demands. Many crowdinvestors mentioned to particularly take a closer look at previous experiences of the lead entrepreneur. Prior involvement in a start-up, both as founder or team member, is perceived as a strong signal for quality and thus increases the investors’ confidence.

Interestingly, when asked about their investment decision-making, none of the interviewees mentioned to look at the educational background of the founders, which is commonly argued to be a highly relevant decision-making criterion for BAs. Additionally, Ahlers et al. (2013) argue for a statistically significant empirical evidence of the percentage of people with MBAs among the founding team increasing the likelihood to successful funding. While our findings do not confound these results, we suggest that these factors may be less relevant in the context of crowdinvesting than assumed.

Our insights imply that the entrepreneurs' experience and management capabilities may not be the most decisive criteria to assess the quality of the entrepreneurial team. For many crowdinvestors the decision to invest or not to invest is based on his subjective impression of entrepreneurial attributes such as trustworthiness, openness, motivation and passion.
8.3.2.3 Trustworthiness and Openness

One of the challenges in crowdinvesting can be identified by the lack of face-to-face interaction between the entrepreneur and the investor. In the context of BA investment decision-making, an integral part of due diligence is to have several personal meetings with the entrepreneur (see Chapter 6.4.3). Given the virtual nature of crowdinvesting, this is typically not the case for crowdinvestors. How can investors evaluate the personality and competencies of the entrepreneur and founding team without meeting them in person? It is at least questionable if a short video is sufficient for investors to make sense of these highly intangible attributes. This argument is supported by the circumstance that many investors seek additional information on the entrepreneur and his team outside the crowdinvesting platform by examining their professional profiles (e.g. LinkedIn), the company website, call them or arrange a personal meeting.

NH, who invested multiple times into one particular venture, presented an interesting case. After his initial investment of EUR 500 NH connected with the lead entrepreneur and decided to meet her and the team in Sweden. Following the meeting and his good impression of the people, he decided to double his initial investment and to liaise with the lead entrepreneur. He explained this involvement helped him to build confidence in the team and that he got a clear view on their motivation and capabilities. Eventually, NH invested EUR 2000 in total, four times the amount of his initial investment (NH, l.2092).

During the analysis it became evident that those investors tend to seek a closer relationship if the company focuses on areas matching their professional background. During these meetings investors exchange ideas with the entrepreneur and not seldom offer to support the venture with their expertise. We find this interaction to be initiated during the funding round and it is often maintained as a part of the post-investment relationship (see Chapter 6.4.5). This behaviour is inherently linked to the motivational aspects highlighted in Chapter 6.3. One the one hand this engagement is highly exciting for the investor and a vital part of the experience. On the other hand it is perceived as a mutually beneficial relationship allowing the investor to extend his professional network, being part of an entrepreneurial venture and to provide the venture with valuable advice, which potentially nurtures his economic interest of making a return on his investment.

From the crowdinvestors’ perspective, each interaction between the entrepreneur and the crowdinvestor is an opportunity to build or breakdown trust. Research has shown that a lack
of trust in the entrepreneur radically curtails the level of BA investment activity (Coveney, 1996). Most of the interviewees agreed that trusting the entrepreneur is important to them. To assess the entrepreneur's trustworthiness crowdinvestors examine few information sources, predominantly the forum where investors post questions answered by the entrepreneur and the video, which is a mandatory component of the pitch in all platforms part of this study. Investors watching the video base their judgement on subjective appraisals. A few investors noted to utilize the video to see if they “like” the entrepreneur or team. LH (l.3368) for example told us, “This may sound funny, but I look at the photos of the team to see if they look likeable”.

Additionally, investors regularly use the forum to take a closer look at the quality and consistency of answers provided by the entrepreneur on inquiries sent by potential investors. We find that investors are not only sensitive to the quality of the response, but also to the response time. On this matter, LH clarified his point, “So I think the response time is very important and the quality of the answer. It is of no help when I get a quick but insufficient answer, but on the other hand waiting a long time for a feedback is a very bad sign, too.” (LH, l.3583). Generally, the investors agreed that if an entrepreneur is avoiding questions or if his answer is poor, he or she might not be trusted. Failing to listen to the question is problematic in its own right. In addition, entrepreneurs who appear to provide contradictory answers lose credibility and trust. A lack of trust would often cancel out any of the business idea’s merits, growth potential, or ROI potential in the minds of the crowdinvestors. The entrepreneur has to be trustworthy.

An interesting subject was pointed out by KNZ, who told us that he is cautious investing into one-person ventures and ventures founded by an entrepreneur who comes across as overconfident. Regarding the latter, KNZ recalls an example of a company where the founder appeared to be reluctant of taking on advice and suggestions proposed by KNZ. From this KNZ inferred that the entrepreneur was too confident that he got his business plan right and therefore believed he did not require any advice. Despite the entrepreneur not opening up to and engaging with the crowdinvestors, his company still succeeded in securing their first round of funding. The striking point is: when the same company started a second crowdinvesting campaign to secure follow-up funding a few month later KNZ contacted the entrepreneur asking for a more detailed breakdown of what the money will be used for (use of proceeds). Again, the entrepreneur failed to respond to his questions, which caused KNZ to publicly disclose his discomfort in the forum (KNZ, l.1786). The campaign failed to reach
its target in the second round. A case like this is interesting since it raises two questions: Did the wisdom of the crowd work come into effect and/or do crowdfunders learn from experience?

It seems that the crowdfunder not only lost confidence in the entrepreneur's ability to build a successful business, but also more importantly started questioning his trustworthiness. KNZ's reflection evokes the impression that crowdfunders learn from their investment experiences and continuously develop their approach based on learning effects. A study on the role of heuristics in crowdfunders' decision-making, similar to the study by Smith et al. (2010), could shed some light on these aspects.

Throughout the analysis it became more and more apparent that what we term as "openness", i.e. the entrepreneur's engagement with the crowdfunders, his ability to give convincing answers to questions posted in the forum and his approachability for personal meetings, directly impacts the level of trust. Not only does it build trust, it is essentially a means to create the kind of entrepreneurial experience most of the crowdfunders seek when they engage in crowdfunding – they want to be part of something special.

8.3.2.4 Entrepreneur’s Motivation, Passion and Commitment

During the analysis the pattern of interviewees pointing out the importance of the entrepreneur’s motivation emerged. Entrepreneurial motivation as a concept is relevant, because it defines why the entrepreneur is pursuing a particular business opportunity and reflects his ambition. Ambition influences the degree to which entrepreneurs seek to create something great, important, and significant when pursuing opportunities. The nature of the entrepreneurial ambition may include making money or the desire to create something new, from conception to actuality (Shane et al., 2003).

Next to motivation, an entrepreneur’s passion is certainly critical for many crowdfunders as it is often a good indication of an entrepreneur’s drive and willingness to work hard and to do his utmost to make his venture succeed. Furthermore, entrepreneurs who are committed to and passionate about their venture can be persuasive and the majority investors regard them as being more engaging and interesting. On that notion, NH (l.2108) stated, "But it grabs me most if I get this feeling of passion and an idea where I can feel the entrepreneur wants to achieve something, they want to do a thing that is different and better." Creating a company only works if one is passionate about it. Only then entrepreneurs will go through the demanding process and survive the downtime. If the entrepreneur is not passionate he/she
will quit at the time the first major problems occur. Although this has direct implications for the possibility of earning a return on investment in the long-term, we find that perceived passion is merely a measure to evaluate if they feel excited about the idea and of being part of this venture.

Again, KNZ provided an exciting case showcasing the power of entrepreneurial attributes such as passion and commitment in order to run a successful crowdinvesting campaign. In the interview KNZ stated that for this particular case, a musical show, he solely invested because the female lead entrepreneur who started the project was highly passionate about her idea and was very persuasive in communicating her vision and commitment throughout the funding round. This is also an example where KNZ scrapped his strategy of investing in scalable and innovative business ideas and decided to invest into the entrepreneur behind the project rather than the idea. He reasoned, "But on occasion you might invest into people – and a good example for my case was a musical [the venture]. I thought the idea or the concept she [the entrepreneur] was trying to sell there was about happiness or happy feelings [...]. For me it was like yeah it is interesting and the way the people spoke there – the passion around it – because I think the product was s***. I thought this was s*** because it is a play that is dependent on people filling up the theatres. The problem with plays is you never have a consistent volume. Volume will peak and drop due to how exciting the entertainment is. [...] But the reason I invested there is you know what, maybe it does not make a lot of money [...] But she was distributing a good message." (KNZ, l.1933).

While perceived passion has a positive effect on the investment decision, we found evidence that absence of this attribute is a strong deterrent to investment. In this regard PS elaborates on his evaluation of a entrepreneurial team that failed in demonstrating their motivation and passion convincingly, which caused him to shy away from investing, “It was not that I could find something and I was like ‘argh’ they are bad people, but I didn’t get this passion kick or sort of I want to team up with those people. So in that I would have felt to rush into something without getting the heart of it.” (PS, l.2263). The inseparability of motivation and action, i.e. investing in early-stage ventures, was constantly reoccurring during our analysis.

The final point in evaluating the entrepreneur and the team that was mentioned by a few interviewees concerns commitment. Entrepreneurial commitment is often interpreted in terms of financial resources contributed by the entrepreneur, or the entrepreneur having “skin in the game” (HBAN, 2012). Nonetheless, we find that some investors assess the entrepreneurs’
resource commitment in terms of time rather than money. A few investors stated to be sceptical if the entrepreneur – and his team – is not working on the business idea on a full-time basis. Committing full-time to starting a venture and maybe quitting a former employment is a strong signal to the investors. This uncompromised dedication on building a successful business is perceived as more important than putting private money at risk. Indirectly, investing one’s own time can be translated into spending money. On that score, PS recounted, “I always look for the person behind the project – who are they and what do they have to gain or to lose. If they are committed and saying this is our full-time thing and we need to make it within one year then they have a lot to win and a lot to lose. So when I look at the people it is also about are they committed in time? They do not need to put in a single dime themselves I don’t care if they are risking their own money. I mean if you are risking your own time you are risking your own money!” (PS, l.2752).

8.3.3 Financial Characteristics and Exit
Before presenting our findings we have to call to mind that the financial terms of the investment, particularly the ventures’ post-money valuation are non-negotiable for the crowdinvestors (see Chapter 8.1). This is one of the most critical differences of crowdinvesting compared to BA investments.

In this chapter we will reflect on our insights gathered on the leverage of financial details on the investment decision by crowdinvestors. During the interviews the most active discussions frequently concerned topics such as valuation and revenue forecasts. However, our findings suggest that financial characteristics of an opportunity are criteria of minor importance to crowdinvestors, usually ranked third behind idea and team. While financial details may not be primary criteria to accept or reject an opportunity, crowdinvestors utilize the information to reflect on the credibility and professionalism of the entrepreneur. Across our sample, investors critically reflected on unreasonable valuations and financial projections. However, only in severe cases investment opportunities where rejected if – apart from the financial details – the venture was appealing to the investor.

8.3.3.1 Financial Traction
When evaluating the financial characteristics of the deal at hand crowdinvestors look at different factors. First, crowdinvestors are interested in knowing what the venture has achieved so far, i.e. if the company has a working business model generating revenue. For investors this is part of assessing the upside potential of the opportunity and also a part of the risk assessment. CI (l.521), who works in private equity, elaborates on his approach to
assessing the financials of any given opportunity, “I would say that’s all a finger in the wind approach. I looked at it and to be honest there is too much uncertainty. If you look at the forecast in all of the pitches, all the companies are going to grow so fast and going to make so much money, big hockey stick analysis. The only thing that I compare is the one thing that I do like which is actually if they already make revenue. That’s a big plus, lots of revenue in its second or third operating year and if they have a lot of cash.” Correspondingly, KG stated to move his investment focus to ventures that showcase an existing business, which to his opinion reduces the risk of his investment significantly, “I think going forward I will put more focus on companies with traction and some proof of business. I don’t feel the very early stage companies will make it on crowdinvesting platforms in the future. It’s too much of a gamble.” (KG, l. 3443).

8.3.3.2 Use of Proceeds
Second, investors want to know why the money is being sought and what it will be spent on. They react unfavourably if they think that their investment will simply be used to repay debt or if they perceive the amount being raised to be disproportionate to the purpose to which the money will be put. On that point CI mentioned, “Sometimes you see start-ups that already have a load of debt on their balance sheet and so I always find it a bit annoying on Seedrs that you don’t have access to the financial statements, but always have to ask for them and then they already have a lot of people investing, but if you look at the balance sheet then the company might be raising GBP 200,000 but it has GBP 150,000 worth of debt in the balance sheet. So basically you are just financing them to repay the debt that they have build through the last year or so.” (CI, l.525). The entrepreneur has to present a compelling case for the sizing of the funding round to be perceived as credible by investors. Mostly, investors will not examine the information in great detail, but expect to see it in order to get a sense if the request appears to be reasonable. TL noted, “All I basically did was to read about their project, read why they were on Seedrs, why they were raising that much and to me it made sense and that’s why I made the leap and invested in it” (TL, l.3136), and LH explained, “so in the last step of the process I looked at their financial plan. There I look at what they want to use the money for and if that makes sense to me. And for the financial assumptions I assess if they sound reasonable.” (LH, l.3540). Their reflections on the evaluation of the financials indicates that many crowdinvestors do not spent too much thought on approving the underlying assumptions in detail, but rather do crowdinvestors superficially judge if the numbers appear to be reasonable.
8.3.3.3 Valuation

The third factor discussed during many interviews was the valuation of the venture seeking funding and its implications on the decision-making of crowdinvestors. In our opinion, these were enlightening dialogues bringing forth interesting insights. Crowdinvestors adopt a suspicious and critical attitude in their assessment of the valuation and financial projections. The amount of finance required and the amount of equity being offered in exchange are an important part of the risk-reward equation for investors. Again, the approach investors follow when judging the ventures’ valuations is rather superficial. An interesting point was made by PS when he said, “I think it is counterproductive because when it comes to these things it is about do you have a good business idea and then the valuation how you calculate if it is a good price or not it cannot be connected to projections two years from now, in my mind. So I never do that calculation. I do it subconsciously: are they asking for a ridiculous amount? (PS, l.2631).

Since the terms, which the investment is based on are non-negotiable crowdinvestors need to understand if the valuation is realistic. This is not done by applying professional methods of valuing a company, but is based on a subjective appreciation. When reflecting on the valuation, a large share of investors believed the values entrepreneurs put on their business to be unreasonable. KNZ for example stated, “[…] the valuation was half of the time s***. To be honest I don’t believe in any of them.” (KNZ, l.1539). And when asked about the valuation of a particular company she invested in AN, who is an experienced angel investor, explained, “I looked at it and it was crazy and it was wrong and the percentage she gave up was too little and the money I spent were completely disproportioned to the company valuation […]”, she continued,“ it does never make sense to invest in crowdinvesting on the basis of the valuation of the company. They do not have a clue how to do their valuation. I think they are uneducated and they don’t have money to bring in anyone who actually has an overview and an understanding of how to evaluate the company.” (AN, l.213).

Furthermore, SD, one of our German interviewees, stated the inflated valuations reminded him of the equity “dot-com” bubble of 2000, since the majority of campaigns overachieve their funding targets. SD implies that entrepreneurs make their numbers seem better then they are to increase the valuation. When we asked him about his opinion, PE said that he was not utilizing information provided in the business plans at all, “embarrassingly not really” (PE, l. 4363). Remarkably, he instantly confides that it was amazing how all the businesses

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20 This is true for campaigns on Seedmatch in particular and Seedrs to some extent.
were justifying their valuation and that he was wondering if anyone was critiquing the valuations since funding rounds closed very quickly. He made his point referring to a concrete example, “Are People critiquing valuations? They are obviously not because the rounds are closing quite quickly. Who would say that X [the company] is really worth a couple of million?” (PE, I.4644). This is interesting because it contradicts his initial statement of not paying attention to valuations – indeed he does so subconsciously alike PS.

Interestingly, despite the strong criticism concerning valuation, only on rare occasions an inflated valuation led to the rejection of a deal. This being said, we found evidence that an inflated valuation may have a negative effect on the amount invested. For example, when considering how much to invest into an opportunity where she was convinced of the idea and the lead entrepreneur, AN implicitly said that the unreasonable valuation led to a reduced investment, since it prevented her from getting a considerable stake in the business, “[…] I knew that I could not get any significant ownership in the company due to her valuation so I thought that if I win or lose SEK 20,000 it does not matter, it was money that I can lose but give her an opportunity. That was my plan.” (AN, I.206).

In many instances investors acknowledged that valuing early-stage businesses is not based on precise science and therefore appreciated if entrepreneurs try to get a good deal, e.g. LH stated, “One of the biggest problems with this form of financing is how do I find the fair value?” (LH, I.3493). In another statement PS is more concrete when he criticises the unprofessional approach of some entrepreneurs when it comes to valuing their businesses, “[…] they want SEK 200,000 for 5 per cent of the company. So then I calculate what does it mean they think the business is worth? And if you read, they valued their company at SEK 7 million and they have no proof of concept and they just go by their “waving a finger in the air” approach” (PS, I.2635). Building on these insights we suggest that financial details contain a valuable informational component allowing for inference on the entrepreneur’s traits and attributes.

8.3.3.4 Financial Forecasts
The last factor covered in this chapter is the informational value of financial projections presented in the business plans. This factor is strongly related to the investors’ reflections on valuation summarized before. In most campaigns entrepreneurs provide potential investors with forecasted income statements to give an indication of how they expect their business to grow over the next three to five years. Analogical to their feedback on valuations, crowdinvestors do not trust projected financial statements and critique entrepreneurs to be
overly optimistic. Early-stage companies are surrounded by high-levels of uncertainty and risk, making it problematic to project the venture’s performance into the future.

CI, who has a professional background in financial modelling, initially approached crowdinvesting with the idea of projecting the venture’s performance and grounding his investment decision on his analysis. By doing so, he believed to increase the chance of picking the ‘winners’ amongst the investment opportunities. However, shortly after his first investments he realized that it was an arbitrary exercise. He elaborated, "[...] so when I first looked into it coming from a modelling background I thought I might do some kind of forecast and that kind of stuff. In my opinion you can forget about all of that at least with early-stage start-ups because there is no way of basically forecasting anything right, I mean it is impossible to tell what’s going to happen next year" (CI, l.391) and at a later point in the interview he continues by critiquing entrepreneurs and their reliance on forecasts, "I would say that’s all a finger in the air approach. [...] If you look at the forecast in all of the pitches, all the companies are going to grow so fast and going to make so much money, big hockey stick analysis." (CI, l.521). Numerous other investors supported his opinion. When reflecting on the financial statements KG (l.3402) stated, "[...] I am sometimes a little surprised about the assumptions [...]" and he resumed “they are too optimistic”, an opinion shared by RN (l.5095). MW (l.3863) stated, “[...] they are often not plausible” and AN (l.217) as well as PS (l.2627) conclude, “they are big guesswork”.

During the development of the business, entrepreneurs will be benchmarked against their overambitious business plans and many will fail to deliver on their promises. To date, there is only insufficient information available on how this may have an impact on factors such as the entrepreneur-investor relationship. Two German investors stated to regularly benchmark the numbers provided in the quarterly updates with the initial financial projections. According to their experiences ventures tend to lack behind their business plans considerably. RN told us, "Within my portfolio there is only one company where – based on the updates – I can expect a return on my investment. All other businesses perform well below their expectations." (RN, l.5081).

We realize that crowdinvestors have a similar attitude towards business plans and financial projections as BAs. Many crowdinvestors require seeing this information prior to investing and expect a realistic and comprehensive business plan. We have shown that in alignment to BAs crowdinvestors are sceptical about financial projections and many had negative
experiences with overly optimistic projections (Mason & Harrison, 1996b; Van Osnabrugge & Robinson, 2000).

8.3.3.5 Exit Strategy
This chapter focuses on our findings regarding exit strategies. Overall, our data on this criterion is scarce. Only a minority of investors was concerned about exit routes at the investment stage and few interviewees unlocked a discussion on this topic. Typically exit strategies become relevant four to five years after investing. We assume that crowdinvestors emphasize the short-term implications of their investments instead of engaging in hypothetical discussion. Nonetheless, we must be aware that the seemingly low importance of exit strategies may be due to methodological limitations.

8.3.4 Miscellaneous
As miscellaneous we categorized two very interesting factors where we unfortunately only have only limited data available. Despite, we consider geographical proximity and wisdom of the crowd to be important factors to explain investor behaviour.

8.3.4.1 Geographical Proximity
Geographical proximity is known as a relevant investment criterion for BAs (see Chapter 6.2). Although we did not directly ask interviewees about the importance of geographical location as an investment criterion, we found evidence that under specific circumstances geographical proximity to the business matters to investors. Particularly investors who, as we will learn in chapter 8.5.1, can be classified as active or “value-adding” investors mentioned to be attracted by businesses located in close proximity to their location. SD noted, "In any case, it is important to me that the companies are from my region. Just because I can come in contact with the founders and I generally also want to support the region. I think it’s very good if someone from my region wants to start something." (SD, l.5169). His statement indicates that, next to the rationale of being able to meet the entrepreneur personally, geographical proximity has a strong emotional component. The UK-based crowdinvestors also stated a preference to invest in local ventures, but this was driven by the SEIS and EIS tax schemes, which are only granted to businesses with a legally based in the UK.

Other crowdinvestors are less concerned about geographical proximity and take advantage of the online nature of crowdinvesting to make cross-border investments. PS, TK, NH and TL have made several investments in ventures located abroad. TK pointed out that crowdinvesting takes place on the Internet and provided him with the opportunity to make investments outside his home country (TK, l.5586). Hence, while some crowdinvestors prefer
to invest in their local region, crowdivestment also entails interesting possibilities for cross-boarder investments and relaxes geographic boundaries known from BA investments (see Chapter 6.4.3).

8.3.4.2 Wisdom of the Crowd

As we have learned in chapter 5.1 the idea of the wisdom of the crowd has its origins in crowdsourcing, but the idea is also widely adopted in the context of crowdfunding and crowdinvesting. In our study the wisdom of the crowd was associated with two cases. First, in connection to campaign traction, i.e. the progression of campaigns towards their funding targets. Secondly, in relation to the forums (Q&A section) on the campaign site, where potential investors can pose questions and see what other investors have asked. Many interviewees mentioned the forum as a valuable tool to get a better understanding of the potential of a business idea and as a possibility to learn from other investors’ perspectives. On this note FP stated, “There is the opportunity to ask questions to which entrepreneurs can respond. And I look at the Q&A’s relatively closely: I look at how the questions are formulated and what they are about. Then I go back to specific points in the business plan again. I think that’s actually quite good, because you have the opportunity to see what other people see what you yourself did not notice.” (FP, l.713). Based on our insights we suggest that the forums are a great opportunity for investors to benefit from the wisdom of the crowd in form of the distributed knowledge of crowdinvestors. In chapter 8.3.2.3, we have mentioned a case where this benefit came into effect.

For the other case, campaign traction as a reflection of the wisdom of the crowd, our evaluation is more sceptical. Only one of our interviewees mentioned to trust investors have done a solid assessment of the opportunity before they invested and thus he interpreted traction as a quality signal for the business. While our results show that the majority of investors make conscious investment decisions this idea may be flawed in several incidents. For example, it may not be the case for a campaign where the entrepreneur was successful in leveraging his direct personal network (FF investors) to contribute a large portion of the overall funding target. In chapter 7.1.1 we have argued that FF investors are not critically assessing the business idea due to their personal affiliation with the entrepreneur.

An interesting example was provided by KNZ, who confided to be guided by certain investors in his investment decision. This means, instead of following the swarm of investors he follows specific investors who according to his opinion are experts in certain areas. When asked if he believed in the wisdom of the crowd KNZ replied, “Basically – yeah. I mean there are a
couple of people I pay attention to when investing.” (KNZ, l.1669). By checking their LinkendIn profiles KNZ was familiar with the professional background of these investors. Therefore, if for example a professional programmer invested in a company developing a new app, he would be less thorough in his assessment before investing. In his opinion the investment by the expert serves as a quality stamp for the business.

8.3.5 Summary

In the previous chapter we exhibited several criteria crowdinvestors assess to inform their investment decision. We always have to keep in mind that the criteria presented previously are a summary of a wide range of references collected during the interviews and that investors differ in how they inform their investment decision.

For most investors in our sample the business idea is considered to be the first filter in the decision-making process. Afterwards, information on the entrepreneur or team is scrutinized in more detail based on a subjective judgement of a diverse set of highly intangible attributes. For this task the video is invaluable. Surprisingly references on market characteristics were scarce. Either investors do not pay much attention to this criteria or methodological limitations are responsible for this seemingly low importance. We realize that crowdinvestors have a critical attitude towards business plans and financial projections. Many crowdinvestors require seeing this information prior to investing and expect a realistic and comprehensive business plan.

8.4 Sizing the Investment

In this chapter, we take a closer look at how investors decide on the size of a given investment. Our sample covers investment amounts in the range of EUR 100 to 7500 per single investment. Sizing of investments is an exercise specific to each individual investor and based on the consideration of several factors. For the majority of crowdinvestors this decision is grounded on two constituents: the individual judgement of the opportunity and their available investment capital or “play money”.

The amounts invested by the investors depend on confidence in the business idea and the entrepreneur. AN, who is both BA and crowdinvestor emphasizes that in her BA investments she is taking a different approach compared to crowdinvesting. As a BA, she is investing larger amounts and therefore is seeking some level of control and only invests through a syndicate (AN, l.77). Her activities in crowdinvesting are based on another approach where
she feels that she can support entrepreneurs fulfil their dreams without the need of monitoring her investment too closely (AN, l.366). An example is her investment of SEK 20,000 in a business where she admired the entrepreneur, “The entrepreneur was interesting because she was the first female entrepreneur I have seen with a campaign. She is an engineer and an industrial engineer too and it is very hard to find female innovators that has bigger ideas than just trying to do a company to live on, not having any dream or aspirations” (AN, l.172). AN’s minimum investment as a BA is SEK 50,000. The lower amount invested in crowdinvesting opportunity was a direct consequence of lacking control and a risk assumption of the entrepreneurs ability, “I thought that if I win or lose SEK 20,000 it does not matter, it was money that I can lose but give her an opportunity. That was my plan.” (AN, l.207).

KNZ, who at the time of the interview managed a portfolio of 48 crowd investments, mentioned to apply a clear strategy to decide on the size of his investments. When investing GBP 500 to 1000 he sees a good opportunity with promising prospects of scaling the business. The next stage are investments of GBP 300 to 500 are opportunities with an interesting business model, but where he is not sure about the scalability of the business. The final category is investments below GBP 300, which he describes as “just a gamble”. He stated that this category is for opportunities sounding good on paper, but where he perceived chances of success as low (KNZ, l.1373).

8.4.1 Play Money
It is our general impression that crowdinvestors take an informed approach to the investment size they decide upon. Following the logic of RN (l.144), “People should only invest if they have a little bankroll, such as if the investment is lost they won’t be affected”. Crowdinvestors know what they can afford to lose without affecting their lifestyle. They share this investment logic with BAs (Baty, 1991). Mason and Harrison (1996b) note that one business angel described his investment money as “casino money” a term with a similar meaning as “play money” or “gambling money”, two terms that occurred in our interviews several times. Play money in the context of crowdinvesting is funds kept aside by investors for crowdinvesting purposes. OGG confided that the size of his investments depends on the money available on his “play-account” (OGG, l.4453) with CI adding, “I always keep GBP 2000 to 3000 in cash just in case there is a really cool business coming online.” (CI, l.489).

The logic is that crowdinvestors are emotionally detached from the money invested in crowdinvesting, which means investors are prepared to loose the invested money. TK added
depth to the observation with his explanation of what play money means for him, “You say I’ll put in EUR 1000 I have actually already decided that I want to spend EUR 1000 so it’s like having a voucher for investing. I have already spent the money and now I need to find the actual product. In that sense it is gambling money, right, because you already spent the money and now you are just shopping where to actually put it […] The money is gone I don’t expect to get it back, I expect the money to be lost. So now what I want is to be entertained” (TK, l. 5697).

The idea of play money appears to be inherently linked to crowdinvesting. Crowdinvestors are aware that they are buying into risky opportunities where their money will be inaccessible for indefinite time. FP (l.1056), told us that he would not invest in crowdinvesting if he did not have any “play money”. PE who is investing GBP 30,000-40,000 a year on “little things like this [crowdinvesting]”, qualifies as one of the more risk prone investors in our sample. During our interview he reflected, “[…] it [crowdinvesting] just feels like it is a more educated form of gambling in some form at the moment. There is not enough information on there for you to make fully educated investment decisions and it is very easy to log on and buy” (PE, l.4641).

8.4.2 Tax Deductibles Influence on Investment Sizing
In chapter 7.2.1 we have discussed the implications of tax deductibles on crowdinvestors investment decision. Keeping in mind that only the three UK-based crowdinvestors were eligible for tax deductibles information on this topic is scarce. Further research has to be undertaken in order to clarify implications of tax deductibles on amounts invested.

8.4.3 Summary
Crowdinvestors estimate the investment amount on the level of confidence in the entrepreneur and the business idea. A common characteristic is that crowdinvestors are terming the money invested as “play money”, money that they can afford to lose without affecting their lifestyle.
8.5 Post Investment

In the following chapter we present crowdinvestors experiences with the post-investment phase. We understand post-investment as the contractual relationship between the entrepreneur and the investors starting immediately after the investment has taken place. This relationship ends once the investors are able to sell their shares “exit” or the business is being shut down. The inclusion of crowdinvestors varies from case to case and crowdinvestors have different expectations for the level of involvement.

It is a common finding of the analysis that investors are more positive towards ventures, where the entrepreneurs provide transparency and remember to update investor on new developments: “I think the smartest CEOs or smartest start-up guys they try to include people [...] the people who are successful are a little bit humble, a little appreciative of people” (KNZ, l.1845). Accordingly investors are disappointed with entrepreneurs who fail to perform in alignment with their expectations. FP experienced that quality of communication dropped significantly after the funding round closed and was very unhappy with a particular venture, which failed to provide a quarterly report, as required by Seedmatch. He felt negative about the venture’s inability to deliver the report and as a consequence started questioning the ability of the entrepreneur and the potential of the venture. He wondered, “if they behave like this to their investors with bad reports, then how they behave with customer support requests?” (FP, l.1032).

While there is a link between expectation (what the entrepreneur promised) and evaluation of experience (what the entrepreneur has achieved), we found two distinct ways in which crowdinvestors are articulating the evaluation of their post-investment experiences. The first is concerned with the entrepreneur’s ability to include investors in the development of the company e.g. asking for opinions and advice. The second is concerned with investor’s ability to reach their milestones.

From the forms of articulation, our analysis suggests two types of crowdinvestors in post-investment phase: The active “value-adding” investor and the more passive “observing” investor. Each type has distinct preferences for the post-investment experience.
8.5.1 Active “Value Adding” Investors

For active investors the entrepreneur – crowdfunder relationship is a partnership where they are actively contributing to the success of the venture. Consequently, active investors evaluate the post-investment experience on the basis of entrepreneur’s ability to engage with and include them in the development of the company. The degree of partnership ranges from informal casual meetings to more strategic engagement on an advisory board level. A common trait is that active investors emphasize offline relations as desirable, and have met with or attempted to meet entrepreneurs in person.

Despite their small stake in the company, active investors are eager to contribute their expertise and know-how, “[...] it is our role to tell them that we are here if they need us, but they don’t have to. We have such a tiny share of the company, but we have so much knowledge [...] and not to use it is a total misunderstanding of why there are business angels” (AN, l.258). As we have shown in the evaluation stage, crowdfunders prefer investing in sectors they are familiar with from personal interest or working experience. The foundation for these rather informal partnerships is driven by personal interest. FP pointed out that he has the best connection with ventures where he is genuinely interested in the product (FP, l.1086). Both, KNZ and SD, stated to have investments in their portfolio where they leverage their investment for their own companies. KNZ by staying informed about technological trends for his consulting company and SD by leveraging networks for his organic food company (KNZ, l.1288; SD, l.5224).

While most of the entrepreneur – ‘active investor’ relations are limited to informal partnerships some investors become engaged on levels similar to the involvement of BAs. They have an active voice in the company, serve in the advisory board and share their experiences with the entrepreneurs. NH, who can be considered to be such an investor mentioned, “[...] they asked me if I want to serve on the advisory board. So I have been very active working with them to give my opinion on questions they have or to give them information or find ideas. And I will probably drive up to Stockholm now and again, which is good fun for me. But again is being part of being actively involved in the company that is fun. So for me it has continued right through the investments and it is an on-going business. Good experience so far and if you consider it is the first investment it has been a very good experience” (NH, l. 2347). NH’s stake in the company is only EUR 2000, which is insignificant compared to average business angel investments (Wiltbank, 2009). Even if the investment will end in a successful exit it will not be higher than other crowdfunders. Still he
invests considerable time and money into the venture, driving from Copenhagen to Stockholm (a six hour drive), and sharing his expertise from a long professional career. He simply mentions the “fun of being actively involved in the company” as the motivation for his engagement. NH’s interview does not indicate that control and protection of investment is a reason for his active involvement. In contrast, BAs who become engaged on an advisory or board level in their investments are motivated to protect their investment from mismanagement (Kelly & Hay, 2003).

8.5.2 Passive “Observing” Investors

Contrary to the value-adding investors who actively engage with the company they invested in, the passive investors stay in the background. Their relation with the ventures is comparable to investors in public limited companies. The passive investors derive value from following the venture’s development through regular updates, without actively engaging in the day-to-day operations. The fact that most investors can be categorized as passive investors is important, since an abundance of active investors can create problems concerning investor relations. OGG explained to us that if, “[...] you open a crowdinvesting campaign you can get a lot of people who wants to invest money. If all of these people want to be actively involved it could be a big problem. You have no chance to do your business, but then you are only working with these people who wants something to do. It is not a good thing.” (OGG, l.4400).

There is unanimity amongst passive crowdinvestors that spending their own time in supporting the entrepreneur is irrational given the small amounts invested and the insignificant ownership in the business. JD for example highlighted, “Due to the small amount but I will not necessarily invest a lot of time. As far as I am informed Seedmatch will keep investors on relevant developments up to date.“ (JD, l.3338). TL added, “I would not go out of my way to promote them or make sure that they succeed.“ (TL, l.3229). KG described his post-investment involvement in the following way, “No, I haven’t been in touch with any of the businesses. I read the updates that Seedmatch sends out now and then, but apart from that I am not spending time on engaging.“ (KG, l.3437). And PS reasoned, “It is a conscious decision, because I have decided that I don’t want to become involved on advisory level. I only want to be involved as a happy consumer [...]” (PS, l.2664). If the amounts invested were higher, they would be more inclined to contact the entrepreneurs directly, “[...] if I make a GBP 20,000 investment I spent a bit more time thinking about it I also keep in touch maybe twice a year if they haven’t given me an update [...]” (PE, l.4616).
The passive investors’ decision not to actively engage with the businesses they invest in should not be misunderstood as being indifferent. They are eager to follow the progress of the company and are regularly reading updates, which is a vital part of their post-investment experience. On this notion JD stated, “Certainly I follow the developments closely.” (JD, l.3337). KG remarked, “Quarterly reports with current numbers are always of interest to me. To see how the companies are doing and if I was right with my assumptions.” (KG, l.3438) and PE sporadically looks for updates, “[...] I might from time to time look and see if there is any updates on Seedrs [...]” (PE, l.4619). Besides quarterly reports and platform updates, we find that social media groups are often a medium used by entrepreneurs to communicate with their investors. Though not being an active contributor and debater, PS is using the Facebook groups to evaluate the probability for investments success, “[...] I notice now that the group is slow and they [the entrepreneurs] are looking for a place and then one month later they asking “oh does anybody have any leads on a nice place somewhere central in Stockholm for our first location?” [...] Had this been a hungry entrepreneur then he or she would have hammered down a place somewhere within three months of starting up.” (PS, l.2736).

8.5.3 Summary

Based on our findings we can categorize investors into two distinct groups, ‘active’ and ‘passive’ investors. Active crowdinvestors pursue active involvement in the venture. If utilized properly, this involvement can be regarded as ‘value adding’. Passive investors consider involvement in the company to be an irrational behaviour, which is not justified by the small amounts invested. However, they still want to be informed about the progress of the venture.

8.6 Harvesting

As pointed out in chapter 8.1 the final stage in the process called ‘harvesting’ has been of subordinate importance in our research. To our best knowledge none of the ventures funded via crowdinvesting has had a successful exit to the time of this writing.

Despite, two crowdinvestors (RN and PS) engaged in a discussion on the subject matter. Both investors advocated for a secondary market where shares in small and emerging companies can be traded. As we have highlighted before, one of the risks of investing in start-ups and small businesses is the inherent lack of liquidity. A possible option to reduce this risk is a secondary market, which provides an additional avenue for investor liquidity. According to PS the presence of a secondary market where shares could be traded would
incentivize him to channel more of his money into crowdinvesting. PS told us, "I am just waiting for it to happen [...] that you can go and trade the stocks that you have. When that happens I think I will do a lot more investing, because right now I have to balance the investing with the accessibility of my funds. If it was regular stocks then I can sell them without waiting for an exit – and without doing a lot of paperwork trying to sell to another person in the investor community so that's really what I am waiting for." (PE, l.2775).

Although discussions around the use cases of a secondary market have been lively, regulatory burdens restrict the implementation. At present two platforms, Bergfürst in Germany and Invesdor in Finland, were granted a licence to facilitate trading of shares through their system. However, a centralized trading infrastructure allowing for across-platform transactions would be the preferred solutions. It is important to put these issues up for discussion since entrepreneurs need to offer exit strategies to crowdinvestors like they do for BAs. For crowdinvesting, these issues remain largely unresolved (Hornuf & Schwienbacher, 2014).

To the best of our knowledge, there is no study available yet providing empirical data on returns generated from crowdinvesting. Likewise, little is known about the riskiness of these investments. What we know so far is that during the last two and a half years crowdinvesting existed in Germany, 4 out of 115 start-ups filed for bankruptcy21. On the other hand we are aware of five successful follow-on funding rounds collected from professional investors22. Unfortunately, we do not have such data on start-ups financed through Seedrs or FundedByMe.

8.6.1 Summary
To date information on potential exit routes is scarce and as highlighted no start-up funded via crowdinvesting has successfully exited. However, we found indication that the implementation of a secondary market to trade shares of non-listed companies could potentially facilitate more investments in the crowdinvesting market.

21 As of April 20th, 2014, the four start-ups are: betandsleep, BluePatent, sporTrade and XCreater. The latter even went bankrupt during the funding process.
22 The five start-ups are: Protonet, Changers, FrontRowSociety, Smarchive, Neuronation.
9 DISCUSSION

The discussion chapter commences with a reflection on a question posed by Hornuf and Schwienbacher (2014) who ask if crowdinvestors are small business angels. With this study we contributed essential work in providing a well-informed answer on this question. Next, we inspire a discussion on potential implications of our findings for different actors involved in crowdinvesting ecosystems. Furthermore, a reflection on how this study is placed in the context of existing research is provided. Finally, we briefly discuss potential limitations of this research.

9.1 Are Crowdinvestors Small Business Angels?

In the course of this research project novel insights on crowdinvestors’ and their decision-making process were presented. In many aspects this research was inspired by existing knowledge on BAs. Therefore, it is relevant to discuss the question to what extent crowdinvesting is transforming the crowd into “small” business angels?23 We will also amplify structural differences and similarities between crowdinvesting and angel investing.

In accordance with previous studies on BAs, we have shown in chapter 7.1 that investors included in our sample share similar characteristics as BAs. The majority of investors is male, holds a higher education degree, has prior experience in stock market investing, is fairly wealthy and is highly interested in entrepreneurship. This is in line with observations by the FCA, which reports that crowdinvestors,”[…] tend to be high-net worth individuals with investment experience” (FCA, 2013:37). In this regard, it appears that crowdinvestors can be considered small business angels.

We have also found that crowdinvestors motives are well aligned with what we know about BA motives. Despite the fact that monetary motives play an important role for both, we clearly see a continuing transition from monetary towards non-monetary motives from BAs to crowdinvestors. Instead of evaluating an investment opportunity from an economic point of view, crowdinvestors seem to be attracted by businesses they believe will satisfy their non-financial motives, such as involvement in an entrepreneurial company, fun or the possibility to extend ones professional network. This may also explain why crowdinvestors often invest in businesses even though financial information provided by entrepreneurs is criticised.

23 This discussion topic has been inspired by a recent publication from Hornuf and Schwienbacher (2014).
Trade-offs between financial- and non-financial returns, as described by several studies on BAs, seem to be even more prevalent in crowdinvestors’ decision-making (Wetzel, 1981; Sullivan, 1994; Tymes & Kramer, 1983). This has important implications for legislation in particular. The main concern of legislation is the investor’s protections. As some legislators explain, “to invest” is “to engage in any activity in which money is put at risk for the purpose of making a profit” (BAND, 2014). Contrary, our findings suggest that making a profit may not be the predominant incentive for this new type of investor. These are investors who make their “due diligence”24 from the customer or human point of view rather than from a pure financial perspective. This is where the true disruption of crowdinvesting can be found: Within the democratization of investment and the emergence of a new type of investor, who is investing based on a broader perspective.

All investors in our sample were rational to the extent to only invest money into crowdinvesting that they could afford to lose without negatively impacting their lifestyles. The investors understand the risks involved and are well aware of the high likelihood of losing the money invested via this channel. In this regard crowdinvestors’ are similar to BAs, who only invest to a degree where it does not become substantial to their financial standing. In both cases, the term “play money” appears appropriate to classify money channelled into early-stage ventures (Mason and Harrison, 1996b). Certainly, given their status as accredited investors for BAs the definition of “play money” is relative since they invest much higher amounts than the average crowdinvestor, but the logic behind deciding on the amount is the same.

Additionally, our analysis has highlighted how crowdinvestors’ evaluation of the merits of an investment opportunity is grounded on similar investment criteria, such as the business idea, characteristics of the market, entrepreneur and his team and financial information. Nonetheless, we have also shown how the evaluation of these aspects is undertaken within a very short time frame, usually less than one day and often within a few hours. The online-based nature of crowdinvesting and the existence of platforms as intermediaries, standardizing most of the time-consuming and costly procedures allow for an extremely streamlined investment process (see Chapter 8.1). This is where we see the major differences between BAs and crowdinvestors. Investment decisions in the context of

24 We have argued in chapter 8.3 that crowdinvestors’ due diligence is not comparable to what is classified as due diligence in the context of BA or VC investing.
Crowdinvesting are barely informed on what is known from more professional informal investors as “due diligence”. In fact, almost all investors stated that their investment process is in no regards based on due diligence. Crowdinvestors inform their investment decision based on the information provided in the pitch and not on extensive background checks, financial audits or the like. Actually, many crowdinvestors described their investment decision as intuition or gut feeling.

While it is evident that crowdinvestors in our study consciously neglect conducting formal due diligence, some sources critique that the possibility for crowdinvestors to conduct due diligence are nonetheless limited. Ludwine Dekker (2014) for example stated recently, “Even if crowdinvestors want to double-check their investment, this is often hard. Most investors understand their money is put into a high-risk-high return project, they don’t know what makes a company flawed and when they do, they don’t have the tools to do so [...]” (Dekker, 2014). On the same subject, Bill Payne pointed out, “Experienced angel and venture capital investors spend lot of time independently evaluating the investment opportunities. This due diligence has been shown to radically improve their returns on investment – helping investors pick the right new companies to fund. It does not appear that crowdinvestors will have the opportunity or the experience necessary to choose better investments.” (Payne, 2011). In chapter 6.4.3 we mentioned that BAs on average conduct 20 hours of formal due diligence prior to investing (Wiltbank, 2009). Despite the fact that these concerns certainly deserve critical reflection, many crowdinvestors appear to understand that given the comparably low investment amounts (i.e. a low equity share being acquired) spending much time on informing their decision would be irrational. Based on our insights crowdinvestors value the straightforward investment process providing them with the opportunity to engage in crowdinvesting as a hobby and the chance to easily diversify their portfolio by making several investments in different ventures.

Next to the absence of formal due diligence Hornuf and Schwienbacher (2014:3) point out that, “Differences stem from various sources, such as variations in financial contracting, differences in securities regulations, active involvement of investors, the resulting degree of information asymmetries as well as potential exit strategies.”

As we have shown the market structure of crowdinvesting suggests that the way financial contracting takes place differs from angel investing (see Chapter 8.1). While crowdinvesting largely relies on standardized contracts provided by the platform and leave no space for
negotiations or amendments in the offer, negotiation of terms and conditions is an integral part of the BA investment process (Mason, 2008). Whether crowdinvestors ultimately suffer extensive financial losses by engaging in crowdinvesting remains to be seen (Hornuf & Schwienbacher, 2014).

Despite our interesting insights the question whether crowdinvestors are “small” BAs cannot be answered unambiguously as the boundary between the two types of investors is vague. Yet, knowledge on crowdinvestors is scarce and further research is required to provide a well-grounded answer to this question. Additionally, we have to keep in mind that crowdinvesting is still at an infant stage of its adoption in society attracting what is known as “innovators” and “early-adopters”, who obviously are primarily people with some level of familiarity of entrepreneurship or finance (see Chapter 7.1; Rogers, 2003). This is why it is important to conduct related studies going forward to understand if and how inexperienced investors will engage in crowdinvesting. Given our conjectural knowledge we imply that similarities between crowdinvestors and BAs are evident, while structural differences, i.e. size, stage and context of the investment, are too significant to misconceive crowdinvestors as BAs. Crowdinvestors is a stand-alone investor type and should be regarded as such, despite resembling BAs to some extend. This argument is supported by AN (l.246), one of our interviewees, who is active as both crowdinvestor and BA. She pointed out that her crowd investments should not be confused as being grounded on the same approach as her investments as a BA.

Instead of comparing both types of investors along their similarities we suggest highlighting the opportunity to complement each other is critical to convey the true potential of crowdinvesting. Crowdinvesting will most likely not replace investments from BAs and instead of conveying crowdinvestors competing with BAs evident complementarities should be embraced (Moritz & Block, 2013; BAND, 2014). Hornuf and Schwienbacher (2014) suggest co-investments between BAs and crowdinvestors can have several benefits. One advantage is that crowdinvestors may rely on the financial skills and monitoring abilities of BAs, which furthermore provide hands-on advice (“value-added”) and lend their reputation to the entrepreneurial firm (Hsu, 2004; Ferrary & Granovetter, 2009). In return BAs can leverage the crowd that may complement what BAs can contribute. The wisdom of the crowd may reveal novel information to the benefit of traditional investors. Furthermore, knowledge of a diverse set of individuals can also be leveraged as a resource to solve problems or develop solutions, similar to the idea of crowdsourcing (see Chapter 5.1).
9.2 Implications for the Crowdinvesting Ecosystem

As pointed out in chapter 1 academic research broadening the understanding of the motives and investment behaviour of crowdinvestors is crucial to design effective ecosystems. This study provides novel insights on crowdinvestors, which can be valuable to different parties in the crowdinvesting ecosystem. Based on our results the following discussion chapter presents implications for crowdinvestors, platforms and entrepreneurs.

9.2.1 Crowdinvestor

The crowdinvestor can be regarded as the ecosystem’s backbone. Both the platform and the entrepreneurs depend on crowdinvestors investing some of their own money through this channel. As we have shown in the analysis, crowdinvestors are well informed about the risks involved when investing and are aware that their money can be lost (see Chapter 7.1). Our analysis suggests that most crowdinvestors critically assess investment opportunities before investing and make conscious investment decisions. However, crowdinvestors should be aware that peers are evaluating investment opportunities on financial as well as non-financial criteria. One implication is that it is difficult to assess the investment decision and rationality of other investors. As a consequence crowdinvestors should refrain from trusting traction as a suitable decision-making criterion.

Another potential problem about traction as a signal of quality is that if no crowdinvestor has made an informed investment decision the idea of the wisdom of the crowd is flawed (Collins & Pierrakis, 2012). Indications from the analysis show that the wisdom of the crowd can be beneficial for the investment decision of crowdinvestors when expressed in an open exchange of information between crowdinvestors and entrepreneurs on campaign forums. Next to the tangible information that potential investors receive from each other, there is also a signalling effect, where the decision of individuals to invest influences the decisions of others to follow. In the ideal scenario, each individual’s decision is driven by his or her own critical assessment of the proposal, based on personal knowledge and the information and signals provided by others.

9.2.2 Platforms

As the intermediary between entrepreneurs and investors, crowdinvesting platforms facilitate the transaction between the two parties. In accordance with a study of Klöhn and Hornuf (2012), our results indicate that crowdinvestors trust that platforms conduct an initial screening and basic due diligence to filter fraudulent activities and ensure businesses fulfil certain quality standards. As more platforms enter the market performing a thorough vetting
of applicants for fraud will become a point of competitiveness. Not all businesses will be suited for crowdinvesting and as the model develops, evidence needs to be generated to indicate what businesses it works best for. This will include the identification of those ventures that are most successful at harnessing the non-financial contributions from the crowd.

A recurring crowdinvestor critique throughout the analysis was venture valuation and financial projections. In general platforms should give more considerations to valuations. As mentioned previously, one of the first stages in the crowdinvesting process requires setting a valuation for the company so the entrepreneurs can decide how much equity to offer for the amount of capital they are seeking to collect. This is an important part of the process, as it is necessary to ensure that the entrepreneur gets a fair valuation for their business, while ensuring shares are not too expensive. But the difficulty in estimating the value of a company must not be underestimated. Much of the assets held by the business may be in the form of intellectual property and valuations are largely based on risky predictions of future market size, competition, revenue and other variables. The most common practice on crowdinvesting platforms is for entrepreneurs to set the valuations themselves based on what they perceive the business to be worth. However, if they get this valuation wrong it might have a significant adverse affect on the entire campaign (Collins & Pierrakis, 2012). While it is the entrepreneur’s responsibility to put a fair valuation on his business platforms should advice and educate inexperienced entrepreneurs on how to determine the “fair value”.

Additionally, it was highlighted that the best investment opportunities raise money too quickly and is funded before the investor can ask questions to the entrepreneurs. A crowdinvestor proposed that the platforms introduce a time period before the investing starts where investors can ask questions and read up on important information. The point is supported by our analysis, which shows that the wisdom of the crowd comes into effect by questions and answers expressed in the forums.

Finally, increased transparency on composition of the investor crowd by disclosing the amount contributed by the entrepreneur himself and FF investors entails informational value. Our analysis suggests that FF investors cannot be considered crowdinvestors due to their fundamentally different motives and investments by FF affect campaign traction, which most likely influences crowdinvestors’ investment decision (see Chapter 7.1.1). Investments from FF, if not identified as such, could be interpreted by other investors as investments primarily
triggered by the perceived financial prospects of the venture. This potentially biases investment decisions by other investors.

However, the presence of funding from friends and family can also have a positive signal in respect to the trustworthiness and ability of the entrepreneur(s) and the likelihood of generating a return for investors. These signals may offer reassurances to investors who are worried how committed the entrepreneur is to making the business a success. For both reasons it is to the benefit of the model to ensure such investments are transparent, so all investors can accurately judge the signals they receive. A study by Conti et al. (2011) found that FF investments increase the likelihood of subsequent BA funding by 5 per cent. If FF investments have a similar affect on crowdinvestors, transparency will also be beneficial for the entrepreneur.

9.2.3 Entrepreneurs

When choosing crowdinvesting as a source of finance entrepreneurs need to be aware that they are subject to the expectations of crowdinvestors. Managing co-investment between various investors with different motivations for investing is one task that the entrepreneur will need to master. As our study adds insights about the mix of factors that drive crowdinvesting investment behaviour, it can assist entrepreneurs (and platforms) on how this can be achieved (Collins & Pierrakis, 2012).

Entrepreneurs should be aware that crowdinvesting does not end by closing a successful funding round. Crowdinvesting entails a long-term relationship between entrepreneur and investor during the post-investment phase. For many investors the post-investment engagement is considered an integral part of the experience (see Chapter 8.5). Interacting with the business through the funding process is of critical importance to investors. Entrepreneurs need to keep investors engaged to leverage the benefit of having access to the crowd.

Our study suggests crowdinvestors’ expectations from the investment are two-sided. Firstly, it is expected that entrepreneurs do their utmost in order to create a successful venture that hopefully will generate a return on investment. Secondly, investors expect that the entrepreneur will provide a unique experience to satisfy crowdinvestors non-financial motivations. Our insights on passive and active crowdinvestors can hopefully help entrepreneurs to develop valuable investor relations. While “passive” investors are emphasizing the financial motives of crowdinvesting and believe the entrepreneur to perform
independently, the “active” investors intend to engage in the venture development on a level similar to BAs (see Chapter 6.4.5). The outlook of managing a crowd of active investors may seem discouraging to entrepreneurs. Research by Larralde and Schwienbacher (2012) indicates that it is possible to create mutually beneficial synergies between entrepreneurs and crowdinvestors, which can support the development of the venture. It should be noted that investors do not have a contractual entitlement to have a say in the company. Instead, it is the responsibility of entrepreneurs to create an environment where value-adding crowdinvestors are activated.

9.3 Our Study in the Context of Current Research

The purpose of this chapter is to map our study within the context of current research by relating back to our literature review in chapter 2. As highlighted previously this study can be regarded the first of its kind. While currently only limited reference points on the specific topic are available we can draw interesting implications of motivational aspects from prior research on crowdsourcing and crowdfunding. When looking at our results on crowdinvestors’ motives the origins of crowdinvesting in these antecedent concepts becomes evident (see Chapter 7.2).

Gerber and Hui (2012) show that non-financial motives such as the feeling of connectedness to a community with similar interests and ideals and helping others (entrepreneurs) are key factors in explaining crowdfunders’ participation. A view shared by Guidici et al. (2012), who believe that crowdfunding has mainly a social and emotional value. People may invest if, (i) the amount of money to be invested is low enough to consider negligible any subsequent loss, (ii) the project has a strong emotional content, and (iii) returns create an exclusive non-monetary benefit that may be shared only among the financers, enhancing the social and emotional nature of the deal. Grounded on our study we can bridge the gap to crowdinvesting by stating (i) “play money” is considered negligible if lost, (ii) emotional content certainly is important for large bulk of crowdinvestors and (iii) the non-exclusive return can be defined in being part of an entrepreneurial venture, independent if active or passive. Additionally, Hemer et al. (2011) highlight supporters in reward-based crowdfunding pledge to attain self-affirmation and to derive joy from the activity. While our insights on self-affirmation as a motivational aspect in crowdinvesting are limited, we illuminated that “joy” is a crucial component in explaining crowdinvestors’ motives to participate (see Chapter 7.2.2).
In chapter 5.1, we have learned how crowdsourcing is based on related aspects, "The user will receive the satisfaction of a given type of need, be it economic, social recognition, self-esteem, or the development of individual skills" (Estellés-Arolas & González-Ladrónde, 2012:9). In the context of crowdinvesting Schwienbacher and Larralde (2010) add the desire to extend one’s network, the pleasure of participating in the exciting adventure of building a start-up and the purely financial motive of reselling shares at a later stage as key motivational aspects.

In addition, Ordanini et al. (2011) find that investors are not only attracted by the opportunity to earn profits, but also by the novelty of the product, a view, which is confirmed by our study. The possibility to foster an innovative product or service gives the investors the feeling of contribution.

Despite the different context in which studies were conducted it is striking how our findings coincide with insights from previous studies. In deed factors such as extending one’s professional network, being part of an entrepreneurial venture, as well as the idea of developing and utilizing individual skills were mentioned during our interviews. It appears that these factors are a fundamental basis to understand user participation in any form of Web 2.0 collaboration, being it crowdsourcing, crowdfunding or as in our case crowdinvesting.

Interestingly, Schwienbacher and Larralde (2010) also distinguish between active and passive investments by investors, a segmentation that is also evident in our study. The authors suggest that active involvement may be structured in the form of crowdsourcing where entrepreneurs can leverage active investors’ skills and expertise, which to our understanding would be suitable way of leveraging active investors as “value-adding”. It is a common opinion by experts that by using crowdinvesting over BA investment, entrepreneurs lose out on the value-adding component commonly known for BA investments (BAND, 2014). While our findings are not generalizable, we argue this rather unilateral view may not hold true if entrepreneurs apply suitable strategies to leverage the crowd. The crowd can be more intelligent than individuals because everyone can build on each other’s skills. Letting investors have their say has to be considered an asset rather than a liability if used correctly.

Whereas motivational aspects have received attention by scholars, studies similar to ours are scarce and provide only limited aspects we can build on to. For example, Agrawal et al. (2013) point out that funders and creators are initially overoptimistic about potential
outcomes and after a first wave of funded artists (the study focuses on funding musical projects) failed to deliver a tangible return on investment, investors revised their expectations downwards. While this insight focuses on crowdfunding, we find similar tendencies for entrepreneurs in crowdinvesting. Based on our insights investors often perceive entrepreneurs as being overly optimistic about the venture’s future. This is reflected in unrealistic financial forecasts and inflated company valuations (see Chapter 8.3.2.3). Detailed information on crowdinvestors’ expectations is limited and a discussion will only be available once data on average returns from crowd investments becomes available. The last factor to be discussed is Hagedorn and Pinkwart’s (2013) statement that the signalling and building of trustworthiness by the entrepreneur plays a vital role in crowdinvesting since the investor is engaged in high-risk and high uncertainty investments. This argument is strongly supported by our findings. As we have pointed out in chapter 8.3.2.3 most investors stressed the importance of trusting the entrepreneur before making an investment.

Mollick (2013) studied a large data sample derived from Kickstarter to evaluate how amateur investors inform their decision to support a project. He concludes that despite structural differences between amateur investors and VCs, they ultimately look at signals of quality to inform their investment decision. Our research sheds additional light on this question by elucidating that crowdinvestors, who are also considered to be “amateur investors”, arrive at their investment decision in a fashion similar to BAs (or VCs).

In one of the first empirical studies on crowdinvesting Ahlers et al. (2013) suggest that financial roadmaps including the type of proposed exit channel have at most a limited impact on funding success. The authors point out that these statements are not legally binding and therefore considered “cheap talk” by investors. Our study adds on to this notion by contributing valuable qualitative insights on crowdinvestors’ view on financial statements. We have shown that firstly crowdinvestors in our sample are highly sceptical about financial information provided in the pitches and secondly only a few investors pay attention to exit routes.

Kortleben and Vollmer (2013) raise questions concerning selection criteria of crowdinvestors. In particular they ask: do these investors apply similar investment criteria as traditional investors or do gut-feeling and/or emotional aspects prevail? Based on our findings this question cannot be answered unambiguously. Our study implies that crowdinvestors do
apply very similar investment criteria as BAs (and VCs), but gut-feelings and emotional or motivational aspects evidently play an important role in the assessment as well.

Finally, Kim and Viswanathan (2013) show that early investments by experts in online crowdfunding markets have a positive impact on follow-on investments by non-experts. While our objective was not to investigate the role of experts in the crowdinvesting space, KNZ provided an interesting case. As we have pointed out in chapter 8.3.4, occasionally KNZ’s investment decision was guided by earlier investments of investors whom he considered to be experts in a certain field. In his logic investments by these individuals served as a quality signal for the investment opportunity and lowered the threshold for him to invest. We hope to inspire further research on these aspects in the context of crowdinvesting.

Overall, academic insights on crowdinvesting are scarce and further research is needed to support well-informed discussions on the subject.

9.4 Limitations

While some methodological limitations were covered in chapter 4.7 it is important to provide a few final remarks on research limitations related to events that occurred during the research. Based on the circumstance that we are relatively inexperienced researchers results of this study may be subject to several biases. The conducting of semi-structured interviews requires researcher’s to control and interpret emerging data. This applies to both the specific interviews and the data set as a whole. In the context of this thesis the latter proved to be a challenge.

Another limitation regarding interviews can be identified in the relatively short timeframe in which we collected, transcribed and analysed the data. Following the overwhelming feedback from investors we conducted a total of twenty interviews within a three-week period. This must be considered a relatively short period of time to handle such large data volumes, especially for inexperienced researchers. We did our utmost to evaluate the interviews on a continuous basis as recommended by Corbin and Strauss (2008), but it is important to point out that time constraints may have limited our reflection on the conducted interviews during the data collection process. Initially we planned to stop data collection halfway through the process (10 interviews) in order to thoroughly evaluate the data for emerging concepts and if necessary to reiterate on our interview protocol. However, this reflection was shortened to one day of skimming the data, which may have been too short to fully comprehend the data.
Further, our transcription might have been subject to bias or inaccurate and selective perceptions. Another potential limitation is a language bias. Some interviews were conducted in Danish or German and subsequently translated into English. While this translation was done as accurately as possible it may have influenced the meaning of the data.
10 CONCLUSION

This study was initiated to explore the problem statement: How are crowdinvestors informing their investment decision? During exploration of the problem statement, we have sought to study crowdinvestors decision-making criteria and process and to provide evidence of their motivation to engage, which is vital to comprehend investors’ investment decision. Crowdinvesting is democratizing early-stage finance by allowing the general public to invest money into start-ups in exchange for equity in the company.

While crowdinvesting as vehicle for start-up funding is gaining momentum little remains known about this new type of investor. To our best knowledge this study represents the first attempt to shed light on crowdinvestors and their decision-making by conducting and analysing twenty interviews with investors from three well-established crowdinvesting platforms. Hereby, this thesis adds on to the limited extent of academic research on crowdinvesting and provides a valuable contribution to a better understanding of crowdinvestors’ investment motives, as well as decision-making process and criteria, which is vital to build efficient investment ecosystems.

In the lack of theory on crowdinvestors investment decision we applied research on BAs as reference point for our analysis. We suggest that BA theory is suitable to comprehend crowdinvestors investment decision and our findings imply that crowdinvestors’ assess investment opportunities in similar ways. While similarities between BAs and crowdinvestors evidently exist, we conclude that crowdinvestors are not small BAs, but a stand-alone investor type. We have elaborated on this delimitation in detail in chapter 9.1.

We have shown how financial and non-financial motives are inextricable when comprehending crowdinvestors’ decision-making criteria and process. The enjoyment derived from participation in crowdinvesting is at the minimum as vital as the prospect for financial gain. In this regard an appreciation of crowdinvesting’s origins in the antecedent subjects of crowdsourcing and crowdfunding is essential to elucidate investor behaviour. In alignment with findings by Larralde and Schwienbacher (2010), we conclude on the distinguishing of “active” and “passive” crowdinvestors. This differentiation is crucial in understanding crowdinvestors motivation to invest and their expectation from the investments.
We have also highlighted key differences between crowdinvestors and BAs investment process triggered by the virtual context of crowdinvesting and its implications on investment decision-making. Investors’ first screening is typically focusing on the merits of business idea. Most investors filter ideas in accordance to personal interest and a clear unique selling proposition.

Investment proposals passing this initial filter will be set out for a more detailed examination by the investor, especially the entrepreneurial team moves into the centre of attention. In this regard, the campaign video is invaluable. We also find that financial details play a subordinate role in the evaluation of the investment opportunity. Yet, a common finding is the criticism of entrepreneurs’ overly optimistic financial projections and the resultant inflated valuations.

Generally the investment process is quick and based on a fairly pragmatic approach guided by what many investors’ described as “gut feeling” rather than formal due diligence. Thus, the information provided by entrepreneurs should be concise, clear and to the point. Poorly presented investment material and unreasonable valuations is perceived as a signal for the unprofessionalism of entrepreneurs and will potentially result in crowdinvestors’ loss of confidence.

We find that the vast majority of investors are well aware of the risks they carry when investing in early-stage start-ups. They also have rationale expectations in terms of potential return on investment. All investors understand that statistically most of their investments eventually fail. On this notion, an important finding of this study is that crowdinvestors’ only channel money into crowdinvesting, which they can afford to lose without impairing their lifestyles. Our discovery of “play money” prevalent in crowdinvesting has earlier been coined in BA research and adds to the understanding of crowdinvesting as a hobby for crowdinvestors. This can also be traced in the fact that most crowdinvestors in the sample are reluctant to state an expectation to a return on investment. Instead it is clear that crowdinvestors expect a return on fun.

While the crowdinvesting industry is still in its infancy, the coming years will reveal how crowdinvestors’ motives and decision-making criteria evolve as the industry matures. In a few years data on prospective financial return on investment via crowdinvesting will become available and reveal its value as an investment opportunity for investors.
10.1 Future Research

While this study represents an initial attempt to provide insights on the investment decision-making criteria and motives more research is required to broaden the knowledge base on crowdinvestors. We encourage researchers to conduct similar studies by applying suitable methods. Precisely because of some deficiencies mentioned earlier we suggest to use methodologies, which allow to examine investor decision-making in real-time. For example, several studies on BAs have used verbal protocol analysis (Ericsson & Simon, 1993), a technique which examines decision-making in real-time, albeit often in artificial or experimental situations, by asking respondents to “think out loud” as they perform a task (Hall & Hofer, 1993; Zacharakis & Meyer, 1995; Mason & Rogers, 1997).

This may include research focussing on the importance of a specific criterion such as the entrepreneurial team or studies solely examining motivational aspects involved in crowdinvesting. Increasing availability of data will allow studies similar to Ahlers et al. (2013) empirically examining factors affecting success of crowdinvesting projects. Empirical studies will be a valuable complement to studies based on quantitative or qualitative methods, which inevitably suffer from several biases.

Another open question is to which extent does crowdinvesting help to close the financing gap and if it facilitates or impede follow-up funding by professional informal investors? (BAND, 2014; Hornuf & Schwienbacher, 2014). Initially, platform providers were focussing their attention towards satisfying the needs of crowdinvestors and entrepreneurs primarily. At present time platforms start to realize that finance from later-stage investors is often needed for the successful growth of the company. Therefore their interests have to be taken into account when structuring the crowdinvesting ecosystem. Implications of such as study can be invaluable for entrepreneurs who consider running a crowdinvesting campaign.
11 BIBLIOGRAPHY


### 12 APPENDIX

#### 12.1 Appendix 1: Literature Overview Crowdfunding

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<tr>
<th>Study</th>
<th>Research topic</th>
<th>Methodology</th>
<th>Main findings/ proposals</th>
<th>Crowdfunding model</th>
<th>Focal area</th>
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<tbody>
<tr>
<td>Belleflamme et al. (2011a)</td>
<td>Study of crowdfunding from an economic perspective. Development of a model associating crowdfunding with pre-ordering and price discrimination. Study of conditions under which crowdfunding is preferred over alternative forms of funding.</td>
<td>Analysis of hand-collected dataset and quantitative analysis (n=19)</td>
<td>Community-based experience key ingredient for crowdfunding to be a viable source of finance. Not-for-profit businesses tend to be more successful than for-profit businesses. Crowdfunding is especially suitable for lower levels of finance.</td>
<td>Reward-based</td>
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<td>Gerber and Hui (2012)</td>
<td>Motivation of investors and entrepreneurs to involve in crowdfunding markets</td>
<td>One-to-one semi-structured interviews (n=11). Subjects identified via three popular platforms.</td>
<td>Extrinsic as well as intrinsic motivational factors, such as social interaction with funder community, are key motivators for participation.</td>
<td>Reward-based and donation-based</td>
<td>Investors and Entrepreneurs</td>
</tr>
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<td>Authors</td>
<td>Title</td>
<td>Description</td>
<td>Focus</td>
<td>Ecosystem</td>
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<tr>
<td>Lehner (2013)</td>
<td>Crowdfunding in a social entrepreneurship context</td>
<td>Literature review of crowdfunding and entrepreneurial finance in an Social Entrepreneurship context</td>
<td>Suggestion of a working scheme for crowdfunding.</td>
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<tr>
<td>Wash and Solomon (2014)</td>
<td>Examining the effect of the all-or-nothing return rule on a crowdfunding marketplace, relative to a direct donation model.</td>
<td>Experiment (n=12) First, under the return rule donors are more willing to contribute money to projects, and in particular high-risk projects, leading to an overall increase in donations. Second, available donations are more spread out over more projects.</td>
<td>Reward-based and donation-based</td>
<td>Platform and Investors</td>
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<tr>
<td>Hazen (2012)</td>
<td>Evaluation of various securities laws and their applicability in the context of crowdfunding</td>
<td>Law review A crowdfunding exemption must be conditioned on meaningful disclosure to give due attention to investor protection.</td>
<td>Equity-based</td>
<td>Regulation</td>
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<tr>
<td>Burtch et al. (2012)</td>
<td>Analysis of the process of consumer decision-making in a crowdfunding context</td>
<td>Analysis of quantitative data collected from different sources (US platform for online journalism; Web traffic;</td>
<td>Contributions are subject to a crowding out effect. This, in turn, suggests that individuals in the studied market are primarily motivated by altruism.</td>
<td>No particular focus</td>
<td>Investors</td>
</tr>
<tr>
<td>Authors</td>
<td>Research Focus</td>
<td>Methodology</td>
<td>Findings</td>
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<tr>
<td>Hemer (2011)</td>
<td>Introduction to crowdfunding in general encompassing the typology of actors, business models, its economic relevance and the implications for start-up finance</td>
<td>Literature review; Web search; Crowdfunding case studies; Interviews</td>
<td>Longer funding durations are found to be associated with higher performance.</td>
<td>Ecosystem</td>
<td></td>
</tr>
<tr>
<td>Schwienbacher and Larralde (2010)</td>
<td>Introduction to crowdfunding as an alternative source of entrepreneurial finance and under which conditions this may be the preferred source of capital for entrepreneurs.</td>
<td>Literature review; Case study ('Media No Mad')</td>
<td>Crowdfunding as a highly dynamic and quickly evolving industry. The author highlights the need for further regulation of the market.</td>
<td>No particular focus</td>
<td></td>
</tr>
<tr>
<td>Agrawal et al. (2011)</td>
<td>Importance of geographical proximity between entrepreneur and the investors for funding success in the context of crowdfunding</td>
<td>Quantitative data analysis. Data set: Sample of 34 artist-entrepreneurs who raised $50,000 on</td>
<td>The results suggest a reduced role of spatial proximity between entrepreneurs and investors. The data indicates an average distance of 3,000</td>
<td>Entrepreneur-Investor</td>
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<tr>
<td><strong>Belleflamme et al. (2011b)</strong></td>
<td><strong>Mollick (2013)</strong></td>
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<tr>
<td><strong>Study of important features of crowdfunding, which build the basis for a proposed model associating CF with pre-ordering and price discrimination.</strong></td>
<td><strong>Investigating the underlying dynamics of success and failure in crowdfunding markets.</strong></td>
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<tr>
<td><strong>Combination of quantitative and qualitative data. A total of 51 data samples and 21 completed interviews were analysed.</strong></td>
<td><strong>Exploratory empirical study based on data from Kickstarter including 48,526 projects with a total funding volume of USD237 million.</strong></td>
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<tr>
<td><strong>Building a community is an essential pre-requisite for crowdfunding to be a viable alternative to traditional forms of finance. Crowdfunding allows for price discrimination in a setting of pre-ordering.</strong></td>
<td><strong>Crowdfunding success appears to be linked to project quality, in that project signalling higher quality level are more likely to get funded, while the a large number of friends on online social</strong></td>
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<td><strong>No particular focus</strong></td>
<td><strong>No particular basis</strong></td>
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<td><strong>Entrepreneur, Investor</strong></td>
<td><strong>Entrepreneur, Investors</strong></td>
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<tr>
<td>Author(s)</td>
<td>Study Overview</td>
<td>Methodology</td>
<td>Findings</td>
<td>Focus</td>
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<tr>
<td>Belleflamme et al. (2013)</td>
<td>This study explores characteristics of individual crowdfunding practices and drivers of fundraising success.</td>
<td>Empirical analysis of quantitative data from 44 crowdfunding transactions combined with questionnaire (n=19)</td>
<td>Insights from the interviews with entrepreneurs suggest that attracting attention on their venture is a key motivational aspect to choose CF over alternative sources of finance. Non-profit organizations tend to be more successful in achieving their target compared to for-profit organizations.</td>
<td>No particular focus</td>
<td></td>
</tr>
<tr>
<td>Giudici et al. (2012)</td>
<td>Studying the crowdfunding phenomenon crowdfunding with the goal of systemizing the current knowledge stock.</td>
<td>Phenomenon-based research approach: combination of literature review, comparison of CF to traditional forms of entrepreneurial</td>
<td>The authors highlight the relevance of problems such as information asymmetries and moral hazard, in an entrepreneurial finance environment. As to date,</td>
<td>Ecosystem focus</td>
<td></td>
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<tr>
<td>Reference</td>
<td>Research Questions and Brief Introduction</td>
<td>Qualitative Analysis of Three Cases: SellaBand, Trampoline, Kapipal</td>
<td>Heterogeneity in Terms of Consumer’s Motivation to Participate in CF. In All Three Cases Interviewees Stated Participation in Innovative Behaviour as an Important Motive (Novelty-Seeking Behaviour). Supporting the Entrepreneur/Project Initiator to Turn His Idea into Reality Was Also Highlighted as a Great Reward. CF Models Can Significantly Affect Value Networks.</td>
<td>No Particular Focus</td>
<td>Investors</td>
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<tr>
<td>Ordanini et al. (2011)</td>
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</table>

**Notes:**
- Crowdfunding is believed to have mainly social and emotional values.
- Ordanini et al. analyse the emerging CF phenomenon to understand the role of consumers as investors in these CF models, and discusses the implications of CF for service organizations.
- Heterogeneity in terms of consumer’s motivation to participate in CF. In all three cases interviewees stated participation in innovative behaviour as an important motive (novelty-seeking behaviour). Supporting the entrepreneur/project initiator to turn his idea into reality was also highlighted as a great reward. CF models can significantly affect value networks.
backer support. Due to a diffusion of responsibility, many potential backers do not contribute to a project that has already received a lot of support because they assume that others will provide the necessary funding. Consistent with the deadline effect widely observed in bargaining and online auctions, it also shows that the bystander effects diminish as the project funding cycle approaches its closing date.

<table>
<thead>
<tr>
<th>Fink (2012)</th>
<th>A discussion of the JOBS Act in relation to the prospect of job creation.</th>
<th>Literature review</th>
<th>Equity-based</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cohn (2012)</td>
<td>A critical discussion of the JOBS Act</td>
<td>Literature review</td>
<td>In short, the implementation of the JOBS Act is a good idea that is being badly executed due to very high burdens imposed on platforms, entrepreneurs and investors.</td>
</tr>
<tr>
<td>Source</td>
<td>Research Question</td>
<td>Methodology</td>
<td>Findings</td>
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<tr>
<td>Griffin (2012)</td>
<td>A critical discussion of the JOBS Act and its implications for equity-based crowdfunding market in the US.</td>
<td>Literature review</td>
<td>Based on such legislation, the idea of equity-crowdfunding is flawed.</td>
</tr>
<tr>
<td>Griffin</td>
<td>Discusses the implications of the JOBS Act for the investors from a very critical point of view. In his discussion paper he highlights the danger of fraudulent behaviour by entrepreneurs and the need to protect investors from losing money. He concludes that equity-based crowdfunding should not be legalized.</td>
<td></td>
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</tr>
<tr>
<td>Kim and Viswanathan (2013)</td>
<td>Kim and Viswanathan examine the role of experts in an online crowdfunding market, particularly the influence of early investors on later investors.</td>
<td>Empirical analysis of dataset taken from Appbackr comprised of 532 apps listed by 396 app developers.</td>
<td>While early investors have a significant influence on later investors, two categories of experts – app developer investors and experienced investors – have a significant influence on later investors – the crowd.</td>
</tr>
<tr>
<td>Australia</td>
<td>A snapshot analysis of the reward-based crowdfunding market. This research was focused on the evaluation of the impact of reward-based crowdfunding on entrepreneurs, investors, and platforms.</td>
<td></td>
<td>The evaluation of the impact of reward-based crowdfunding on entrepreneurs, investors, and platforms.</td>
</tr>
<tr>
<td>Council for the Arts (2012)</td>
<td>current state of the Australian crowdfunding market</td>
<td>interviews delivers valuable insights into potential barriers to donation, such as a perceived gap in the entrepreneurial team, missing tax incentives or the general reluctance of pledging money through the internet. Additionally, underlying motivational factors are presented, including the desire to help creative people, the personal affiliation with the entrepreneur, the participation in cultural production or social kudos.</td>
<td>based on interviews combined with 17 semi-structured interviews.</td>
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<tr>
<td>Author</td>
<td>Title</td>
<td>Methodology</td>
<td>Highlights</td>
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<tr>
<td>Aitamurto (2011)</td>
<td>The rise of crowdfunding and its implications for journalism.</td>
<td>Case study: Spot.Us, a platform to crowdfund journalism. A total of 7 interviews with reporters and 8 interviews with donors were conducted.</td>
<td>The act of participating in crowdfunding seems to be more important than the actual journalistic output. The reasons for contributing donations to a pitch are more altruistic than instrumental in nature.</td>
</tr>
<tr>
<td>Giudici et al. (2013)</td>
<td>The study intends to shed some light on the impact of the entrepreneur's social capital, on the likelihood to achieve the targeted funding goal.</td>
<td>Empirical analysis of a data sample consisting of 461 crowdfunding projects collected from 11 Italian crowdfunding platforms.</td>
<td>Individual social capital has a significant positive effect on the probability to reach the funding target, while geolocalized capital has no significant effect. Territorial social capital may be detrimental for crowdfunding, since it marginally weakens the signalling effect of the individual social capital.</td>
</tr>
<tr>
<td>Mitra (2012)</td>
<td>This brief study seeks to examine the role of crowdfunding in the funding of start-ups.</td>
<td>Literature review</td>
<td>This paper delivers a broad introduction to the concept of crowdfunding and a brief discussion of the legal barriers to equity-based crowdfunding</td>
</tr>
<tr>
<td>Authors</td>
<td>Study Description</td>
<td>Methodology</td>
<td>Results/Findings</td>
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<tr>
<td>Kortleben and Vollmer (2012)</td>
<td>A comprehensive report discussing the prospective impact of Crowdinvesting in the sphere of entrepreneurial finance.</td>
<td>Literature review and case study analysis: Innovestment, a prominent German platform.</td>
<td>Kortleben and Vollmer delivered one of the most compelling introductions to the field of equity-based crowdfunding in the context of entrepreneurial finance and in comparison with alternative forms of risk capital. Thus, the study provides an thorough understanding of the mechanisms underlying this new phenomenon.</td>
</tr>
<tr>
<td>Mäschle (2012)</td>
<td>This paper focuses on the competition among CF platforms and its impact on the disclosure requirements imposed on the entrepreneurs offering equity on CF platforms.</td>
<td>A simple three-stage theoretical model is used to demonstrate competition among equity CF platforms should lead to a maximization of disclosure requirements.</td>
<td>Factors with high relevancy for maximization of disclosure: Balance sheet information, human capital (education, work experience, demographics), firm-specific information (size, legal form, ownership structure, industry, geographical location)</td>
</tr>
<tr>
<td>Ahlers et al. (2013)</td>
<td>Ahlers et al. study can be regarded as the first attempt to</td>
<td>Empirical analysis of data consisting of a</td>
<td>Results highlight the fact that retaining equity and providing</td>
</tr>
<tr>
<td>Source: Best et al. (2013)</td>
<td>A first attempt to estimate the size of the debt and equity crowdfunding market.</td>
<td>A set of comparisons, assumptions and estimates.</td>
<td>Depending on the applied data reference, CFI market size is estimated to range from USD184 million to USD1.59 billion.</td>
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</table>
| Source: Mollick (2013)   | An examination of the role of quality signals, along with other determinants of successful crowdfunding compared to VC investment criteria. | Empirical study of 2,101 high-technology projects derived from Kickstarter. | Overall the results suggest that CF investors respond to similar signals of quality as VC Investors.
  1. Past evidence of success is predictive of successful funding.
  2. Outside endorsements significantly increase | Reward-based | Entrepreneur, Investor |
<table>
<thead>
<tr>
<th>Study</th>
<th>Description</th>
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<th>Findings</th>
<th>Focus</th>
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<tr>
<td>Gerber and Hui (2014)</td>
<td>Study to explore the motivations and deterrents for participation in crowdfunding.</td>
<td>Exploratory research based on semi-structured interviews (n=83)</td>
<td>Supporters are motivated by the desire to collect rewards, help others, to support good causes and to be part of a community. Deterrents to participation include amongst others lack of trust.</td>
<td>Rewards-based Entrepreneurs, Investors</td>
</tr>
<tr>
<td>Agrawal et al. (2013)</td>
<td>The paper illustrates how economic theory – such as transaction costs, reputation, and market design, can explain the rise of non-equity crowdfunding and offer a literature review.</td>
<td>Literature review</td>
<td>1. Funding is not geographically constrained 2. Funding is highly skewed 3. Funding propensity</td>
<td>No particular focus Ecosystem</td>
</tr>
<tr>
<td>Hagedorn and Pinkwart (2013)</td>
<td>Introduction to crowdfunding and crowdinvesting, based on the German market. Terminology, process and motivations.</td>
<td>Literature review</td>
<td>Equity-based</td>
<td>Ecosystem</td>
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<tr>
<td>Klöhn and Hornuf (2012)</td>
<td>Crowdinvesting in Germany: market overview, regulatory environment and perspective on future developments.</td>
<td>Literature review</td>
<td>Crowdinvesting offers both significant opportunities and challenges and current regulation does not provide a framework to utilize crowdinvesting at its full potential.</td>
<td>Equity-based</td>
</tr>
<tr>
<td>Ley and Weaven (2011)</td>
<td>Exploration of due diligence processes involved in the setting of crowdfunding compared to insights from Venture Capital.</td>
<td>Exploratory research based on in-depth interviews (n=11)</td>
<td>This research provides a preliminary guide to assist entrepreneurs in how to appropriately engage with crowdfunding capital sources in the context of start-up finance. As such, this research provides the first criteria in identifying appropriate start-ups for crowdfunding. That is, start-ups with high information sensitivity, complex due diligence requirements, and a long duration before an available exit would not be appropriate candidates in accessing finance through crowdfunding models.</td>
<td>Equity-based Entrepreneurs, Investors</td>
</tr>
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### 12.2 Appendix 2: Literature Overview Business Angel

<table>
<thead>
<tr>
<th>Study</th>
<th>Method</th>
<th>Sample size</th>
<th>Mgmt skill &amp; (industry) experience</th>
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<th>Track record</th>
<th>Mgmt stake in firm</th>
<th>Integrity/ Trustworthiness</th>
<th>Technology knowledge</th>
<th>Personal Motivation/ Passion/ Commitment</th>
<th>Personality</th>
<th>Entrepreneur/ Team characteristics</th>
<th>Product/ service characteristics</th>
<th>Financial characteristics</th>
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<td>Questionnaire</td>
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<td>x</td>
<td>x</td>
<td>x</td>
<td>x</td>
<td>Mgmt skill &amp; (industry) experience</td>
<td>Product attributes</td>
<td>Cash-flow</td>
<td>Business Plan</td>
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<tr>
<td>Mason and Harrison (1996a)</td>
<td>Interviews</td>
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<td>x</td>
<td>x</td>
<td>x</td>
<td>x</td>
<td>x</td>
<td>x</td>
<td>x</td>
<td>x</td>
<td>Venture team</td>
<td>Proprietary rights/ protectability</td>
<td>Cash-out method/ Exit</td>
<td>Entrepreneur fit</td>
</tr>
<tr>
<td>Landström (1998)</td>
<td>Conjoint Analysis</td>
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<td>x</td>
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<td>x</td>
<td>x</td>
<td>x</td>
<td>x</td>
<td>x</td>
<td>Track record</td>
<td>Growth potential</td>
<td>Expected ROR/ ROI/ Valuation</td>
<td>Business fit</td>
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<tr>
<td>Feeney et al. (1999)</td>
<td>Qualitative study</td>
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<td>x</td>
<td>x</td>
<td>x</td>
<td>x</td>
<td>x</td>
<td>x</td>
<td>x</td>
<td>Mgmt stake in firm</td>
<td>Product Interest/ benefits</td>
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<td>Location</td>
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<td>Financial characteristics</td>
<td>Venture creates new market</td>
<td>Investment fit</td>
<td>Business Plan</td>
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**Entrepreneur/ Team characteristics**

- Mgmt skill & (industry) experience
- Venture team
- Track record
- Mgmt stake in firm
- Integrity/ Trustworthiness
- Technology knowledge
- Personal Motivation/ Passion/ Commitment
- Personality

**Product/ service characteristics**

- Product attributes
- Product differentiation
- Proprietary rights/ protectability
- Growth potential
- Product Interest/ benefits
- Market acceptance/ market validation
- Innovation/ quality
- Platform/ Development risk

**Market characteristics**

- Market size
- Supply/ distribution
- Market growth/ potential
- Barriers to entry

**Competitive threat/advantage/ market dynamics**

- Venture creates new market

**Financial characteristics**

- Cash-flow
- Cash-out method/ Exit
- Expected ROR/ ROI/ Valuation
- Expected risk
- Percentage of equity
- Plan/ presentation
- Investor provisions
- Size of investment
- Liquidity

**Investment**

- Entrepreneur fit
- Business fit
- Location
- Referral source
- Co-investment
- Investor role

**Other**

- Business Plan
- Endorsements (FFF investment, mentors etc)
### Appendix 3: Literature Overview Venture Capital

#### Study

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<tr>
<th>Method</th>
<th>Personal interviews</th>
<th>Questionnaire</th>
<th>Phone survey and questionnaire</th>
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#### Notes

- **Wells (1974)**
- **Poindexter (1976)**
- **Tyebjee and Bruno (1984)**
- **MacMillan et al. (1987)**
- **Robinson (1987)**
- **Timmons et al. (1987)**
- **Hall and Hofer (1993)**
- **Silva (2004)**
12.4 Appendix 4: Suggested Disclosure Requirements

<table>
<thead>
<tr>
<th>1. Disclosure requirements for companies younger than two years old</th>
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<tr>
<td>a) Disclosure requirements for balance sheet data</td>
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<td>Required information to create an opening balance sheet:</td>
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<td>- Bills of tangible fixed assets (machines etc.)</td>
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<td>- Certificates of intangible fixed assets (patents etc.)</td>
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<tr>
<td>- Bills of operating expenses (heating costs etc.)</td>
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<td>b) Disclosure requirements for human capital information</td>
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<td>Identity cards of members of the entrepreneurial team</td>
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<td>Certificates of education, apprenticeship and employment</td>
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<td>Certificates verifying self-employed experience</td>
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<td>Credit reports like German “Schufa-Auskunft”</td>
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<td>c) Disclosure requirements for firm characteristics</td>
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<td>- certificate of legal form and</td>
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<td>- pre-investment ownership structure</td>
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<td>Tenancy agreement as</td>
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<td>- certificate for the geographical location</td>
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<td>Labor agreements as</td>
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<td>- certificate for the number of employees</td>
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<tr>
<td>Industry-specific authorization or fellowships as</td>
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<td>- certificate of industry affiliation</td>
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</table>

| 2. Additional disclosure requirements for companies older than two years |
| Complete balance sheets of the last two fiscal years            |

Source: Mäschle (2012)
February Newsletter

Fueling Great European Startups

At the end of last year, we announced that Seedrs is open to entrepreneurs and investors throughout Europe. We have already had members from every EU country join Seedrs, but now we are beginning our on-the-ground outreach efforts to spread the word and develop our community across the multiple European startup hubs.

We kicked off in Latvia, where we took part in the mini-Sendcamp, attended the Techsale Robotics conference and met entrepreneurs at TechHub. There is incredible talent and a close-knit eco-system developing in the area. We’re keeping an eye on the blog over on our blog.

And, just returned from Paris, where we met with incredible leaders in the French startup scene and some interesting startups. We look forward to heading back in the next few months to catch up and see even more people. If you’re based in France and want to meet with us when we’re back in Paris, please let us know.

Meanwhile, on the other side of the world, we gave a talk at the Stanford Engineering School to the European Entrepreneurs at Stanford group about how equity crowdfunding. You can watch our talk here.

February Funding

This month has seen four more fantastic startups reach and exceed their investment targets. We’re really excited that two of them are led by female founders and one of them...

Be a Part of Groundbreaking Research

Interest in equity crowdfunding is spreading quickly throughout Europe. To get a better understanding of investor motivations and interests, we’ve partnered with students from Copenhagen Business School and the Danish Crowdfunding Association to briefly interview crowdfunding investors.

If you’d be interested in helping shape the future of startup investing in Europe, please visit their webpage to learn more and to share your availability for a brief interview.
# 12.6 Appendix 6: Interview Guide

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<tr>
<th>Interview Question</th>
<th>Guiding questions</th>
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<td>2. Profession</td>
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<td></td>
<td>3. Education (Entrepreneurship?)</td>
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<td>4. Nationality</td>
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<tr>
<td>What is your experience with entrepreneurial finance and/or stock market investments?</td>
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<td><strong>2. EXPERIENCE WITH CROWDINVESTING</strong></td>
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<td>How did you get involved with crowdinvesting?</td>
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</tr>
<tr>
<td>In how many ventures have you invested?</td>
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<td>What is your average investment size?</td>
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<tr>
<td><strong>3. INVESTMENT PROCESS</strong></td>
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<tr>
<td>Now, try to think back to your last investment.</td>
<td>1. How long time did you take to finish the whole process?</td>
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<tr>
<td>Can you try to take us through your investment process, from screening opportunities to the actual investment?</td>
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<tr>
<td>a. SCREENING</td>
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<tr>
<td><strong>How are you searching/finding your investments?</strong></td>
<td>1. Do you have any industries you favor more than other?</td>
</tr>
<tr>
<td>---------------------------------------------------</td>
<td>---------------------------------------------------------</td>
</tr>
<tr>
<td><strong>b. SELECTION</strong></td>
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<td>How did you identify your last investment?</td>
<td>1. In your opinion what makes a good investment opportunity?</td>
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<td>Can you explain your due diligence?</td>
<td>2. Do you have any criteria that you use to evaluate the opportunity?</td>
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<td>3. How did you evaluate the risk involved in the investment?</td>
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<td>4. What information are you looking at?</td>
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<td><strong>c. INVESTMENT</strong></td>
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<td>How did you decide on the amount you invested in the opportunity?</td>
<td>1. Do you feel comfortable sharing the amount you invested in the venture?</td>
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<td>Are you looking for additional information outside the platform?</td>
<td>1. Are you Googling the entrepreneurs or checking other online information?</td>
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<td>Can you mention the top three criteria that you evaluate?</td>
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<td><strong>d. POST INVESTMENT</strong></td>
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<td>How has your experience been after you made the investment?</td>
<td>1. Have you been actively involved with the project?</td>
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<td></td>
<td>2. Is there anything you miss involvement on?</td>
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<td>Will you invest in equity crowdfunding again?</td>
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