

The reality and prospects of crowdfunding for startups in the digital transformation era

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Abstract:

This research paper aims to investigate the role of crowdfunding models in assisting startup companies' fundraising efforts in the era of social media networks, electronic marketing, and digital transformation. This will be achieved through a comprehensive review of the literature, focusing on the evolution of digital transformation phases and the dynamics of startups in the application of crowdfunding platforms.

This study assessed the global crowdfunding market at USD 19.86 billion in 2023. Startups account for 55 percent of this market. It is expected to expand from USD 22.12 billion at the end of 2024 to USD 72.88 billion by 2032, displaying a compound annual growth rate (CAGR) of 16.1% during the forecasting period (2024-2032).

Keywords: Digital Transformation, crowdfunding, Startups, digital platforms.

Jel Classification Codes: G240, G230, D9.

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1. INTRODUCTION

In the digital transformation era, crowdfunding has emerged as a dynamic and accessible method for startups to secure funding and gain market validation. This paper explores the multifaceted perspectives of crowdfunding, highlighting its significance in empowering entrepreneurs, democratizing investment opportunities, and fostering innovation. By leveraging digital platforms, startups can reach a global audience, build a community of supporters, and navigate the complexities of modern market demands. This study delves deeply into the various crowdfunding models, showing the role of technology in enhancing crowdfunding processes, and the impact of this funding method on the startup ecosystem in a rapidly evolving digital landscape.

On the other hand, Crowdfunding platforms have paved the way for individuals and organizations to raise funds for various projects and ventures. By influencing the power of the internet and social media, these platforms enable entrepreneurs, artists, non-profits, and others to reach a vast audience of potential backers. Unlike traditional funding methods, which often rely on a small pool of wealthy investors or financial institutions, crowdfunding democratizes the fundraising process, allowing anyone with an idea to solicit donations from a large number of people worldwide.

In addition, Startups can also choose to raise funding through crowdfunding platforms, where they pitch their business idea to a large number of investors who can contribute small amounts of money to the project. For example, Kickstarter company has conducted over USD 815.0 million from 4.9 million funders to roughly 50k projects worldwide since 2009. (fortune business in sights, 2024). Meanwhile, securing funding is a crucial aspect of launching and growing a successful startup, as it provides the necessary resources to bring the company's vision to life in widespread.

So, what are the prospects and the future of crowdfunding for startups in the digital transformation age?

Objectives

1.To define the concept of crowdfunding in the digital transformation era.

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2. To study the opportunities and challenges that startups face in the fierce competition worldwide.

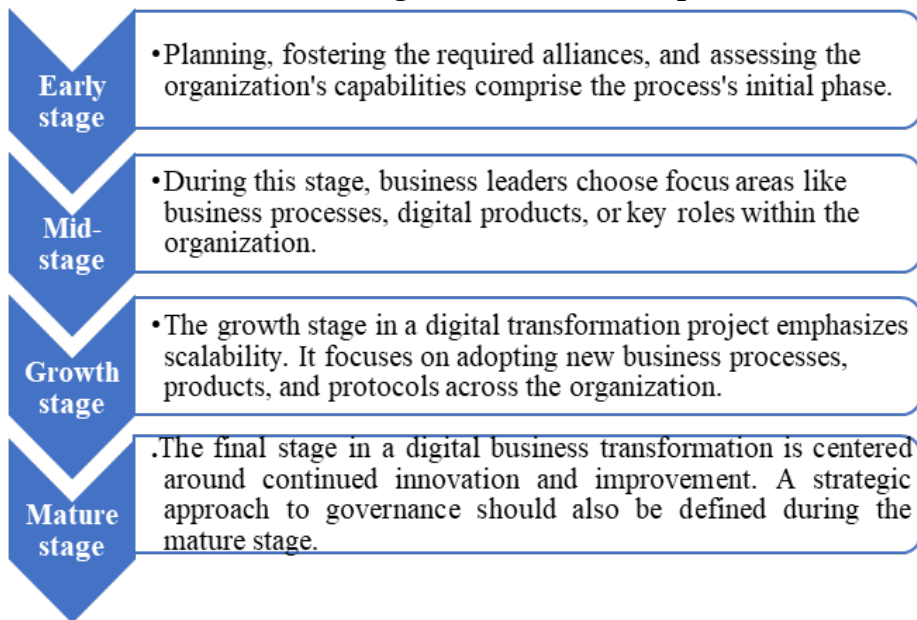
3.To discuss the future of crowdfunding in promoting startups.

2. The Digital Transition and Crowdfunding Concepts

2.1 The digital transition concepts

Digital transformation efforts look different from one industry to another. However, the overall digital transformation process can be broken down into four phases: (Coursera 2023).

Table01: digital transformation phases



Source Developed by researchers.

2-2-The Benefits of Digital Transition

The benefits of digital transformation include: (managed Outsourcing solutions 2022).

- Increased accuracy and higher productivity by reducing cost and time.
- Agility and efficiency in business operations using automation processes.
- Increases opportunities for growth in large markets.
- Better customer engagement and satisfaction by exploring

consumer needs.

- Higher revenue and profits thanks to machine learning, cloud computing, and blockchain.

Briefly, the notion of Digital Transition encompasses a wide range of technologies that enhance numerous services and commodities. Examples include applications, television series, chatbots, and so forth. By the way, implementing the crowdfunding approach can enable enterprises to rely on the internet to immediately receive financial aid from the public as a replacement for seeking financial support from investors. (Muhammad, Ahmad, & Muhammad K, 2017)

2-3 -What Crowdfunding Is?

At its foundation, the phrase "crowdfunding" derives from the more commonly recognized term "crowdsourcing," which comprises leveraging the "crowd" to gather ideas, opinions, and solutions for business operations. (Muhammad, Ahmad, & Muhammad K, 2017). As alternative finance

Crowdfunding is an Internet-enabled approach for companies or other entities to receive capital in the form of gifts or investments from a number of individuals. (The World Bank, 2013, p. 08).

Crowdfunding uses web-based technology and the knowledge and wisdom in communities to determine which projects should receive funding and how much funding they should receive, as well as providing real-time feedback on start-ups and small businesses. It leverages the power of technology, particularly social media, to market the idea, raise funds, and hold entrepreneurs accountable. (The World Bank, 2013, p. 14).

Crowdfunding is one technique by which individuals, organizations, and businesses, including startups, can raise funds from the public to support a project, cause, or person.. (www.fca.org.uk, 2023).

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Table02: Crowdfunding Models

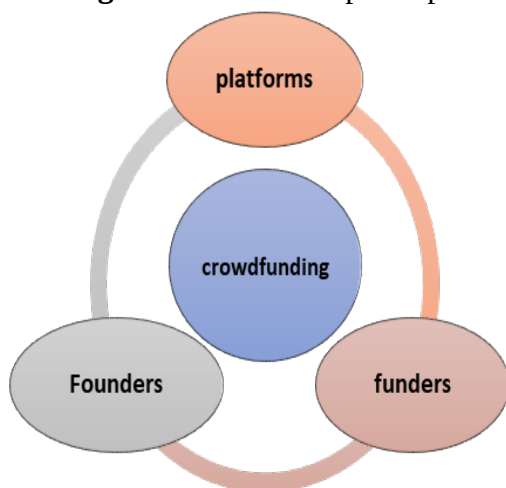
Crowdfunding Models	Description	Examples of Cf platform
Donation - based Cf	funders donate without expecting monetary	<u>GlobalGiving</u> , <u>JustGiving</u> ,
equity-based Cf	funders receive equity instruments or profit-sharing arrangements.	<u>GrowVC</u> , <u>Upstart</u> , crowdfunding
lending-based Cf	funders receive debt instruments that pay a fixed rate of interest and return principal on a specified schedule.	<u>Kiva</u> , <u>Zidisha</u> , lending club, Prosper
Reward-based Cf	funders receive a token gift of appreciation or pre-purchase of a service or product. This model is evolving into a marketplace of its own, with a firm raising considerable sums through pre-sales.	Kickstarter, Indiegogo,
royalty-based Cf	funders receive a share in a unit trust, which acquires a royalty interest in the intellectual property of the fundraising company.	Royalty Exchange, <u>SongVest</u> , Royalty Flow,

Source: Developed by the researchers depending upon (The World Bank, 2013, p. 20).

2-4- The Crowdfunding's Benefits and Challenges

❖ **The benefits:** crowdfunding is a decentralized funding model that relies on collective contributions. The three primary participants in the crowdfunding process founders, crowdfunding platforms, and funders benefited from crowdfunding as follows. (The World Bank Group, 2017).

Figure 01: The main participants in crowdfunding



Source: Developed by the researchers.

a. Founders: The capacity of crowdfunding to give business owners new sources of income is one of its main advantages. With crowdsourcing, entrepreneurs may access a larger pool of possible investors instead of depending just on conventional sources like bank loans or venture capitalists. This raises the project's chances of financing and encourages the growth of a network of supporters who care about its success. (Faster Capital, 2024). Crucial outcomes for business entrepreneurs also include gender agnosticism, access to early-stage support networks, market testing, demand assessment, and connections to the diaspora. Founders also learn more about potential demand creation. Product demand is measured through crowdfunding, especially pre-sale crowdfunding. Additionally, because both unsuccessful and successful ideas are represented, crowdfunding offers a useful window for researching emerging entrepreneurial endeavors. It makes it possible to evaluate and contrast a wide range of novel business ventures.

b. Platforms: The majority of platforms are for-profit businesses that normally take a cut of the fundraising amount as a service charge. Their job is to act as a liaison between investors and entrepreneurs. The goal of these platforms is to enhance the quantity of initiatives that succeed. However, they also make an effort to present financiers with creative and feasible initiatives as well as investment opportunities. Give them access to

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transparent data as well.

c. funders: Funders may support a project for a variety of reasons, such as political, social, or humanitarian goals; they may also do so in anticipation of benefits, ownership stakes, or set returns. Whereas funders earn interest in loan crowdsourcing, they acquire ownership in equity crowdfunding. Several incentives are available with reward-based fundraising, including early access to items and recognition. Another important factor is philanthropy, where some donors support initiatives without anticipating financial gain. Equity crowdfunding has gained legitimacy and is now a realistic investment alternative, enabling donors to become investors.

❖ **The Challenges:** Funders' Prospective Disclosure Issue: Crowdfunding necessitates making ideas public, exposing them to the public, and forfeiting their confidentiality, in contrast to obtaining cash from personal sources like family, friends, or venture capitalists, where the entrepreneur maintains their ideas private. While this is not an issue for initiatives that are altruistic, charitable, or patronage-based, it is a severe challenge for creative product concepts or entrepreneurial businesses. (Muhammad, Ahmad, & Muhammad K, 2017, p. 1302)

Moreover, inadequate professional assistance. When venture capitalists or angel investors contribute money to a project, they also offer other advantages, such as expert advice on how to launch a profitable company in the industry in which entrepreneurs already operate or want to operate. Founders cannot get these kinds of perks from unlicensed fund providers.

The ineptitude of crowdfunding entrepreneurs is another problem. Sometimes a concept appears to be extremely good and has the potential to draw in a lot of investors, but the creator lacks the necessary skills to successfully turn the idea into reality.

3. What A Startup Is?

The term startup denotes a corporation in the first stages of activities. A lot of entrepreneurs launch startups to create a good or service that they think there will be a market for. These businesses typically begin with large

expenses and little income, so they search for funding from a range of sources, including angel and venture capitalists. (GRANT 2022).

3-1 Start-up Features

- ☞ A startup is a business in its early development stages.
- ☞ Founders typically fund their startups initially and may seek external investment to help launch their venture.
- ☞ Funding sources include family and friends, venture capitalists, crowdfunding, angel investors, seed funding, and loans.
- ☞ Startups are high-risk due to the potential for failure, but they offer unique work environments with significant benefits, a focus on innovation, and excellent learning opportunities.

3-2 Advantages and Disadvantages of Startups

There are several benefits to being employed by a startup. There are two: chances for development and increased accountability. Because startups sometimes employ fewer people than larger, more established organizations, employees at startups occasionally take on a range of duties and wear numerous hats. This fosters accountability and generates educational opportunities. (GRANT 2022).

Table03: pros and cons of startup entrepreneurship.

Pros	Cons
☞ More opportunities to learn. ☞ Increased responsibility. ☞ Flexibility. ☞ Workplace benefits. ☞ Innovation is encouraged.	☞ Risk of failure. ☞ Having to raise capital. ☞ High stress. ☞ Competitive business environment.

Source: Developed by researchers according to (GRANT 2022).

A technical startup provides technology solutions to improve the speed, security, and convenience of operations and services. (MacDonald Ventures 2021). A startup company is an entrepreneurial venture in the initial stage of its operations. (Wilhelm 2018). Moreover, the management

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and employees in start-ups generally have real ownership (shares) or options and thus often feel a strong responsibility for their firm, especially in branding. (Picot, et al. 2018, 36).

Furthermore, Motives to establish a start-up are to get the freedom to work on projects that have meaning in your life, be your boss, tap into creativity, share your talents with society, etc. (Meghasham 2021).

3-3- Startup stages:

There are many stages to achieve a "fully-fledged" company including the following: (Wilhelm 2018).

Table04: Startup Development stages

Pre-Seed	•A Pre-Seed round is a pre-institutional seed round that either has no institutional investors or is a very low amount, often below \$150k.
Seed	•A seed round is a type of funding round usually raised by a new company to support early product development and market research
Series A	funding round for established companies in which start-ups allow for investment in the company by venture capital firms or angel investors
Series B	•Private equity and/or venture capital financing round.
Series C	Series C round is a private equity and/or venture capital financing round.
Series D	•Private equity and/or venture capital financing round
Series E	Private equity and/or venture capital financing round
IPO	•An initial public offering (IPO) refers to the process of offering shares of a private corporation to the public in a new stock issuance.

source: Developed by researchers.

3-4- Characteristics of Startups:

Startups tend to share several characteristics that serve to distinguish them from small businesses:

- **Creativity:** Startup businesses are often formed around a novel concept, approach, or product. While technology enables the products and services that startups provide, not all firms are founded on distinct, defensible intellectual property.

- **Risk:** Startup businesses are sometimes found on the outskirts of a technical sector or market for their product or service. Startup enterprises fail at a high rate due to their tiny size, and limited resources.

- **Scale:** startups are built from a management and economic sense to grow beyond their initial markets and service widely their clients.

- **Speed:** Small team sizes and flat organizational structures enable startup teams to make decisions fast and grab market opportunities. Due to limited accessible resources.

3-5 Incubators VS. Accelerators of Startups.

There are many significant differences between incubators and accelerator startups as follows: (Sandner 2023).

- ❖ **Startup Incubator:** A startup incubator program focuses on assisting startups in their early stages of foundation. It provides guidance, training, networking opportunities, and sometimes funding. start-up incubators play a crucial role in the root stages as well as in the ongoing growth road.

- ❖ **Startup Accelerator:** A startup accelerator program is designed to assist firms scale once they have established product-market fit. It provides counsel, training, networking opportunities, and occasionally money, with a particular emphasis on. In addition, they give start-ups the key strategies to deal with many issues they face in their business lives. Startup accelerators are considered the cornerstone of supporting training and enforcing networking among small and medium companies. Furthermore, startup accelerators may fund some start-ups were face setbacks.

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TABLE05: incubator, accelerators similarities and differences

	Startup Incubator	Startup Accelerators
Focus	achieving product-market fit that matches the founders' capabilities.	Target the growth phase and rapid expansion.
Content	Training courses with experienced experts in startups are provided by the materials.	Expert guidance is offered by programs to help startups raise seed capital.
Startup Stage	Applicants for the initial foundation.	Appropriate for startups that have already gained their first customers.
Product	During the incubation stage, startups are not required to have a developed product.	Acceleration-stage startups must have either an MVP or a developed product.
Equity	Most startups keep most of their equity; the typical equity request is between 4-15%.	Startups retain the majority of their equity, just like incubators. The typical equity request is 5-15%.
How to Participate	Entrepreneurs can apply for incubator programs with their skills, ideas, or startups.	Startups have the option to apply for acceleration of programs for their existing business.
Team	both individuals and teams to apply to incubator programs.	Commonly, startups applying to an accelerator will already have a core team,
End Goal	The primary goal of incubators is to help startups reach product-market <u>market</u> .	Accelerators prioritize assisting startups in scaling massively and preparing for further investment.

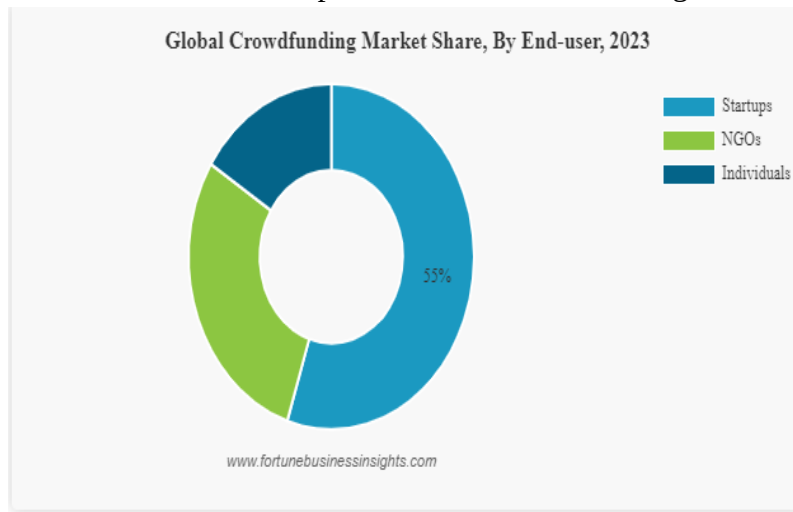
Source: Developed by researchers.

4- The Crowdfunding Method for Startup Companies

According to end-user, in 2024 the crowdfunding market will be divided into startups, (non-government organizations) NGOs, and individuals. In 2023, the startup segment held the largest market share,

which enabled them to test their ideas and products in the market without the need for a final Minimum Viable Product (MVP). Startups assist in the development of new products, financial support, and feedback from investors and potential users on a single platform.

FIGURE 02: The startups' share from crowdfunding in 2023.



Source: (Fortune Business Insights, 2024).

Within the course of this project, crowdfunding software provided by firms such as GoFundMe, Kickstarter, Indiegogo, Inc., Double the Donation, Fundable, and others was taken into account. Groups may easily share a project or cause on their social networks by using online social.

According to the Arora Project, a website that monitors crowdfunding efforts and data, over USD 215 million was invested in businesses using equity crowdfunding platforms this year. It will have grown by almost USD 200 million by May 2024 compared to the same time last year. (Mordor intelligence, 2024).

5 - Prospects of Crowdfunding: Market Size and Growth

5-1 The global Market size of Crowdfunding.

Global market research and consulting firm Polaris Market Research projects that the crowdfunding industry will grow to a value of USD 19.86 billion by 2023.

Under the projected period (2024-2032), it is anticipated to expand at a compound annual growth rate (CAGR) of 16.1%, from USD 22.12 billion

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in 2024 to USD 72.88 billion by 2032. (Polaris Market Research, 2024). In the meanwhile, the worldwide crowdfunding industry was estimated by the International Industry Analysis Research and Consulting Group (IMARC Group) to be worth US\$ 16.5 billion in 2023. According to the IMARC Group, the market will expand at an average annual rate of 11.26% from 2024 to 2032, reaching US\$ 42.9 billion. The market is expanding steadily as a result of the industries' growing digitization, which makes operations more efficient and creates new opportunities.

Globally, the market is changing in favor of sustainable and moral business practices as well as deliberate international growth. (Bahri , Benbouziane , 2023).

5-2- The geographical market size of crowdfunding

In 2023, the worldwide crowdfunding industry was estimated to be worth USD 19.86 billion. According to projections, the crowdfunding industry will expand at a compound annual growth rate (CAGR) of 16.1% from USD 22.12 billion in 2024 to USD 72.88 billion by 2032. (Polaris Market Research, 2024).

FIGURE 03: The geographical market size of crowdfunding

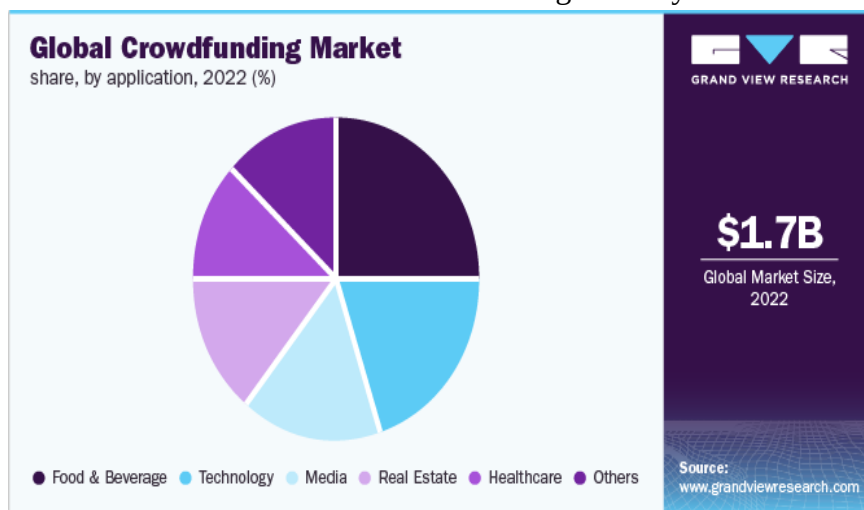


Source: (Polaris Market Research, 2024).

5-3- Crowdfunding Share by Field

The food and beverage category led the market, accounting for more than 24.0% of worldwide revenue in 2022, according to the grand perspective study displayed in Figure 4. The rising number of food and beverage startups globally is responsible for the segment's rise. To get more traction in the market, food companies are growing their businesses. For example, in November 2022, the macaroni and cheese producer 8 Myles announced an equity crowdfunding effort to collect funds for brand recognition, and production equipment purchases to improve capacity and operational expansion.

FIGURE 04: Crowdfunding share by field



Source: (Grand View Research, 2024)

Furthermore, beverage companies such as Waku have launched a crowdsourcing initiative to support their growth strategies. (Grand View Research, 2024). Cutting-edge technologies like artificial intelligence (AI), blockchain, and machine learning are becoming more and more popular in the end-use business, and they are predicted to increase significantly in the next years. Blockchain technology improves security and transparency across a range of sectors, including the Internet of Things, cybersecurity, healthcare, and finance. The segment's expansion may be ascribed to the rise in technology businesses' fundraising efforts as the need for cutting-edge technologies in a variety of applications grows. (Grand View Research, 2024).

5- Conclusion:

In summary, this study shows how important crowdsourcing is for helping people or enterprises obtain funding that banks and other lenders are either unable to supply or would only do so at a significant cost. Customers may get joy from helping a business or project grow, from supporting a community initiative, or from helping other people. Crowdfunding strategies may be strengthened by digital transformation, which may also result in higher returns than traditional financial services.

The digital revolution has had a specific impact on startups, notably in the areas of digital marketing, customer experiences, and fostering investor confidence in creative idea owners. According to the research, incorporating digital transformation calls for a well-rounded strategy that makes sure that technology innovation is in line with moral behavior and long-term corporate expansion.

Due to its success in assisting individuals, communities, and several businesses operating in the digital sphere, the crowdfunding industry is expanding rapidly, particularly in the donation-based financing sector. As such, it's a great method for new businesses to make money and build their following. Before making a complete commitment, it's also a smart technique to find out if clients are interested in company ideas.

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