



## Equity-Based Crowdfunding Vs. The Stock Market:

### Who Wins?

For most Small and Medium-sized Enterprises (SMEs), the biggest challenge facing their businesses is lack of capital. With banks and venture capital firms setting strict limits on how much money they can lend ; more and more firms are turning to Equity-based Crowdfunding platforms and The Stock Market for a solution. Why these two platforms? We shall cover the reasons in this article. First let us have a reminder of what each of these platforms represents.

Let us start with Equity-Based Crowdfunding. This is a platform that enables the so called unlisted businesses (those not listed on a securities exchange) to raise funds by asking people, 'crowds,' to invest in the company in exchange for a percentage of the shares in the business (equity).

A securities exchange platform is a platform that connects investors to security sellers so that they can buy shares or other securities of a particular company in a regulated environment. It is a regulated marketplace to buy and sell securities. The most popular are the stock market and the bond market. For the topic of this article we will focus on the stock market.

### Understanding The Platforms

Now, the big question is: Are the equity crowdfunding and the stock market platforms rivals?

Yes, No or maybe? While both of these platforms provide methods for SMEs to raise money, their modes of operation are entirely different. Let us see how by understanding how each platform works.

## How does Equity-Based Crowdfunding work?

To successfully raise funds through equity crowdfunding, a business has to advertise itself on a crowdfunding platform. First, they'll create a profile with an overview of the company, their business plan, a pitch deck, a profile of the owners, and a history of financing (if any). Next, they'll have to set a fundraiser goal, specify the campaign timeline, and the percentage they're willing to offer the investors for their money. Once this is done, the campaign will run until they meet their target. If a business can't raise enough funds to meet its target, the campaign shuts down, and the money invested is refunded to the investors. Generally, it is not easy for a crowdfund-equity investor to sell his/her participation at the best possible price later on. We will touch upon on this issue of "liquidity" later.

Note: Most crowdfunding sites have a strict due diligence process that every business has to undergo, to validate the authenticity of the business, and to protect investors' money.

## How does a Securities Exchange work?

A securities exchange is essentially a marketplace for both investors and sellers. It allows sellers and buyers to trade securities under a standard regulated environment for transparency. Businesses listed on a stock exchange get to define their companies in terms of shares, i.e., 'xx million' shares. They then choose to sell a number of their shares to investors, who, in turn, become shareholders of the company. So, if the business decides to sell 10,000 shares for \$100 each, the business gets \$1 million in fresh capital. The investor can choose to sell the shares back in the market based on their evaluation of the business' performance in the stock market. Lastly, Securities Exchange platforms earn their income with membership fees, listing fees, and trading-transaction fees.

## The Benefits and Challenges

Now that we know how both platforms work, you would probably wonder: what are the benefits and challenges of choosing these platforms? From the SMEs perspective, let us start with the benefits and challenges of equity-based crowdfunding followed by the benefits and challenges of a securities exchange.

## Benefits of Equity-Based Crowdfunding for SMEs

### ➤ **Easier access to Investors**

Crowdfunding platforms make it easier for SMEs to access accredited investors. Since they get to showcase their work to a large number of people, the chances of attracting investors and customers significantly increase.

### ➤ **Brand awareness and marketing**

An equity crowdfunding campaign serves as an excellent opportunity for companies to market their services and products. With the help of social media, it becomes an easy way to draw attention to your site and attract more customers and credible investors.

### ➤ **Great for research**

Through equity crowdfunding, you'll have the chance to interact with prospective investors and discuss your plans and ideas. You'll also get their feedback, which should help you determine if your product is viable in the market.

## Challenges of Equity-based crowdfunding for SMEs

### ➤ **Maintaining campaigns**

While setting up your campaign is simple, the real task starts with maintaining it. It's possible you'll spend a lot of time and money creating attention to your campaigns on social media and the platform – which wastes a lot of time that you'd have used to work on your business.

### ➤ **Your reputation is on the line**

Raising funds through Equity crowdfunding may be a good way to get 'cheap money,' but it's more than that. If you fail to reach your fundraising target, your reputation will take a massive hit. Both your customers and potential investors may lose faith in your services/products.

### ➤ **You give up part of your business**

With every investor who funds the venture on an equity basis, you lose a portion of your business. The more investors you have, the less you own. If you're not careful, this can lead to having an inexperienced management team.

## Benefits of using a Securities exchange for SMEs

### ➤ **Easy access to capital**

Businesses can quickly raise more funds for development by putting more shares in the market. This means that they won't have to take debts to cover operating costs.

### ➤ **Increased visibility**

Going public with your business is one of the best ways to draw attention and increase your market visibility. This visibility attracts more customers and investors to your operations. You might also get the attention of the press – which is good.

### ➤ **Ability to retain quality employees**

With a public company, you can reward your best employees with stock options and other incentives that will retain them. You'll also become visible and attractive to the top talents in the industry.

### ➤ **Better credibility**

When you go public, your company is subject to a lot of scrutiny. This proves your transparency to clients, customers, and potential investors, and helps build trust among them.

## Challenges of a securities exchange for SMEs

### ➤ **More transparency**

While transparency is often a good thing for a business, it can also be somewhat harmful. Since you'll be under a lot of scrutiny, the general public, including your competitors, will have access to your business's most relevant information. You'll lose some “confidentiality”.

### ➤ **Less management/ownership control**

Once you start trading shares of your company, the management structure mostly changes. You'll now have to deal with a board of directors and other stakeholders to make decisions regarding the business, even if you're the majority shareholder.

## Joining Forces

What would happen when an Equity-based Crowdfunding and a Securities Exchange work together?

Despite this being rare for most businesses, combining equity-based crowdfunding and stock exchange amounts to numerous benefits, not just for SME businesses but also for investors. For one, investors from the crowdfunding platforms get more liquidity as they can trade their shares in a company with other investors through the Securities Exchange. Secondly, it enables SMEs to raise more than enough funds for their operation and expansion costs – allowing them to enter the capital market. The merger also increases the visibility of most equity-based crowdfunding campaigns since the business will have to go public. This will attract more investors and clients to the platforms. The scrutiny involved in the Stock Market will also reduce the numbers of fraudulent campaigns in crowdfunding platforms.

Nevertheless, when these two forces join, challenges also crop up – the biggest of them being regulations. Since both the equity-based crowdfunding platforms and the securities exchange platforms may run under different regulatory authorities, it becomes a bit “diffuse” to properly regulate the buying and selling of stocks or other securities. The regulatory framework for equity-based crowdfunding platforms is also considered quite ambiguous, and thus, it creates room for many loopholes for conducting trades.

## Final thoughts

After comparing Equity crowdfunding with the Stock Market, we can conclude that they are very different from each other and its therefore unfair to compare them with the same parameters. Crowdfunding will be the preferred option in some instances, while the stock market will be the preferred choice in other cases. It all depends on the startups and SMEs needs, but for equity crowdfunding platforms and the stock market to join forces could certainly help business growth and could be beneficial for a country's economic growth in the long run. It is a proposal both the equity-based crowdfunding platform owners and securities exchange management should consider and discuss with their stakeholders and regulators.

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