ERC Enterprise Research Centre

Policy Briefing

The contribution of alternative finance to business growth

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This paper analyses the characteristics and activities of firms that use crowdfunding, using data from the new Longitudinal Small Business Survey (LSBS). Our aim is to better understand the role that crowdfunding plays in the business lending market, and potential implications for policymakers.

Key findings

Crowdfunding is still relatively uncommon compared to other forms of finance. In the LSBS, 1.8% of all firms are using crowdfunding, compared to 42% using bank overdrafts. Crowdfunding appears to be relatively difficult to obtain compared to other sources of finance, based on comparing success rates of applications for different sources of finance. Across both crowdfunded and non-crowdfunded firms, finance is most commonly used for working capital and cashflow.

Crowdfunded firms are of a similar size and sector make-up compared to other SMEs. We find that crowdfunded firms are more likely to have innovated by introducing new or improved goods in the past three years, compared to non-crowdfunded firms. We find a similar pattern for new or improved services (marginally statistically significant). There are no other significant performance differences between crowdfunded and other SMEs.

Crowdfunding and growth

Alternative finance, largely taken to mean equity-based crowdfunding and peer to peer lending, is a small but growing source of finance for small businesses in the UK. It has been estimated that around £2.8 billion of gross lending was facilitated by online platforms in 2015, an increase of 76% on 2014. On a per capita basis, the amount of lending enabled by online platforms in the UK is on par with the US, and much higher than those seen in other European countries.

This paper sets out the results of an analysis of Wave 1 of the new Longitudinal Small Business Survey (LSBS). The LSBS is a telephone survey of 15502 UK small business owners and managers. Our definition of crowdfunding includes: Peer-to-peer lending and equity-based crowdfunding.

Few significant differences emerge in either the observable characteristics (e.g. age, sector, size) of crowdfunded and non-crowdfunded firms. Growth metrics are also broadly similar between groups, apart from the fact that crowdfunded firms are more likely to have innovated. At this point there is little evidence on whether crowdfunding provides any significant growth dividend.

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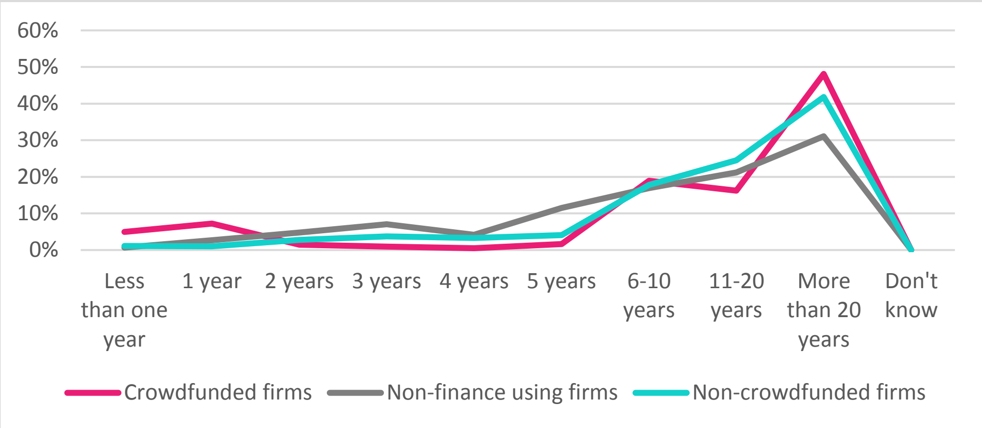
Success rates for obtaining P2P debt are relatively low compared to other forms of finance. This indicates that it is not necessarily easier to obtain crowdfunding compared to other sources of finance. It may be the case that because crowdfunding is newer, more firms are likely to apply, and fewer are discouraged because of past failures to obtain finance. There may be a perception that it is easier to obtain crowdfunding than it really is. Alternatively, it may be the case that higher risk (and potentially more innovative) firms are more likely to apply for this type of financing.

Distribution of age of crowdfunded and non-crowdfunded firms



It is common for crowdfunding firms to be using other sources of finance alongside crowdfunding. Only 13% of crowdfunded firms in our dataset are not using any other form of finance. Bank overdraft (61%) and credit cards (51%) are the most common other forms of finance used. Crowdfunding may therefore be acting as a complement rather than substitute for other funding.

Policy implications

Our analysis suggests that crowdfunded firms tend to be already well-served by the lending market. In this sense, crowdfunding does not appear to be a solution to structural gaps in financing for SMEs, but rather is more likely to compete with more traditional forms of finance, and potentially provide a complementary source of financing for SMEs that are already able to access finance.

Crowdfunding may be less accessible for firms that do not have a traditional company structure, and firms that are ethnic minority-owned. Wider research shows that ethnic minority business owners tend to face other disadvantages that reduce access to finance. From a policymaking perspective, this means that initiatives to increase access to finance will continue to be important even as crowdfunding grows. There may be a case for further investigating ethnic minority access to crowdfunding more specifically, and examining whether differences arise at the application stage (which could be driven by differing levels of awareness) or due to different success rates in obtaining funding.

Full paper link:
http://www.enterpriseresearch.ac.uk/our-work/publications/?type=whitepaper-research