THE BASICS OF

CROWDFUNDING

CROWDFUNDING
Danmark

INTRODUCTION

CROWDFUNDING

The concept of crowdfunding is simple:

People funding people.

The idea has been around for years and is still growing in popularity. However, it can be daunting for the uninitiatied to get an overview.

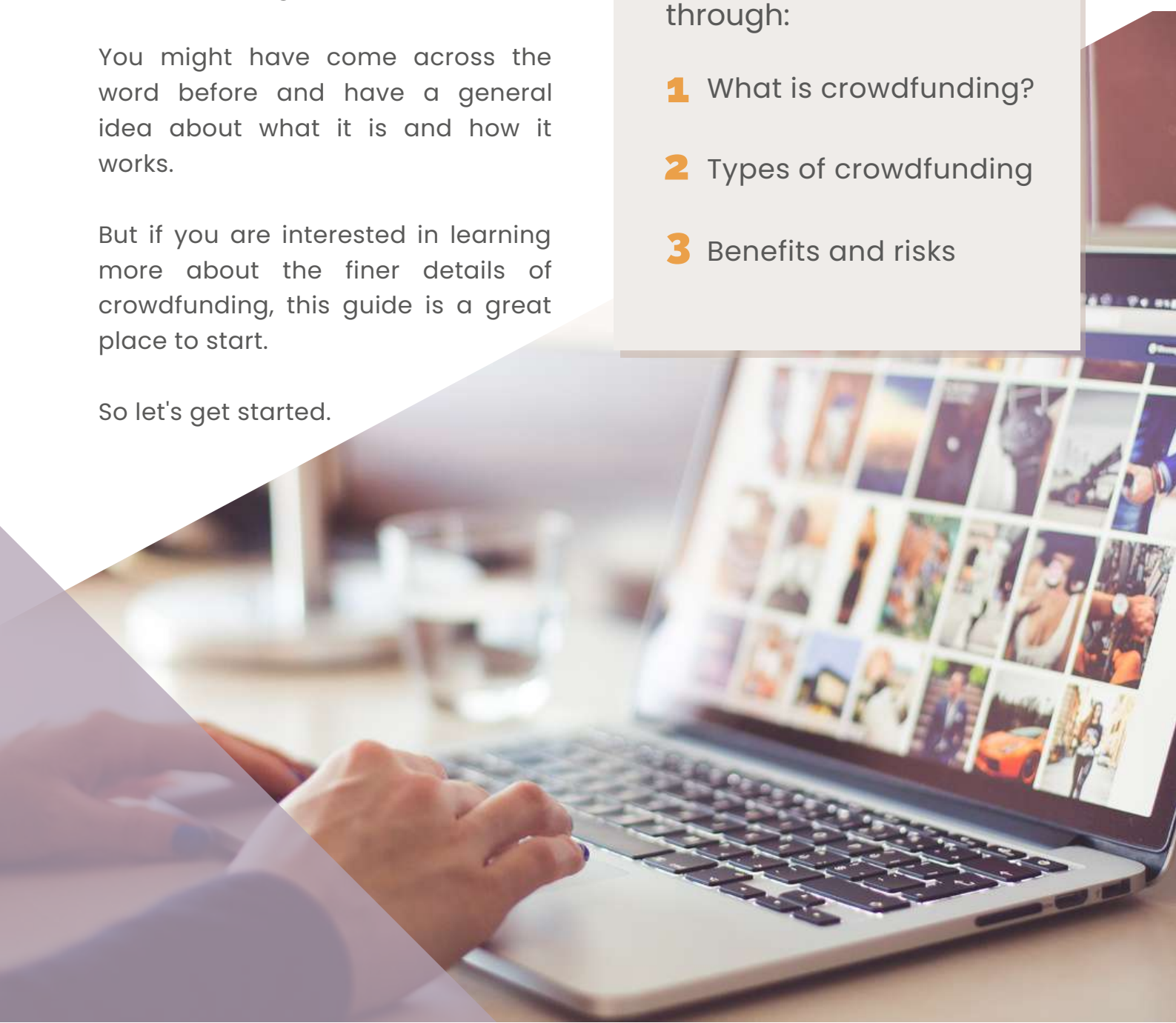
You might have come across the word before and have a general idea about what it is and how it works.

But if you are interested in learning more about the finer details of crowdfunding, this guide is a great place to start.

So let's get started.

In this guide you will go through:

1. What is crowdfunding?
2. Types of crowdfunding
3. Benefits and risks





CHAPTER 1

WHAT IS CROWDFUNDING?

Let's begin with the basics: What is crowdfunding? And how does it work?

In short, crowdfunding is a way of raising money for a specific project from a large "crowd" of people. The investors - usually known as "backers" - receive rewards, interest or even equity in the company in return for their contribution. In some cases, backers can also support a campaign as a donation, expecting nothing but a 'thank you' from the project owner.

Traditionally, if you needed to raise capital for a business idea or to develop a new product, you would need to go to the bank or contact angel investors and venture capital firms and hope you reached the right investor at the right time.

Crowdfunding opens up a new source of financing by giving entrepreneurs a space to pitch their business idea to a wider audience of waiting investors.

This interaction between fundraisers and the crowd is enabled by online crowdfunding platforms. These are websites where any entrepreneur with a good idea can raise money. At the same time, investors can select from many projects and invest in both large and small amounts. Usually, the platforms charge the project owners a fee on the successfully funded campaigns.

Crowdfunding platforms can have fixed or flexible funding - or both. Fixed funding is the most popular and it means that the owner of the project only receives the money if



the campaign meets its set goal, otherwise the money is returned to the backers. On the other hand, flexible funding allows fundraisers to keep the money raised even if they don't reach the goal.

Crowdfunding has many benefits (but also risks), but before we go through them let's explore the different types of crowdfunding.

Did you know?

That the base of the Statue of Liberty was financed with crowdfunding.
In 1885 the newspaper mogul Joseph Pulitzer created a crowdfunding campaign through his newspaper.
More than 160,000 donors contributed.

In 1997

a British rock band funded their reunion tour through online donations from fans. Inspired by this successful experience of alternative finance, ArtistShare became the first dedicated crowdfunding platform in 2000.



CHAPTER 2

TYPES OF CROWDFUNDING

In general, we can group crowdfunding into four main categories: donation, reward, debt and equity.

DONATION

As you may have guessed from the name, in this type of crowdfunding backers get nothing but good karma in exchange for supporting a project. It is especially used by individuals, charities and NGOs to raise money for personal needs as well as for community-based projects.

Common examples of donation-based crowdfunding initiatives include raising money to pay tuition, medical bills for individuals, to fund disaster relief or new community initiatives.

Strengths:
As it relies only on peoples' goodwill, you don't need to give anything in return for the support. In some cases, a project can go viral and collect a lot more money than was originally intended.

Weaknesses:
Because backers don't get anything in return, donations are usually small. The fundraising goal should therefore also be small.

gofundme
DONORS CHOOSE
ULULE
I believe in you
FundedByMe

REWARD

Reward-based crowdfunding is similar to donation crowdfunding in the sense that backers don't get financial returns for their investment. The difference is that in reward-based projects, backers get a reward in return. It is often the preferred type of crowdfunding for startups and small businesses that want to develop a new product or test a market.

Fundraisers define a few rewards in their campaign that backers can choose based on the amount of money they want to invest. For example, for 20 EUR you could get a pack of organic beer once it has been produced, but for 150 EUR you could both get the beer and an invitation to the launch party.

Strengths: Businesses can raise quite a lot of money without having to pay it back or give up equity. Besides the money, they can build up a customer base, get the idea validated and get feedback directly from the customers.

Weaknesses: If the campaign successfully reaches its goal, the project owner has to live up to his/her promises and deliver the rewards. sometimes the costs of running the project, producing the rewards and shipping them to backers can leave project owners with very little extra money to actually carry out the goal of the project.



Some crowdfunding examples

Crowdfunding can be utilized by a variety of different industries and types of organizations: sports, education, healthcare, arts and culture, museums, charities and NGOs, municipalities, businesses, etc.
Let's review some successful crowdfunding campaigns.



Dyrehøj Vingaard is Denmark's largest vineyard.
They wanted to buy a set of machines to be used in the production of their sparkling wines, so they started a crowdfunding campaign on Coop Crowdfunding.
They raised 130,000 DKK by offering rewards that included tours of the vineyard, wine tastings and bottles of wine and spirits.

Luchtsingel Rotterdam in the Netherlands became the first public infrastructure project financed by crowdfunding. The project was to create a 400-metre pedestrian bridge to connect three areas in the city that were separated by railway tracks.
In return for their contribution, backers received their name on a wooden plank on the bridge. Each plank cost 27 EUR and 17.000 were sold in just a few weeks.





World Help organized a campaign during the crisis of the Horn with the objective of raising $120.000 to send containers of food to the Horn of Africa.
Not only did they manage to raise over $180.000, but the campaign also helped them raise awareness, form a team with more than 150 volunteers and attract other funds.

Veronica Mars was a TV series about a young private investigator. When making the movie-sequel, director Rob Thomas decided to use crowdfunding. Backers could choose from various rewards including autographed merchandise, DVDs, tickets to the red carpet, a day on the set, a copy of the manuscript etc. The project was a great success: They raised a total of $3 million, surpassing their goal by an additional million, and the crowdfunding campaign gained international reach.



DEBT

This type is also known as crowdlending, peer to peer lending or marketplace lending. With debt-based crowdfunding, businesses or individuals receive money from a large number of people with the promise to pay them back with interest at a later date.

It is important that the debt fundraiser clearly states the amount of money needed and the time frame of when donors can expect repayment.

Strengths: This is a good alternative to bank loans or other traditional sources of funding. Interest rates are often not as high, the application process is simpler and shorter, and everything is done online.

Weaknesses: Even though it is often easier to apply for a loan through a crowdlending platform than at a bank, not all projects that apply to crowdfunding platforms are admitted.



EQUITY

Also known as crowd-investing or investment crowdfunding, equity-based crowdfunding allows backers to become part-owners of a company by buying shares. Each investor is entitled to a stake in the company proportional to their investment. This form of crowdfunding works best for growth-focused companies in areas where there is high potential return. It is mostly used by startups and early-stage companies

WEFUNDER

Republic

SEEDRS

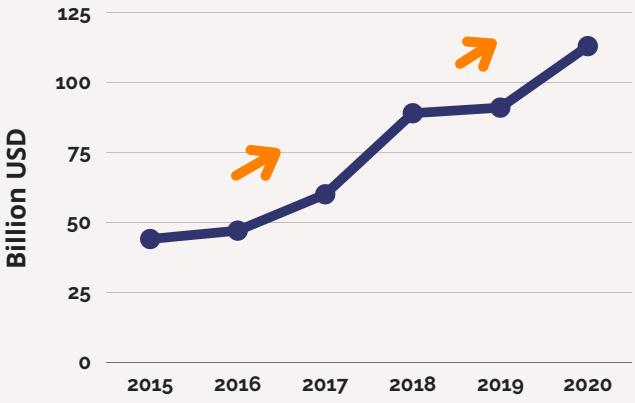
FUNDERBEAM

Strengths: Project owners can get larger sums without having to give immediate returns. In addition, unlike the traditional method, having a large number of investors means that the power is not concentrated around a particular group of shareholders, which puts less pressure on the management and gives them more freedom of action.

Weaknesses: Fundraisers give away part of the company. Also, in some countries, it is not yet legal to give out shares of a non-public company, so the specific regulations of each country have to be checked before planning a campaign.

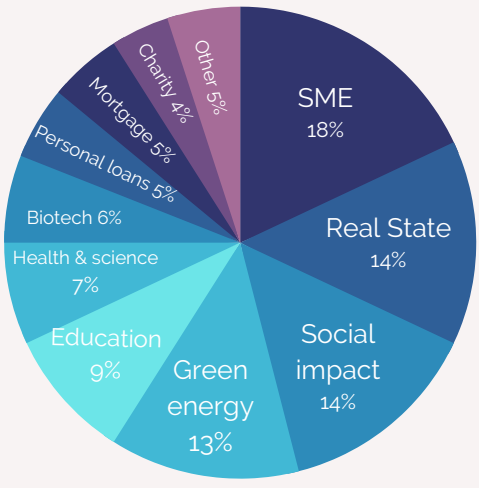


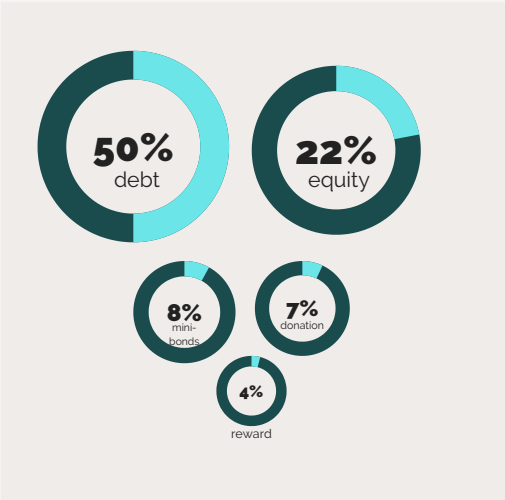
Crowdfunding in numbers



Withouth taking China into consideration, the global alternative finance market (including crowdfunding) has continued to increase in the last two years even against the backdrop of COVID-19.

In Europe, the most predominant industries that raise money through crowdfunding are small and medium-sized enterprises, followed by the real estate sector.





Debt models have been the predominant model during 2019 and 2020, followed by equity. Reward and donation make up only 11% of the crowdfunding during those years.



The average success rate of crowdfunding campaigns is 22.4%

Source: The 2nd Global Alternative Finance Market Benchmarking Report



CHAPTER 3

BENEFITS & RISKS

Crowdfunding is a powerful tool and a great way to get funded. No matter how ambitious the goal is, with the right project one can get funded in a matter of days, or even minutes! But of course, nothing is riskproof. We have already mentioned some of the good and the not-so-good about crowdfunding, but let's expand more in this section.

BENEFITS

Let's begin with some of the things that make crowdfunding wonderful.

✓ Accesibility

Crowdfunding allows start-ups, small businesses or individuals to collect the necessary capital without going through the burdensome process of taking a loan, particularly when those businesses are not creditworthy enough to go through traditional funding.

✓ Efficiency

Instead of having to pitch investors one by one (which can be very stressful and time-consuming), businesses can prepare and present their idea online to many supporters at once.

✓ Awareness and exposure

By using a crowdfunding platform, project owners have access to many and more diverse investors who can see, interact with, and share their campaigns. Whether they are people visiting the platforms to discover new and exciting products or previous backers of other projects, there is already a community around these platforms where one can create a buzz and build a name.



✓ **Build a community**

From the beginning till the end and even beyond the campaign, entrepreneurs keep communication open with their backers, posting regular updates about the progress and answering questions. Backers are let into and engaged in the financing process and they often become the most loyal customers and ambassadors of the brand.

✓ **Test the waters**

Presenting a project to a larger audience provides a great opportunity to refine and validate your offer. One can check if the crowd actually supports what you have in mind and give you the feedback or the data needed to improve the concept.

✓ **PR & marketing**

While promoting a campaign through social media, newsletters, etc, you can attract other media outlets to cover the process of the campaign. Also, with more backers getting involved and believing in your product or service, there are better opportunities for your messaging to be shared and spread through social media.

RISKS

Whether you want to raise funds for your project or want to back a project, let's list some of the risks of crowdfunding to be aware of.

Use of resources

Developing a successful campaign may require significant resources (money and/or time) to build up interest even before the project launches.

Product/service not delivered

Of course, crowdfunding platforms typically have procedures in place to prevent this from happening, but there is always the risk that project owners don't deliver on their promises. This ruins the project owner's reputation and backers wach their investment go down the drain.

Regulations

Depending on the country, there can be regulatory or fiscal challenges that one needs to be aware of.

The project not reaching its goal funding

If the crowdfunding platform has fixed funding, the money gets sent back to the backers and the resources spent setting up the campaign get lost.
If the platform offers flexible funding, project owners can keep whatever funds they have raised but they will need to pay the platform and payment fees, and they must still deliver on their promises to those who supported. This can be a problem if the campaign was made to bring a new product to market, as they might not have the necessary funds to produce their rewards.

Competition

Presenting your whole business plan to a large crowd makes it accessible to investors but also to competition. Ideas can be stolen if they are not protected with a patent or copyright.

Expertise

Professional investors bring also their expertise when investing that could benefit small companies





CROWDFUNDING
Danmark