How Do Crowdfunding Platforms Perform Financial Intermediation? Mechanisms and Archetypes

Extended Abstract

In the last decade, the Internet has affected, threatened, and radically changed traditional industries with start-ups introducing innovative solutions, which deeply impacted today's societies and individuals. Especially, the financial service industry is facing radical changes, driven by fast growing *fintech* newcomers, which offer complementary and substitutional products for traditional banking services (Gartner, 2010). By taking unusual ways and providing innovative approaches in order to perform financial intermediation, crowdfunding gained large attention during the last few years, as they are able to move faster and more flexible than traditional financial intermediaries.

In contrast to traditional financial intermediation, crowdfunding intermediation is characterized by certain fundamental differences. First, in crowdfunding intermediation the funding decision and funding activities are no longer reserved to professional financial institutions (e.g., banks) or investors (e.g., venture capitalists) but opened up to the public. Second, crowdfunding intermediation provides funding for projects, who would have struggled via traditional forms of funding by making use of information technology (e.g., Web 2.0, big data analytics, and process automation) (Haas et al., 2015). Third, in contrast to traditional financial intermediation, the crowdfunding intermediary is not involved in the actual funding process (e.g., pooling or lending capital on own account). By contrast, the crowdfunding intermediary serves as matchmaker by linking capital seekers and capital givers directly and by enabling them to exchange value and information.

However, crowdfunding intermediation is not entirely new compared to traditional financial intermediation and the intermediary still is essential due to the existence of transaction costs and information asymmetries (Mahadevan, 2000, Malone et al., 1987, Bakos, 1991, Bakos, 1998). Thus, a theory of crowdfunding intermediation is needed in order to describe how crowdfunding performs the transformation functions of traditional financial intermediaries. As crowdfunding is applied to various purposes, ranging from altruistic donations to profit-oriented funding of start-ups, the way of how the crowdfunding intermediation is actually performed fundamentally differentiates according to the specific crowdfunding setting and aim (Haas et al., 2014). Thus, various instantiations of crowdfunding intermediation exist, which

has been largely neglected in existing literature so far and hampers our understanding about crowdfunding.

In this paper we, thus, address the crucial question of how crowdfunding intermediaries perform financial intermediation. In order to answer this question, we follow a two-pronged approached. We first develop a theory of crowdfunding intermediation and then use this theory for identifying patterns of crowdfunding intermediation by analyzing 160 crowdfunding intermediaries. In so doing, we apply financial intermediation theory to crowdfunding and develop an explanative theory of crowdfunding intermediation. This theory of crowdfunding intermediation considers financial intermediation as the transformation of lot sizes, information, and risk between capital seekers and givers in crowdfunding. These three transformation functions are conceptualized as a set of organizational and technical mechanisms whose implementation determine the type of crowdfunding intermediation being performed by a single crowdfunding intermediary. In two waves of data collection, we collect data on the mechanisms of crowdfunding intermediation having been implemented by 160 crowdfunding intermediaries. Applying various unsupervised and supervised machine learning approaches (i.e., a series of approaches for clustering and classification), we identify three different and temporally stable types of crowdfunding intermediation. First, hedonistic crowdfunding intermediation, which aims at enabling the funding of innovative and creative projects by proposing non-monetary rewards as compensation for capital givers. Second, altruistic crowdfunding intermediation, which enables fundraising for charitable projects without providing compensations for capital givers. Third, profit-oriented crowdfunding intermediation, that comprises financial compensations for capital givers, which is mostly applied for the funding of start-ups and loan lending.

This study provides two important theoretical contributions. First, we extend financial intermediation theory and apply it to the domain of crowdfunding by developing a crowdfunding intermediation theory. This theory extension enables to gain a better understanding of how crowdfunding performs financial intermediation. This helps to illustrate the inner workings of crowdfunding by a set of mechanism and to better understand the similarities and differences between different types of crowdfunding. Also, the developed theory contributes to our understanding of how the digitization, the Internet and the opportunities of innovative information technology do affect traditional financial intermediation. Second, our study contributes to the crowdfunding literature by identifying three dominant patterns of crowdfunding intermediation, which extends current classification approaches as it is theoretically grounded, empirically verified, and provides a more fine-grained perspective on the phenomenon. Our results allow for much deeper insights into the phenomenon of crowdfunding. This will help to systematize research on crowdfunding and helps to inform future designs of crowdfunding intermediaries.

Additionally, our study provides valuable contributions for practice. Traditional financial intermediaries get deeper insights into how the Internet affects their industry and how their core functionalities are performed by applying innovative information technology. This helps to characterize potential competitors in a new competitive arena and helps them gain a better understanding of the disruptive potential of crowdfunding. For established crowdfunding intermediaries and emerging new players in the crowdfunding domain, the identified mechanisms of crowdfunding intermediation basically represent design choices for implementing crowdfunding intermediation. This might encourage current crowdfunding intermediaries to expand their activities and new start-ups to enter the market in order to open up unexploited niche markets, help to establish the phenomenon and to develop it further. For both purposes, the identified mechanisms should facilitate the corresponding design and implementation process.

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