

How Crowdfunding can help bridging the funding gap for SMEs in Europe

The current financial climate has been very detrimental to Small and Medium Enterprises (SMEs) for the past couple of years. The retreat in financing has created a very tough situation at a time where SMEs need to invest to adapt and anticipate a new economic environment. The funding gap that is witnessed today by SMEs is very worrisome for the survival of many of them, and is a real threat for the future growth that Europe could experience in the coming decades.

With the continuing impact of the Internet, new models like crowdfunding have emerged lately to offer alternative ways to contribute to the economic development and therefore job creation. More direct and transparent financing of SMEs is now possible, even though an adverse legislative environment is preventing crowdfunding to express its full potential.

What is crowdfunding?

Crowdfunding is the use of online communities to raise money from individuals to fund a project or an initiative. The investors/donors are typically ordinary citizens with no specific financial background. Crowdfunding platforms are enablers for people wishing to see that their money goes into well-defined entrepreneurial projects.

Based on donations, lending or investment in equities, crowdfunding has proved to be a reliable and scalable solution to fund more and more projects, starting from very early seed financing and going up to funding of development growth.

In its JOBS Act, the Obama administration has validated the benefit of crowdfunding as a tool to develop employment and created a "Crowdfund Act" where investments up to \$2,000 by retail investors for a total consideration below \$1 million can proceed without the burden associated with a standard offer to the public.

What is the situation of crowdfunding in Europe?

Crowdfunding has been prospering, from Asia to Latin America. According to a Massolution survey, as of April 2012, 452 active crowdfunding platforms were identified globally, a number expected to grow to 536 by the end of 2012. Most platforms are in North America, which has 208 (191 in the USA). North America raised the lion's share of the money, with \$837.2 million, over half of the global total and is the fastest growing region. The USA should record an acceleration once the Crowdfund Act is in application at the beginning of 2013.

Europe with 139 platforms (44 in the UK, 29 in the Netherlands, 28 in France, 20 in Germany, 18 in Spain) has been very much in line with what has happened in the USA. Douw & Koren estimated the market size for the Equity based crowdfunding segment in 2011 at a modest €10 million. Equity based crowdfunding is expected to grow exponentially in the coming years.

Despite the increasing number of crowdfunding platforms in Europe, legal constraints and fragmentation of the European market represent an impediment to European platforms to



experience comparable growth to their American peers. Zopa of the UK for example, one of the forerunners in p2p lending on the planet, managed to lend approximately £150 million since its launch in 2005 because of adequate legal framework for personal lending in its home market. But it is currently lagging behind Lending Club, launched in 2007, who has \$600 million worth of lending in total, because Zopa's model is impeded by the legal environments in the other European member states.

European entrepreneurs are currently in a situation in which they are matching American entrepreneurs' initiatives and creativity, but are missing enough elbow room in their own domestic market because of unfavourable legal environments, and are missing scale effect because of the inexistence of a single European market for Crowdfunding that could let them truly succeed in creating a new model for financing SMEs growth throughout Europe.

Why do we need new forms of financing?

Funding of SMEs has always been a difficult area, with Europe lagging behind the USA in equity financing of young startups. Since the 2008 financial crisis, the funding gap, that concerned only growth companies once, worsened because of the retreat of bank financing on many categories of SMEs. It is about to become abysmal and touch large portions of the economic fabric of our society.

Because of Basel III rules, banks will no longer be able to supply credit to many projects. Because of budgetary constraints, public aid won't be able to cushion the disappearance of traditional source of financing for many SMEs either.

Crowdfunding is offering a more direct and transparent way for savers to invest their money directly into industrial or service projects they can relate to.

An EU initiative in this field would have 3 advantages:

- Awareness rising, especially in Member States with little financial engineering culture,
- Standardisation at EU level. An internal market requires a single framework and not 27 different sets of rules,
- Cross-border deals.

What are we proposing?

Our current regulatory environment has been built to safeguard investors when information was costly and difficult to obtain. With the Internet, savers can directly obtain answers from issuers but are not allowed to invest directly their money outside very limited situations. This is why we propose to:

- Raise the threshold below which a company is exempted from making a public offer of securities from €100 000 to €1 million.
- Raise the number of natural or legal persons constituting a restricted circle of investors from 150 to 1 000.
- Create an exemption from making a public offer of securities when the operation is addressed to investors who cannot acquire more than a total consideration of EUR 2 000 per investor, for each separate offer.



Who are we?

“Crowdfunding For Europe” is an open movement meant to let any organization interact and cooperate at the European level. Fellow minded crowdfunding supporters are invited to participate and cooperate:

- by following us on Facebook: <http://www.facebook.com/CrowdfundingForEurope>
- by joining us on: <https://groups.google.com/group/crowdfunding-for-europe>

