

# Where does the crowd feel confident? The role of culture, politics, and institutions

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## 1. Background and Research Question

In recent years, microfinance has been growing rapidly with more than 211 million clients having received microloans from microfinance institutions (MFIs) by the end of 2013 (Reed, 2015). The MFIs refinance the loans they grant partly through deposits and partly through international investors who provide capital through indirect or direct investments. The rising interest of socially-oriented investors in contributing to microfinance development is recognised by several online crowdfunding platforms. Indeed, crowdfunding has become an alternative financing option for small ventures and entrepreneurs across the globe to gain visibility and access to a multitude of investors (Strausz, 2017). While crowdfunding is on the rise (Mollick, 2014), we know very little about what drives entrepreneurs and investors to pursue crowdfunding as their preferred method of raising and investing funds. The academic literature has investigated what factors, especially personal characteristics, influence crowdfunding. We propose to examine macro-institutional factors that may affect investor's choice when deciding where to fund a microloan. Specifically, using data from a global online microfinance crowdfunding platform, we examine whether culture, politics and institutions take precedence in influencing decisions to invest in a venture through crowdfunding.

With the ever-expanding technological reach, online crowdfunding platforms are continually growing in membership of both entrepreneurs and investors (Armendáriz and Morduch, 2010). They operate by connecting entrepreneurs with investors whose funding is dispersed through donations, equity offerings, loans, and/or rewards (Mollick, 2014). Crowdfunding offers several advantages for entrepreneurs such as easily accessible funding, financial risk avoidance, the ability to overcome the disadvantage of the liability of newness, and access to a global target audience (Martinez-Cañas *et al.*, 2012). The benefits from online crowdfunding platforms are a driving force behind its popularity and growth. As such, studying the phenomenon of crowdfunded lending is pressing because crowdfunding is growing in the microfinance industry. Microfinancing comprises an ever-growing segment of funding available to entrepreneurs and accounts for a significant and global economic impact despite each loan's small size (Odell, 2010). We examine what characteristics of the micro-entrepreneurs' country of origin including culture, politics and macro institutional factors, influence investor's decisions and lead ventures to successfully acquire funding through crowdfunding.

Economic decisions, such as investing, are well documented in the decision-making literature. Evidence exists that investment decisions are made both with rational processes and by relying on emotions and intuition (e.g., Bazerman and Moore, 2012). However, literature has mostly examined more traditional forms of financing (e.g. institutional investing, stock purchase). In this study, we add to the knowledge of the crowdfunding phenomenon by seeking to understand where the crowd feels confident to invest and whether country-specific characteristics drive investors' funding decisions in the context of crowdfunded lending.

## 2. Relevance

The main objective of this study is to uncover some of the nuances of the crowdfunding investment choices, and to contribute to the gradually developing literature on crowdfunding. This study seeks to expand the understanding of what drives investors to fund micro-entrepreneurs seeking finance. An interesting research area would be to understand whether investors base their funding decisions on the micro-entrepreneurs' country-level factors such as culture, political regime, institutions and macroeconomic conditions. We use a dataset obtained from the peer-to-peer microfinance platform, Kiva, a global crowdfunding platform which operates by offering borrowing entrepreneurs microloans from investors worldwide through local MFIs. Kiva is widely identified as the largest micro-lending crowdfunding platform operating locally in 69 countries (Allison *et al.*, 2014).

This paper makes the following contributions to the literature. First, our study adds to the knowledge on micro-enterprise finance. More specifically, we add to the field's limited existing knowledge on global crowdfunding, a new and growing area of micro-enterprise finance with significant international implications. Our findings are not only important for researchers trying to understand this booming field, but also for practitioners around the world whose economic impact is growing exponentially. Second, our study extends the understanding of entrepreneurial ventures around the world. The online platforms on which crowdfunding has thrived have transcended national boundaries. This has enabled entrepreneurs and micro-entrepreneurs worldwide to seek out and secure financing from a worldwide pool of financiers. Likewise, financiers worldwide now have a global pool of entrepreneurial investments to choose from when identifying potential investments for their investment portfolio.

### **3. Research Methodology**

This study uses data collected directly from Kiva's website. Borrowing micro-entrepreneurs and crowdfunding investors from all over the world can sign up through Kiva's online platform to either borrow or lend funds. Each micro-entrepreneur goes through a field partner (the MFI who works with Kiva), to secure financing. Each micro-entrepreneur's loan, through the field partner, can then be backed by crowdfunders who, voluntarily sign up with Kiva to lend funds to whomever they want. We collect microfinance specific information from the Microfinance Information Exchange (MIX market) database. The country-specific data is collected from the following sources: (a) World Development Indicators (WDI), compiled by the World Bank, for data on "ease of doing business" at country level; (b) Database on Political Institutions (DPI), compiled by the World Bank, for political ideology (left, right, or centrist) of the main party in government; (c) Hoffstead, for information on country's culture. Data on macro-institutional factors is collected from various sources of the World Bank.

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