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Equity crowdfunding: Crowdcube

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INTRODUCTION

My thesis is structured in three chapters and respectively in the first chapter there are eight paragraphs, in the second four and in the third and last one there are three.

The aim of my thesis is to analyse possible trends observing the interactions between investors and entrepreneurs on one of the most important platforms of crowdfunding in the world, "Crowdcube".

Firstly I decided to report a general introduction on the crowdfunding phenomenon, focusing on the history, on the different models and platforms which are currently available on the web.

Later I collected a part of the empirical background and I analysed the literature available on the web regarding this phenomenon and I explained the process of crowdfunding.

This topic is very new, that is why scholars have started discussion on that just in the current years, some of them have classified different types of crowdfunding, others focus on the role of female investors in this area, but also some analyse the information asymmetry between investors and crowdfunders.

In the second part of my thesis I focused on a particular type of crowdfunding, that is called "equity-based crowdfunding", in which investors obtain shares of the companies in return for their financing, wishing for successful exits in the coming years.

Later, I moved on focusing on the platform of "Crowdcube" itself and how it works.

I also focused on the taxation part and on the LCIF, a particular London-based fund that invests in best startups.

At the end, in the last chapter of my thesis I moved on the "Empirical Research" area, in which I properly analyse the interactions between investors and entrepreneurs with the aid of my dates, collected in time on Crowdcube site. Resuming, I collected dates on twenty-six campaigns launched on Crowdcube and in the last paragraph of my thesis I used the results of my analysis for revealing some tendencies.

Also referring to the literature review, I compared tendencies I found on past analysis of scholars and it emerged there is a link between these two.

1. Crowdfunding: An overview

In this first chapter I want to analyse in general the new phenomenon of crowdfunding. Explaining in details the history, the platforms, the process, I also report the empirical background of the phenomenon and the literature review.

1. 1 Definition

Crowdfunding is defined as a gathering of funds raised, principally via internet, from little contributes by the “crowd”, which is a group of people that are liked by common interests or common projects or that are people willing to support an innovative idea (<http://www.investopedia.com/terms/c/crowdfunding.asp>).

1. 2 History

Crowdfunding has a relatively old origin, there I list some of the most important cases from the sixteenth century up to nowadays.

A case of crowdfunding is when in the 1730s London's mercantile community saved the Bank of England supporting the currency until confidence of the population in the pound was restored, while all the people were trying to change their pounds into gold. Also in 1885 a newspaper-led campaign raised small donations from 160,000 donors to invest that amount in building the base of the Statue of Liberty because the government funding campaign failed.

Nowadays crowdfunding is much related to social media, crowdfunding is even used to raising funds in the music field or in the film industry but also for videogames, for instance, two famous cases are the videogames “Bloodstained: Ritual of the Night” and “Shenmue III”, which both obtained the required funds from Kickstarter.

1. 3 Models

There are two most common types of crowdfunding:

Rewards crowdfunding

Entrepreneurs without incurring in loans or sacrificing part of the shares, just presell a product to analyse the response of the crowd to the concept.

Equity crowdfunding

Investors receive shares or equity in return for the money pledged.

Other types of crowdfunding that occur:

Software value token

Another kind of crowdfunding is to raise funds for a project where a digital or software-based value token is offered as a reward to funders. Sometimes softwares are released before the creation of the value token or before a market valuation of that return.

Debt-based

For this kind of crowdfunding borrowers have to apply online, generally for free, and their application is reviewed and verified by an automated system, which also determines the borrower's credit risk and interest rate. Investors buy securities in a fund which makes the loans to individual borrowers or bundles of borrowers. Investors make money from interest on the unsecured loans; the system operators make money by taking a percentage of the loan and a loan servicing fee.

Litigation

This is a particular type of crowdfunding type because it is related strictly to Law. For instance, Crowdfunder in UK operates as a legal crowdfunder. It selects public interest cases and publicizing them on its sites inviting the crowd to fund them, the interested people are donors rather than investor. The funding works as an all-or-nothing, which means that if a pitch does not reach the target funds the money gathered will be refunded to former owners.

Donation-based

Charity donation-based crowdfunding is the collective effort of individuals to help charitable causes. One type of this "donation-based" crowdfunding is the civic crowdfunding, in which funds are raised to enhance public life and space.

1. 4 Crowdfunding platforms

Over 450 platforms of crowdfunding have been created since the phenomenon started, possible investors are willing to choose the one that suits more their needs.

These platforms are commonly known as “CF platforms” and they perform the intermediary between entrepreneurs and investors (Goerlitz, Roland,Bertsch, Valentin,Caton, Simon, 2015).

They are located in the Internet as sites differing for the types of the projects and models of crowdfunding(equity-based, reward-based, etc.).

A sum that goes from 3% - 10% of the total raise from the fundraising represents the percentage that will be taken from the entrepreneurs that submit their pitches, these sum is due both to the transaction costs and the intermediary commissions.

For instance, some of the most popular sites are:

- Experiment, a platform focused on the scientific community where you can raise funds for causes as diverse as biology, political science, physics or computer science
- FunderHut, a specialised platform for individuals, small businesses, non-profit and communities. This site has also the option to offer fundraising consulting services
- Indiegogo, in which are included projects of various types of projects, but particularly focused on funding film ones
- Kickstarter, perhaps the most well known crowdfunding platform. This platform raised over 1 billion dollars since 2009
- Crowdrise, specialised in charitable giving and leader in event fundraising
- Angellist, particular because it is more orientated to a social networking approach
- Crowdcube, based in UK, is an award winning, leader investment crowdfunding platform that offers the chance to invest in startups, early stage and growth businesses through equity and debt
- Seedrs, UK based, as Crowdcube, offers also support before, during and after the fundraising

According to (Niznik-Klocek, 2012) and to their scripts, platform managers selects the projects basing on the originality of the idea and its practicability, and not on the profitability of the business, as it could be easy to think.

Additionally, there are different criterias for the selection:

- Quality of the project
- Capacity of the entrepreneurs

- Nature of the project
- Project leader
- Location

1. 5 Theoretical and empirical background

Key points that could lead companies to their competitive advantage are defined by the resource based theory (Barney, 1986; Penrose, 1959). The critical points of this theory are the fact that each firm has its own different capabilities and resources, so the competitive advantage is based on variety amongst companies. Knowledge is considered the most valuable competitive advantage, also for its property of transferability among firms but also within these ones too. Knowledge can be divided in two lies, tacit and explicit knowledge, that differ for the way of transferability. The explicit one is easier to transfer because it is revealed by communication, on the contrary, the tacit one is more difficult to obtain because it is revealed by its application. The uncertainty of the second case due to its tricky transmission makes it more difficult to be acquired (Kogut and Zander, 1992).

Efficiency in transferability of the knowledge is based on its properties of aggregation, which depends on the capability of the recipient's ability to add new knowledge to the previous one. The aggregation is easier to achieve when knowledge can be translated in common language. For instance, a very common and useful way for transferring data is Statistics. Appropriability is defined as "the ability of the owner of a resource to receive a return equal to the value created by that resource" (Teece, 1987; Levin et al., 1987).

Problems for knowledge appropriability are many, in particular, tacit knowledge cannot be straight transferred and, on the other hand, explicit knowledge has problems due to its easiness to transfer also to competitors (Arrow, 1972)

They only way firms have to protect their knowledge is thanks to patents and copyrights, which allows companies to have their knowledge protected by legally established property rights.

Regarding the production, it is fundamental to a knowledge-based theory of the firm that the core in production is knowledge.

Critical to Simon's principle of bounded rationality (1991) is the assumption that the human brain has a limited range to acquire and process knowledge, with the final result that individuals specialize in different fields of knowledge.

1. 6 Literature review

Crowdfunding has been analysed, mostly in the last decade, for understanding its main characteristics. (Giudici, Nava, Lamastra, Verecondo, 2012) firstly reviewed the literature on the phenomenon, then, they made a comparison between crowdfunding and other patterns of entrepreneurial finance and finally they listed most important Italian crowdfunding companies.

Crowdfunding is becoming a top way for raising funds, it draws in “an open call, mostly through the Internet, for the provision of financial resources either in form of donation or in exchange for the future product or some form of reward and/or voting rights” (Belleflamme et al., 2011). Crowdfunding platforms have the role of intermediate between entrepreneurs and potential investors, therefore extending the conventional resources for raising finances, lining in with the principle of multi-side markets (Hagiu, Wright, 2011).

(Kappel, 2009) has classified crowdfunding in two types, “ex post facto crowdfunding”, in which capital is offered with the expectation of a return as a product, typically reward based crowdfunding and “ex ante crowdfunding”, where financial support is offered to achieve a target result. (Lambert and Schwienbacher, 2010) divided crowdfunding patterns in groups regarding the nature of the reward for investors, donations, active investment and passive investments. (Wojciechowski, 2009) underlined that the boundaries of the crowdfunding phenomenon are not still so clear. As regard the success of crowdfunding, there are three key points listed by (Agrawal et al., 2011) that are , firstly, the difficulties of raising funds due to the global crisis, secondly, the evolution of Web 2.0 and, at last but not at least, the success of crowdfunding.

It is also clear that the development of social network (Facebook, Twitter, etc.) facilitated this phenomenon thanks to the easiness to make advertisement of the projects, as explained by (Moissejev, 2013).

As regards to the legal aspect of crowdfunding, in the USA, in 2012 the JOBS has been approved and signed into Law by President Barack Obama and the final rules became effective in 2016. This law and its advantages and disadvantages are analysed by (Martin, 2012). In Europe there is a different and chaotic situation due to the diversity of the national regulations.

In particular, in Italy, a decree for stimulating startups and fundraising, the “Decreto Sviluppo-bis”, was approved in 2012.

Crowdfunding platforms can be subdivided in four groups regarding participation rights (Giudici, Nava, Lamastra, Verecondo, 2012):

- 1) Equity-based, investors have the right to participate in future incomes

- 2) Lending-based, crowdfunders are refunded receiving also an interest payment contractually agreed
- 3) Donation-based, funds are furnished to startups with no upcoming returns
- 4) Reward-based, funds are paid for non-financial benefits, most of the time the return is on product

According to (Hemer, 2011) the complexity of these four forms of crowdfunding is exponential, in fact, donation-based CF is the easiest form and equity-based CF is the most complex one, going through reward-based CF and lending-based CF.

Another aspect I would like to report is about the investment behaviour, because, on average female investors seem to be more risk adverse than men.

Many psychology and behavioural economics literature spaced in this area of differentiation of genders approaching to investment risk (Eckel and Grossman 2002; Byrnes et al. 1999).

This phenomenon is not just according to investment risk but it is widely suitable for a large group of European firms, while in the passage from male CEOs to female CEOs there is verified a phenomenon of decreasing in corporate risk taking (Faccio et al. (2014).

This phenomenon is also valid for the USA, were studies from (Palvia et al., 2014) underline the fact that banks with female risk manager tend to have more conservative levels of capital. It is also suitable for Italy and local banks (Bellucci et al.,2010).

But why is it like that? A possible explanation could be that women's behaviour facing the risk is influenced by the possible vision in the world of investment of the females as not as competent as the men, probably due to cultural prejudices (Devine 1989; Eagly and Mladinic 1994).

Female investors might have some doubts on the prejudice on their level of competence, regarding to male-dominated fields, as it is the investment world (Ridgeway, 2009).

Another topic well treated from literature is information asymmetry between investors and firms. It emerged that entrepreneurs tend to exaggerate in the possible valuation of their firm (Cooper et al. 1988; Busenitz and Barney 1997; Baron 1998), that most of the times gives as result a growth picture overrated, conversely to the real assets of the startup (Shane and Cable 2002; Shane and Stuart 2002).

This "deformation" of the entrepreneurs' attitude to valuation will be very significant in my case study.

But why crowdfunders are willing to invest their money?

Schwienbacher and Larralde (2010) describe the main motivations of the crowdfunders, which are:

- The idea of “exciting adventure” for participating in the creation of a new project
- Interest in challenging themselves and make new experiences
- Extending their network
- The concept of investing in a company to make a profit in the future

(Kleemann, 2008) underlined that crowdfunders have either intrinsic motivations, for instance the personal pleasure in participating in a new project, or extrinsic motivation, for example a reward that can be either profit but also simply a product.

(Ter Kuile, 2011) described other two motivations for investors:

- The altruistic idea of helping someone in doing something, which causes pleasure to the investor
- The importance of the location proximity, investors, in fact, prefer projects located nearby him

Moving on the other side, there are also three types of project creators according to (Hemer, 2011):

- Independent; Individual starting in business
- Integrated; An entrepreneur related to a private firm, non governative organization or institution
- Start-up; An individual that starts as a freelancer, but with the aim of integrating in an organization

What are the advantages and disadvantages of CF?

Each method of financing has its own PROs and disadvantages, but focusing on the CF method, the author (Steinberg, 2012), in his book, “The Crowdfunding bible”, reports some of them:

ADVANTAGES

- Keeping the full control of the fundraising control until it expires
- Testing directly products or services
- There is the possibility for the campaigns to be overfunded, which means that the pitch raised more money than the target amount
- Having the ability to pre-sell the product or service
- Extending your network

DISADVANTAGES

- Stressful campaign due to the possibility to fail until the last moment of that
- Big preparation for business and marketing plans
- Difficulties in investing lots of money in a pitch
- Increasing competitions between projects

- Entrepreneurs have to be always focused on the campaign

How to make a successful campaign?

(Steinberg, 2012) in his book also listed some fundamental tips for having success in CF:

- Clear understanding of the product or service
- An interesting pitch that excites people to know more about that
- Solid schedule
- Marketing plan including social networks
- Realistic funding goal

Also (Mollick E., 2013) furnished three key points thanks to his analysis on 47.000 companies:

- The success ratio of the campaign is strictly related to personal networks and the quality of the project
- Geographical factors are very important, in fact, projects launched in cities with creative communities have an higher success ratio
- More than half of the businesses launched their products with a delay, which depends on the amount raised

1. 7 The process

The crowdfunding process is characterised by three main phases, (<http://www.internetmarketingforcompanies.com/>):

- Pre-crowdfunding phase

When a person has an idea for creating a new startup, there is a long list of activities to address before starting the campaign, including:

1. Recruiting the team
2. Development of the product prototype,
3. Lining up of production partners, sub-contractors and suppliers
4. Determining who the target market will be
5. Defining who social media crowd should be, and how to best engage them
6. Scheduling how the product should be marketed and which channels it could be sold through
7. Create a project plan

8. Finally this phase involves prepping for Crowdfunding campaign: selecting the right crowdfunding platform, setting up financial accounts, designing the actual crowdfunding page with the related text, images and video, getting approval for the campaign

- Funding phase

This is the actual crowdfunding phase, in which there are some people of the crowd willing to finance the project and they do so by making a small contribution expecting a reward that can be a profit share or the product as a return on investment. Once the target amount is reached the money is given to the initiative taker to start the project, however if the target amount is not reached within certain time limits, crowdfunders will be reimbursed.

- Post-crowdfunding phase

The third phase can be divided as it follows:

1. Production
2. Delivering the pre-sold items or backer awards
3. Staffing up
4. Lining up distribution
5. Packaging
6. Marketing: with pre-launch, launch and branding campaigns.

After that the initiative taker completes the project and sells it to the market and the crowd receives the profits made by the initiative taker or the product as a reward.

2. Equity Crowdfunding

In this second chapter of my thesis I focus on one of the different models of crowdfunding, the “equity-based” model. I pushed myself through the explanation of the two models in which differentiates also the equity-based crowdfunding.

Then I describe in details the platform “Crowdcube” and two important aspects of these site web, the London Co-investment fund (LCIF) and the taxation part (SEIS/EIS).

2. 1 In general

Equity crowdfunding is one of the most successful patterns of crowdfunding, where the investors, literally “the crowd”, provide funds for the startups, via internet, for financing projects they believe in, with the rights to expect for a return in shares of the company itself and the relative patrimonial and administrative rights deriving from the participation in the company (<http://www.investopedia.com/terms/c/crowdfunding.asp>).

It is one of the new methods of financing belonging to the area of “Alternative finance”, which are financial channels emerged outside of the traditional finance system. The most of these systems are practised through “online marketplaces”. The other channels are reward-based crowdfunding, peer to peer consumer and business lending, but also cryptocurrencies such as Bitcoin, SME mini-bond, social impact bond, community shares, private placement and “shadow banking” mechanism. This methods has grown in the recent years, particularly as financial platforms for the small and medium enterprises , due to the financial crisis.

All these activities are regulated by the Financial Conduct Authority (FCA) in the UK and in the UK by the JOBS act.

There are two basic models:

- **All or Nothing** (AoN) , Before the beginning of the crowdfunding campaign a target amount of money to raise is determined and just if this target is reached or even the pitch is overfunded, the process goes on and the money is taken by the startup, on the contrary, if the funds are not enough all the money are given back to investors;
- **Keep it All** (KiA) , Whether the goal of the pitch is reached or not all the funds are taken by the entrepreneurs but, if they are not sufficient to meet the minimum objectives, it is possible for the investor to be refunded.

Unfortunately, in Italy the crowdfunding phenomena is less developed compared to Uk and USA, but, however regarding to equity crowdfunding nowadays there are 17 platforms active. Inter alia: Assiteca crowd, Cofyp, Crowd4capital, Crowdfundme, Ecomill, Equinvest, Equity Startup, Fundera, Investi-re.it, Mamacrowd, Muum Lab, Next Equity Crowdfunding Marche, OpStart, Starsup, Startzai, Unicaseed and We are standing (<http://www.economyup.it/>).

2. 2 Crowdcube

Crowdcube was funded by Darren Westlake and Luke Lang in 2011, the former is the CEO of the company and the latter is the CMO and his duties space between branding, media coverage and marketing communications.

Crowdcube is an equity-based crowdfunding platform and it operates on the “all or nothing” model. If the target amount is reached a commission is charged on successful pitches. This platform differs from the other leading crowdfunding platforms, for instance, Indiegogo and Kickstarter, where the patterns are on reward-base or donation-base.

The most successful raises of capital in the history of Crowdcube are the pitches of Crowdcube itself, on its platform, goHenry in the financial area, JustPark in Travelling, Sugru and Gritpit Fixings for “manufacturing”, Chilango for “food and drink”, 1Rebel for “Health and fitness”, eMoov for “Estate agency”, Witt energy for “Energy”, PodPoint for “Renewable energy”, Hab housing limited for “Real Estate” and Lovespace for “storage”.

The two most renowned successful exits are E-Car club, that was acquired by Europcar and Camden Town Brewery, that has been bought by Anheuser-Busch InBev for around 85 million of pounds.

Today Crowdcube raised a total amount of money equal to £185,451,795, with 299.896 of registered investors on the site and 437 of successful raised startups (<http://crowdcube.com>).

Before starting to invest, all the possible investors are tested, while registering on website, with some questions on investing basic theory, which could give you the pass to starting to invest or not. Instead in the pages of the site it is often quoted this warning due to the risks on investing: “Investing in start-ups and early stage businesses involves risks, including illiquidity, lack of dividends, loss of investment and dilution, and it should be done only as part of a diversified portfolio. Crowdcube is targeted exclusively at investors who are sufficiently sophisticated to understand these risks and make their own investment decisions. You will only be able to invest via Crowdcube once you are registered as sufficiently sophisticated.”

It is also possible for investment companies to invest in startups, for instance, there are cited on site top investment companies such as Octopus investments, Balderton Capital, Index Ventures, Passion capital and Seedcamp.

Crowdcube also won about 40 different awards. To quote some of them : ADVFN International Finance Awards 2016, Best Crowdfunding Platform; AltFi, Best equity Crowdfunding Platform for Startups 2015, Edinburgh Chamber of commerce, Innovation in business.

Crowdcube investment opportunities are all listed on site and it is possible to filter them for adding time, product type, which means whether the startups are offering bond or equity shares, sector, growth stage and taxation type, such as EIS and SEIS. For growth stage it means how is the business radicated from time, seed stage, early stage and growth ones.

It is also possible to find startups that are listed in "Crowd10".

Crowd10 South-West is an initiative from Bristol-based Crowdcube affiliate, IdeaSquares. The programme was launched with an aim to support 10 of the region's startups in raising up to £150k of SEIS investment via Crowdcube.

At this moment there are 6 of this selected startups registered on the site: Lux Rewards, This mum runs, Coherent, Chocolate bear kitchen, Esole and Apps4arts. The first 4 ones are already overfunded, on the contrary, the last 2 ones are not going to be funded because Esole could not reach even the 50% of the amount and Apps4arts just trespassed 50% with respectively 1 and 2 days left for their funding campaigns.

Analysing Esole and Apps4arts I found two different problems that could be the reason for not achieving the target funds. Esole has some issues related to a competitor with patents for US and Canada markets and the lack of answers to questions of the possible investors could facilitate mistrust of Apps4arts by them.

I also noted that there could be also a possible link between the growth stage of the business and the amount of target investment the startups reached. In fact, none of the "seed stage" startups yet obtained the 100% of the target investment and probably they could not at all also at the end of the pitch, that is typical because it is surely at this stage where the majority of startups fail. At the contrary, in the "early stage" group there are either overfunded pitches, such as Plumen, or that are going to reach the necessary funds in the next days, such as Mbj London, but also some pitches that would not definitely reach the amount required and uncertain ones. The trend is also the same for the "growth" group of pitches. The final image is that trust is very important for possible investors and, as a consequence, they are inclined to invest in more mature startups.

In the main page of each campaign it is possible to read about business plan, financials and informations on the team, on the founders and their background. You can also read more about the idea itself.

There is an area where all the Q&As and the updates from the campaign are gathered. A possible investor can also personalise his research on Crowdcube website through filters on the target investment, equity offered, "investors so far" and "investment raised so far".

The pitches, however, are all listed in the part named “Investment opportunities” and there is an explanation part, “How Crowdcube works”, in which there is an introduction on the functioning with a video related.

It is possible for newcomers to know more about Crowdcube either in investing in startups or raising funds. In the area “More” there are more detailed services and explanations of the site. In the personal area it is possible to manage the portfolio of investments, settings and other profile key points.

2. 3 London Co-Investment Fund (LCIF)

The UK Government-backed London Co-Investment Fund (LCIF) is investing in London’s finest seed-stage technology, digital and science businesses through Crowdcube. The investment pot is earmarked for high-growth firms making the transition from start-up to growth phase and typically for companies looking to raise between £250,000 and £1m.

Established by Funding London and Capital Enterprise, LCIF is a new Government-backed fund designed to address the funding gap in London faced by tech start-ups, and will see £25m invested in over 150 seed stage companies within the Technology, Digital and Science sectors over the next three years. The £25m is being contributed by the Mayor of London’s ‘Growing Places Fund.’

LCIF investments are alongside private monies sourced by its selected partners and represent up to 25% of any qualifying investment round. With its strong track record of raising investment for start-ups and high growth businesses, Crowdcube will source the companies for co-investment and our highly experienced fund managers in the Crowdcube Ventures team led by Stuart Nicol (Octopus Investments, The Capital Fund) will bring their venture capital expertise to bear on assessing deals.

Who is eligible for LCIF review?

- **Seed stage:** Early stage companies where the proof of concept stage has been successfully concluded, ideally showing some traction.
- **Sector:** Your company must be in the Technology, Digital or Science sectors
- **Location:** Your primary operations must be based in or about to move to Greater London
- **Job creation:** As businesses grow with LCIF investment, it is key that they are creating jobs within London

- **Funding requirement:** You will need to be raising between £250,000 - £1.0m in this round of funding. If you are seeking up to £1.5m, please contact us as exceptions may be possible.

What does this mean if you are raising finance on Crowdcube?

If your business meets the assessment criteria for receiving investment from LCIF and you plan to launch a funding round on Crowdcube, your business will be presented to Crowdcube's fund managers for consideration (process outlined below).

The value added by an LCIF investment along with having a Crowd of brand ambassadors also investing into your business presents an exciting opportunity for an alternative form of raising equity finance.

2. 4 Tax Relief

There are two key, and very generous, tax breaks to look for when it comes to investing on Crowdcube. Both of which can be 'carried back' to the previous tax year (<http://crowdcube.com>).

EIS – Enterprise Investment Scheme

The Enterprise Investment Scheme is designed to help smaller, higher-risk companies raise finance by offering tax relief on new shares in those companies that qualify. For the investor, it's a tax efficient way to invest in small companies.

The EIS is aimed at the wealthier, sophisticated investors. People can invest up to £1,000,000 in any tax year and receive 30% tax relief. However, they are locked into the scheme for a minimum of three years. EIS seeks to encourage investment into unlisted companies, just like the ones featured here.

SEIS – Seed Enterprise Investment Scheme

SEIS is an incredibly generous derivative of the Enterprise Investment Scheme (EIS) and was introduced in April 2012. Its aim is to encourage seed investment in early stage companies. Investors, including directors, can receive initial tax relief of 50% on investments up to £100,000 and Capital Gains Tax (CGT) exemption for any gains on the SEIS shares.

The maximum amount to be raised for each company is £150,000.

3. Empirical research

In this last chapter I arrive at the main part of the thesis, in fact, collecting all the data I found on the Crowdcube database, I analyse all the aspects of these twenty-six pitches for finding some trends that can help me for giving some suggestions to the investors. That is why in these three paragraphs I explain how I collected my dates, the way I sorted these, and then I report some possible trends and finally I give to investors my personal suggestions for investing in startups.

3. 1 Case study: Crowdcube, How investors have interactions with entrepreneurs

The main point of this thesis is to analyse the interactions between investors and entrepreneurs, for this reason I decided to search and list from the online crowdfunding platform "Crowdcube".

I decide to utilise this platform because it is one of the most important equity-based platforms not just in the UK but also in the whole world.

The website is very clear and there are many interesting pitches to work on.

There is also a database of the successful past cases and it is possible to read and learn from the interactions between potential investors and entrepreneurs, with the aid of the Q&As area linked in the main page of each pitch. If the details on the primary page are not satisfying it is also possible to interact privately with the entrepreneurs to have clarifications on financial and business plans or on any other aspect of the business.

Firstly, on 6th July 2016 I decided to make a broader analysis on the list of the all successful cases of Crowdcube.

I actualised to find trends is the analysis of successful cases (420), splitting up them by sectors I registered that this cases were belonging to :

- Education 18
- Food and drink 97
- IT and telecommunications 22
- Manufacturing 24
- Art and design 8
- Media and creative services 18
- Leisure and tourism 5
- Professional and business services 31
- Retail 28
- Environmental and ethical 7
- Health and fitness 12

- Consumer products 9
- Internet business 15
- Oil and gas 2
- Technology 7
- Sport and leisure 1
- Film, TV and theatre 4
- Accelerator 0
- Other 9

Some pitches are not to be seen in the database but, however, with these results I can say that surely investors are more keen to invest in startups of the sector “Food and drinks”, but also in “Retail”, “Manufacturing” and “Professional and business services”. It is also due to underline the 0 for the “Accelerator” sector, probably because of the particular and specific knowledge required to be sure in investing in it.

Then, on 6th June 2016, I moved my attention to the twenty-six ongoing campaigns.

3. 2 Data collection process

I created a page on Excel with the main key features of each of the pitches I decided to analyse. Firstly, I collected all the names of the twenty-six pitches, then I sorted these for sectors, target investment, raised funds, equity available, which means the part of the equity of the company the offered to the “crowd”, entry date, expiration date, premoney value, if it is available and for the number of key members.

Secondly, I divided them in two groups, which are successful campaigns and unsuccessful ones. If they are successful I also noted the amount of the overfunding capital, which is the part of the capital that exceeds the first request of funds.

Subsequently, I listed weather the pitches dates of expiration were extended or not, if they received subsidies from LCIF or not.

Finally, I reported the percentage of answers from key member at the investors and specifically who answered those.

As I have done with the past successful pitches firstly, I regrouped them by sectors.

Some pitches belong to more than one sector and it emerged that:

- Consumer products 2
- Health and fitness 7
- Technology 13
- Sport and leisure 2
- Media and creative services 5

- Leisure and tourism 3
- Internet business 9
- Food and drink 7
- Retail 2
- Environmental and ethical 3
- Manufacturing 3
- Education 2
- Professional and business services 3
- Art and design 2

Secondly, I listed the target amount each pitch requested as minimum for being successful and it emerged that the average amount requested is 303.462 pounds with a range that varies from a minimum request of 35.000 to a maximum of 1.000.000 for the most ambitious ones. The total raised funds for each campaign equals on average and amount of 164.430 pounds, it is noticeable that the average of the obtained capitals is just a little higher than the fifty percent of the requested ones. It varies between 8.970 and 554.140 pounds.

The third information I listed is the equity available for each pitch, that refers the part of the company given in return to the investors for their capital. This equity is divided between the “crowdfunders” proportionally to the amount given by each one of them on the total amount requested to be fund. Sometimes it is possible, when the pitch is overfunded, that this amount agreed of equity given to the crowd has to be augmented by the entrepreneurs to contain the dilution of the equity.

Howsoever, the average equity offered in return equals the 17,19% of the total amount of the equity of the companies and it ranges from 4,76% to 30,77%.

The number of investors varies a lot between pitches from a minimum of 14 to a peak of 236, with an average amount of about 88 investors.

As regards to the period of the pitch it depends on the time established by the entrepreneurs but it could be of 30 or 60 days. It is also possible to have an extension for special reasons that usually are for ongoing discussions between important investors and entrepreneurs. This time also varies from 1 week to 3 weeks, due to agreements with Crowdcube web platform. In my case study fourteen of twenty-six startups extended the period of the pitch, as I mentioned before, in all this cases there were ongoing negotiations between crowdfunders and startupper.

All the pitches I analyses belonged to startups settled in the UK, mainly in England.

An interesting point on location I want to report is the fact that there is a group of pitches, called “Crowd10” that regards only the South-Western area of the UK.

The main online pages of the campaign also give the opportunity to have a look to the pre money valuation of the company, unfortunately not all the entrepreneurs have

made an evaluation of their business. The pre money evaluation is an internal valuation made by the team members of the startup that, analysing the cash flows, the revenues, the patents and other specific evaluation of the company, is given as possible value. It is called “pre money value” because it is the valuation before the crowdfunding process. Anyway, on a total amount of twenty-six startups examined, twelve have a pre money value. The lowest pre money value is 500.000 pounds and the highest is 5.400.000 pounds, and the average is 1.123.417. Despite this average value there are only three startups that have a pre money value over 1.000.000 pounds and only one over 5.000.000 pounds.

The number of key members, that are the mentioned part of the staff on the page of the campaign, varies from a range of two people to nine, while only six campaign on twenty-six have more than five key members.

Regarding the group “Crowd10” I mentioned before, in the group of companies I studied there were six belonging to this group, which means that these ones received subsidies from the UK Government investment fund, capitals set aside for finest businesses.

The Q&As pages is very interesting for my case study and I can point out that the percentage of answers by startupper is very high, in particular 20 teams answered at all the questions, 3 teams answered at the 90% of the questions, 2 at 50% and there is just one case of no answers at all.

In all the cases the questions are directly answered by the CEO itself, probably because he is able to have a sight of the full map of the business and be more prepared to discuss about all the topics.

On 6th July 2016 eight of these campaign were already successful, on 11th September instead there are ten, perhaps sixteen of the were unsuccessful, which means that there is a success ratio of 38,46%.

3. 3 Data analysis

As I underlined before I decided to analyse twenty-six pitches from the site Crowdcube trying to find some trends according to the interactions between investors and entrepreneurs. For this reason the most significant part to scan is the Q&A section, in which are collected all the questions from potential crowdfunders with the subsequent answers by entrepreneurs.

Three main trends have been analysed, specifically (1) investors’ questions before the investment, (2) company stage and campaigns’ success, and (3) entrepreneurs’ behaviour.

Firstly, In my study it emerged that there are some pattern of types of questions from investors, in particular the principal topics with very little variations according to the specific questions and personal attitudes. These main topics are twelve and regard:

- Brexit; after the shocking break from Europe Union and the UK, investors want to know how the startups will change the way to approach to foreign markets and how do they think to deal with exchange rates
- Customers; some investors need clarifications on who could be the possible customers for the product or service
- Scalability; potential crowdfunders want to know if the startups are willing to expand in other markets or to remain in the UK market, and if it is possible to know how and where are they going to extend the business
- Market research; Possible investor want to know if there are datas from researches on the market or not, they want to know if the picture depicted by the company is facing the reality or not
- Patents; A question that is due to asymmetries of information between the two parts, in fact investors want to know the real value of the assets of the companies to have a general valuation of those
- Exit strategy; Straight to the point, most of the possible investors need to know what are the plans according to time and the way for being sold to other companies because of the necessity to have an idea on how much their shares' value is planned to increase and when are they going to take that capital in return
- Products; Some pitches' products are not described well or not enough according to some potential investors, it could be also another issue of asymmetry of information
- Pre money value; A remarkable group of investors is sceptical on the premoney valuation, that is one of the points I analysed on my literature review, but resuming, entrepreneurs tend to be exaggerated on the valuation of their firms
- Business plan and financials; Most of the pitches inserted a link to have a look on the business plan and the financials of the companies but for some of them investors have to send a private message to the entrepreneurs to obtain one, there are some issues for possible crowdfunders who submitted the request but not received the dates or even some who received properly the material ask for clarifications
- Differentiation from competitors; Some pitches seem to have nothing different from the competitors and possible investors ask what are the real advantages in supporting the company instead supporting another. This is also related to the market piece the startups are going to achieve in reality

- Marketing strategy; Possible investors want to know if the service or product is going to be driven properly to the market with proper advertisements and marketing strategies
- Shares; The pitches give the list of advantages of a possible investor could get deciding to invest in the company. This advantages are depending on the grade of the shares are offered to the crowd, for example, A share usually have more advantages than a B share. Advantages could be only financials but also administrative or different. The grade of the shares an investor receives is, most of the time, related to the amount of the money invested in the startup. Some advantages could also regard discounts or product rewards as a sale on the online site or even a bucket of beers, etc.

Almost all the pitches had a 100% of questions answered, the other few pitches that did not have CEOs that responded at all the questions clearly were unsuccessful. Overall the results are good, but answering those questions was not enough for the management of the startups to obtain the target funds. On the total amount of 26 pitches, 23 had managers that answered all the questions or delaying just a few times, that it is not a relevant data because of the high amount of questions asked in some pitches. But on a total of 23 only ten reached the target funds, why?

Secondly, as per the developments stage of the company, I noticed that there is a relation between the stage of maturity of the companies and the capital raised, the newest to the less recent ones all the pitches are divided in seed stage, early stage and growth ones.

Crowdfunders are more confident in investing in early stage and growth businesses than seed ones, the reason seems to be that the search, first of all, business and entrepreneurs they can trust, and trust could be a driven of maturity stage.

In my study, in fact, emerged that, seed stage companies are more likely to be unsuccessful than the other ones. Conversely, in the group of ten successful pitches there is a large amount of growth businesses first, then a part of early stages and just one seed stage.

The seed stage companies, if the product or service is considered enough good to catch the attention of possible investors, are the ones with more question asked and it is up to the entrepreneurs to seem reliable and to explain very well all the aspects of the business itself.

This is a turnaround related to the previous trend I analysed, in fact, questions asked are inversely proportional to the growth stage while the success of the campaigns is directly proportional to the maturity of the business.

Moreover, despite the fact that all the entrepreneurs that answered to questions relative to the 26 listed companies were the CEOs, the more prepared one seemed to be the CEOs of the growth stage startups, probably due to maturity and the years in the business field.

Lastly, analysing entrepreneurs' behaviour in answering the questions posted by their potential investors I found the following trends.

Pitches with lots of questions, are not sign that something is not working in it, on the contrary, this means that lot of people want to invest in those, but also means that the best entrepreneurs at responding to questions attract more curiosity from the investors, who continue asking.

Pitches were entrepreneurs are more exhaustive in replies are the successful ones, in fact, investors love CEOs that give the idea of attention and preparation in what they are talking about.

The updates of the pitches give also other important informations for possible investors such as events for promoting the products or the services of the startup.

Some events also regard the direct interactions between investors and entrepreneurs and can be another good moment for creating networks and also to touch the reality of the company, in fact, having a real interaction with the business and its key members is surely better than only an online imprinting.

Investors are more keen to accept to invest in companies they created a link with, and these meetings can be a good occasion for doing that.

The way the managers replied is directly linked to the success of the campaign, most prepared entrepreneurs were able to catch the trustiness of the possible investors. It is likely that some ideas of the unsuccessful pitches were good but the entrepreneurs were not able to create a relationship of trustiness with the crowdfunders or also to explain their ideas as it was supposed to be.

Moving forward to the side of the possible investors another tendency I noticed is that there were more female investors asking clarifications for the growth stage startups than seed stage ones, while men were both present in all the categories.

My observation is based on the nicknames of the investors, some of those remained ambiguous but I could find a good number of cases with nicknames typically female names.

This point was also underlined in the literature review as female adversity to risk (Faccio, M., Marchica, M.-T., & Mura, R. 2014), see also (Palvia, A., Vähämaa, E., & Vähämaa, S. 2014) due to the prejudice of women less prepared than men in the business area, which is clearly a field "men dominated" (Devine, P. G. 1989).

The fact that women are less present than men in this field is remarked also by the fact that the majority of the entrepreneurs with pitches on Crowdcube are men.

Moving forward, I noticed that the ten successful pitches spaced between ten sectors, that are:

- Technology
- Internet business
- Health and fitness
- Media and creative services
- Professional and business services
- Art and design
- Manufacturing
- Food and drink
- Consumer products
- Retail

Moreover, not all these sectors have the same frequency, in fact, the most frequent ones are in order: Technology, Food and drink and health and fitness.

Later, I moved my analysis on the successful cases registered in Crowdcubes's database and the trends seem to be the same as for my twenty-six pitches analysed. The most of the companies successfully funded that I found on the database belongs to at least one of these ten specific sectors, with the exception of two sectors that were not on those ten but also had a lot of successful campaigns. These two sectors to add to the ones I underlined in my research are:

- Educational
- IT and telecommunications

This means that there is clearly a tendency of recurrence of success in some sectors. I think that famous past exits could be a valuable driven in this case, for instance, the "food and drink" sector could be so successful due to the celebrity of the case of the multimillionaire exit by Camden Town Brewery which was sold to AB InBev for \$85 millions, that is probably the reason why investors think the chances to have a large increment of the valuation of the share are higher in this particular sector, or for the case of the incredibly high raising of Chilango.

3. 4 Results

Summarizing the results of my researches there are some advises I can suggest to potential investors.

First of all potential crowdfunders have to be sure on the profitability of the business before they decide to give some money to a startup, but how can they be sure?

The main aspect is the “trustiness”, I suggest to possible crowdfunders to assess the quality of the entrepreneurs. At the beginning, they should check the background of the key members of the startup they are interested in, and trying to value their attitude at running the company, then, they should check the main aspects of interest, firstly checking the questions asked to considered companies by other crowdfunders that could be useful either for questions they wanted to ask personally but also for some particular questions that may were not to be asked for the entrepreneur himself but which are also important and can add useful infos, and then, if not satisfied by the question database, they can ask their personal questions at the company, but there are some principal topics I suggest to ask in each case, according to the relevance of those topics on the businesses themselves; some of the twelve recurrent questions I cited before. For instance, questions on the impact of the Brexit on the business, Scalability in other markets or clarifications on business plan and financials, if these are not enough clear, etc.

Asking question do not have to be a problem for possible crowdfunders, they need to scan all the aspects of the business until they reach their goal, “trustiness” in the pitch and its members.

Another suggestion for possible investors is to do not follow just impressions or investing in startups that seem to be “cool”. Sometimes plan B is better than plan A, that is why the eligible crowdfunder must base on quantitative dates and even if a startup seems to be less interesting but it has the requirements to be a successful business, the investor has to be able to go over appearance and go for the most profitable one.

For a newcomer in the crowdfunding world, I suggest to starting investing in more mature startups, such as the pitches listed in the “Early stage” or “Growth” areas, leaving behind “Seed stage” companies for the moment. As underlined in my analysis, the “seed stage” ones have a success rate much lower that the first two I cited before, those are more inclined to be successful, because the already passed the first steps of their lifecycle as a company and they are more eligible for becoming successful and also the member on average have are more experienced thanks to the time passed on the stage. That is why they seem to be less risky for investors.

As investor, I will follow trends and tendencies, that is why, I think crowdfunders have to invest in some particular sectors that have an high success rate and some famous cases of exits, such as the “Food and drink” sector, for instance a famous case I cited before as the exit of “Camden Town Brewery”. This trend is confirmed by Crowdcube databases, in which emerges also the high rate of success of some sectors, in particular “Manufacturing”, remembering Sugru and Gritpit Fixings and their incredibly high raising of capital, “Retail”, “Professional and business services”, “Educational” and “IT and Communications”.

I suggest also to avoid the sector “Accelerators”, which regards the part of startups accelerators, if the crowdcube investor has no experience in this area but if he knows how to move in this field, this could be a good reason to invest here.

In Crowdcube this sector have no successful cases, probably due to the seed stage of this sector itself but also for the difficulties for investors to value such a difficult type of business.

Moreover, crowdfunders need to start investing in that sectors they know the most, as the entrepreneurs need to create a startup in a sector in which they worked during their previous careers.

CONCLUSION

I decided to focus on this particular topic because I witnessed the exponential growth of these “alternative finance” that become very popular during this years of global crisis , in particular I was “captured” by the phenomenon of crowdfunding thanks to my interest in startups. Due to the fact that crowdfunding is probably the most important method of financing startups I decided to see on the web which where the most important and renewed sites on this specific area and I discovered the site “Crowdcube”, on which I focused my studies for this research.

I was curious to know how worked the specific process of financing a startup so I decided analysing the twenty-six pitches that were available currently on site and I started my study.

In particular, I wanted to find out some trends that recurred in the startup investment world.

In my literature review and theoretical background I underlined some patterns of behaviour by the investors that were confirmed also by my data analysis of the pitches on Crowdcube.

I decided to use this platform due to its facility of utilizing it and its broad database of past successful cases, which was very useful for reinforcing my analysis and finding some trends.

The “Crowdcube” website is very schematic and easy to use thanks to all the functions and the explications which are given.

Later on, I analysed all these twenty-six pitches and I sorted them how I described before in the thesis.

The results of my analysis confirmed the trends I revealed before, the sectors that instinctively seemed to be more suitable for success of the campaigns were successfully founded and I found also relations between the gender of the investor and

their investing behaviour, in fact, women investors seem to be less risky than men, as a consequence that they invest in more mature companies, as previous analysed by (Eckel and Grossman 2002; Byrnes et al. 1999).

Based on my analysis, I provide investors with some suggestions also for the sectors they may start investing in, in fact there are sectors that have an higher success ration, for instance “food and drink”, “manufacturing”, “Retail”, “Professional and business services”, than others, for instance “accelerators”.

Also it has been said on (<http://www.cityam.com/248952/these-best-and-worst-sectors-rates-return-crowdfunding>) that there are clearly higher trends of internal rate of return in some sectors than others, for instance, this article open up with “Better invest in Food and beverage than entertainment”. This datas are based on an analysis on seedrs in which emerged that the IRR is higher in the sectors I found that have a better success ratio. For instance, food and beverage, technology, etc..

I also suggested to eligible investors that the most important key value for investing in a company has to be “trustiness” because there is a clear link between the preparation and the dedication of entrepreneurs in responding questions from investors and the success ratio. That is why potential crowdfunders need to check that qualities of the entrepreneurs with questions.

I also noticed twelve recurrent topics, analysing questions of investors to entrepreneurs, that has to be clear to investors before deciding to invest in a campaign and these are the topics to be asked specifically to CEOs of the companies.

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