
Is Sri Lanka Ready to Accept Crowdfunding as a Fundraising Mechanism?

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A B S T R A C T

The emergence of information technologies has promoted the alternative finance industry to fund entrepreneurial interventions all over the world. Crowdfunding is one of the viable alternative sources of financing for start-up ventures. The typical process is that a pool of investors is funding a certain venture via an internet platform expecting a monetary or non-monetary return. Even though this method is well popular in the developed world, the developing world is still in its infancy in using it for fund generation. Adaptation of crowdfunding requires certain conditions in the economy such as technology, culture, regulations, etc. Thus, the aim of this paper is to assess the readiness of accepting crowdfunding in Sri Lanka. The crowdfunding readiness- self-assessment tool proposed by the World Bank was used for the survey to study the level of readiness of the country in terms of technology, culture, capital, and regulations. The questionnaire included 26 items representing four main pillars of the assessment tool. 78 responses received from the online survey were used for identifying the current readiness level of the country to implement crowdfunding. The highest value of the four main sections of the assessment tool was obtained for technology while the other three sections obtained values between 2-4, which shows that there is a potential. But on the other hand, it was evident that some adjustments to the existing conditions are needed. The results of the study would be useful for policymakers and platform owners.

Keywords: crowdfunding, crowdfunding readiness tool, Sri Lanka

1. Introduction

Expansion and advancement of Internet technologies are the reasons for the breakthrough revolutionary methods of doing business, investing, and thus searching for seed money for implementing business ideas. Accordingly, these alternative models for financing new ventures reflect the alternative finance industry. Crowdfunding is one of the methods of alternative financing which is a sub-category of the widespread concept known as

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crowdfunding, which is a method of fundraising via an Internet platform to achieve a common goal where a pool of individuals contributes to small amounts. Moreover, the growing frustration with traditional financial services allows crowdfunding to gain momentum (Stasik & Wilczyńska, 2018). Additionally, the growth of financial technology, 'fintech' is another reason for the revolution of new fundraising platforms which challenges existing financial institutions because they deliver an economic value and value-added services for start-ups (Yang & Lee, 2018). Accordingly, these alternative models for financing new ventures reflect the alternative finance industry.

The rapid development of the alternative funding industry contributes to the popularity of crowdfunding too as a method of alternative source of funding for small ventures. The alternative funding industry is still a young industry and crowdfunding is one of the products in this industry. It has been growing over 300% from 2014-2015 in the Asia-Pacific region (Zeigler, et al., 2018). Alternative finance industry report for Asian Pacific Region emphasized that the online alternative finance industry will surely take roots and thrive in the World's most populous region. Further, it emphasizes that these financing models may have the greater capacity to stimulate economic and regional development, spur innovation and creativity, improve capital market efficiency and access, promote gender equality, and empower financially marginalized and disenfranchised populations (Zeigler, et al., 2018). Based on that, comparing the traditional sources of capital for small ventures, alternative financing models are characterized by easy access and reduced transaction costs for both entrepreneurs and investors. Additionally, the nature of global accessibility allows the founders to bring their business ideas within the whole online population around the globe.

Due to the importance of crowdfunding, the operations of the crowdfunding industry have been growing 182% in South and Central Asia over the last four years (Ziegler, et al., 2018). This is one of the forms of financing entrepreneurial ventures used mainly in developed countries. It is a potential tool for the developing world to support innovation, growth, and jobs (Best et al., 2013). The rapid development and usage of information technologies allow the developing world to adopt such financing tools in order to get the benefits of alternative financing. Moreover, the growing frustration with traditional financial services allows crowdfunding to gain momentum (Stasik & Wilczyńska, 2018).

Adaptation of this new alternative method in different economies depends on several factors. Since it involves a considerable level of technology utilization, countries require a certain level of technology utilization, and an entrepreneurial ecosystem that fosters entrepreneurial interventions. Additionally, there are certain challenges in the crowdfunding industry regardless of the country in which it is operating such as, transparency problems of reporting performance and activity levels, risk, lack of required regulatory background, lack of education about alternative funding industry in the overall society, etc. (Current state of crowdfunding in Europe, 2016). Since most of the developing countries have high context cultures, there are certain issues of building relationships between investors and entrepreneurs in this online context.

In this situation, it is worthy enough to assess the socio-economic environment of Sri Lanka to know the suitability and feasibility of crowdfunding as a tool of fundraising. Accordingly, the aim of this study is to investigate the readiness of the country to introduce crowdfunding. To achieve this objective this study expects to focus on the readiness of

accepting crowdfunding in the Sri Lankan economy based on four main areas proposed by (Best et al., 2013) as technology, entrepreneurial culture, capital, and regulations. Before the initiation of crowdfunding in the economy, assessing the readiness of people in the country is an important preliminary activity.

2. Literature review

2.1. Crowdfunding

Crowdfunding is derived from the term crowdsourcing, which describes the process of outsourcing tasks to large numbers of individuals (Hemer, 2011). Since crowdfunding is still going through an evolutionary flux, it is difficult to provide a complete definition (Mollick, 2014). The word crowdfunding can be identified as a proverb as “many a little makes a mickle” which means large amounts of money can be raised by accumulating small contributions (Gierczak et al., 2016). Mollick (2014, p. 2) has redefined the concept of crowdfunding in entrepreneurial context as ‘the efforts by entrepreneurial individuals and groups- cultural, social and for -profit- to fund their ventures by drawing on relatively small contributions from a relatively large number of individuals using the Internet, without standard financial intermediaries’. Further, Alegre and Moleskis (2016) have operationalized the definition as ‘an alternative model for project financing, whereby a large, dispersed audience participates through relatively small financial contributions, in a purposeful project, in exchange for physical, financial or social rewards. It is usually done via Internet-based platforms that act as a bridge between the crowd and the projects. Accordingly, it has eliminated the role of intermediary parties who were in the traditional sources of entrepreneurial finance such as bank loans, venture capitalists, business angels etc (Schwienbacher & Larralde, 2010). Thus, it brings people with disposable income, a new way to give to others and invest in projects which are expecting funds for implementation through online transactions (Gerber & Hui, 2013). Since the late 1990 crowdfunding was used in creative industries for their aesthetic projects and until 2006 it was a closed shop phenomenon (Hemer, 2011). The crowdfunding model combines the characteristics of online philanthropic behavior, online consumer behavior, online peer-to-peer lending, and online peer production (Gerber & Hui, 2013). It is a model where, investors can receive community-based experiences that generate community benefits. Additionally, crowdfunding can be treated as a type of market in which the creators produce and market their ideas or products and supporters consume those (Gerber & Hui, 2013).

Crowdfunding is an umbrella concept that can be identified in different models. Accordingly, it can be categorized into two broad categories as investment crowdfunding and non-investment crowdfunding. Investment crowdfunding includes models as equity-based crowdfunding, lending-based crowdfunding, and invoice trading whereas non-investment models consist of donation-based crowdfunding and reward-based crowdfunding (Ziegler, et al., 2018). Accordingly, investment models provide a monetary return for the investors, and non-investment crowdfunding offers non-monetary gains such as a token of appreciation or the pre-purchasing of products or services or just a self-satisfaction of supporting. There are two strategies that fundraisers can use in receiving funds through the crowdfunding campaign such as ‘All or nothing’ (AON) or ‘Keep it all’ (KIA) (Hemer, 2011). In the AON model the fundraiser will receive the funds only when the total amount of campaign target is reached. Belleflamme et al., (2010) named this model as the threshold pledge model. If the funding target amount is not achieved within the campaign period (usually 60 days), the entrepreneur may receive nothing in the fund-raising campaign. Differently, in the KIA model, a fundraiser may have the opportunity to receive whatever the amount accumulated

during the campaign period regardless of the funding target achieved or not. Thus, this is a flexible funding strategy.

Crowdfunding as its nature of using web-based platform for linking founders and funders, it consists of several advantages such as lower searching cost for funders, reduced communication cost to gather information and monitoring the project (Alegre & Moleskis, 2016), lower capital cost as an alternative source of finance (Agrawal et al., 2014), attract public attention (Belleflamme et al., 2014) engagement in product development (Agrawal et al., 2014). Moreover, the benefits for founders and funders are different for different types of crowdfunding models. Accordingly, ventures can use different crowdfunding models over the life cycle of their ventures (Paschen, 2017). Choosing the best crowdfunding method is important for startup ventures as they allow different forms of benefits for both founders and backers. For instance, in the pre-startup stage ventures can use donation crowdfunding as it provides an opportunity for entrepreneurs to solve customer problems as it brings the new business idea to the public (Paschen, 2017). Additionally, there are a range of benefits that crowdfunding offers for SMEs at their early stages such as it guarantees access to capital, permits to develop and test a concept, hedges risk, allows brainstorming with the comments, feedback, and ideas from the crowd serves as a marketing tool, introduces potential loyal clients, it is easier than traditional tools, and makes possible the pre-selling (Rossi, 2014).

2.2. Crowdfunding in developing countries

In the developing world, the banking sector is the dominant player in providing external finance for entrepreneurs. But there are many challenges for banks as providing finance since it does not meet the demands of small ventures in the absence of clear financing history. Additionally, the banking sector in developing countries is underdeveloped, which does not address the customer demands. Based on this claim there is substantially larger potential in the developing world than matured economies for alternative financing such as crowdfunding. Lewis et al. (2020) reported that even though crowdfunding is growing in popularity, it should further be broadly legitimated and institutionalized.

The World Bank publication 'Crowdfunding's potential for the Developing World' identified that building a crowdfunding ecosystem depends on key enablers of trust. The trust over this new investment vehicle will create through, a) a regulatory framework that leverages the transparency, speed, and scale that advances in technology and the Internet can deliver to early-stage funding marketplaces; b) strong social media market penetration and Internet usage, which is necessary to harness demographic and technology trends to drive collaboration and cultural shifts; c) a regulated online marketplace that facilitates capital formation while providing prudent investor protections through education and training; d) collaboration with other entrepreneurial events and hubs including business plan competitions, incubators, accelerators, universities and co-working spaces to create a channel for opportunity and oversight (Best et al., 2013).

In the process of adaptation, it should be concerned about the success factors, environmental factors (including technological, regulatory, cultural factors), and also it is needed to ensure investors and entrepreneurs with the benefits (financial and non-financial benefits) of different crowdfunding models. There are certain barriers for the implementation and usage of crowdfunding as a financing source. For instance, Yang and Lee (2018) have pointed out the factors that negatively affect the choice of using crowdfunding as operational cost of managing crowdfunding campaigns, reputational risk due to failure of

crowdfunding campaigns, business information disclosure, crowdfunding complexity, etc. Further, considering developing countries, there are certain barriers to implement crowdfunding such as the absence of crowdfunding know-how, scarcity of government support and vulnerability of security, risk of reputation, and unfavorable nature of crowdfunding (Islam & Khan 2019). Accordingly, Sancak (2016) also shows that regulatory flexibility is important in the successful implementation of crowdfunding.

2.3. Crowdfunding in Sri Lanka

The concept of crowdfunding is not a novel concept for the country. As a country, which is characterized by a collective culture, it has been a tradition of Sri Lankans in helping others and helping socially valuable events together. For instance, most of the religious activities, community projects are funded by small contributions of a large number of people in the society. Almost all the religious ceremonies are funded by people in the community with a small amount of money from each person. Thus, offline crowdfunding is a common method of fundraising in Sri Lanka. A shred of exceptional offline crowdfunding evidence could be found in the country over 60 years ago with the efforts of finding funds for the leading Sri Lankan vocalist and composer, W. D. Amaradewa (1927-2016) to get specialized music training in India (Gunawardene, 2018). The campaign was run through Lankadeepa daily newspaper together with the leading scholar Prof. Ediriweera Sarachchandra which initiated the Amaradewa Scholarship fund from contributions from rich and poor. These donation-based contributions allowed Amaradewa to complete his studies in Bhatkhande Music College in Lucknow, India, in October 1953 for five years of studies in classical music. Another remarkable donation crowdfunding offline campaign can be found in history with the initiation of the 'one cent fund' launched by P de S Kularathna as the Principal of Ananda College, Colombo (Gunawardene, 2018). Word of mouth was the communication medium in this campaign where all students and teachers were asked to collect contributions from crowds in Colombo to support the expansion as a leading Buddhist boys' school from 1918. Modern scenario crowdfunding operates through online platforms which differs from these offline projects due to the usage of internet-based platforms for connecting backers and founders. Accordingly, earlier fundraising mechanisms for socially valuable events/ activities were transferred into technology-based applications with crowdfunding. Word of mouth information or short information of the project shared among interested parties for funding was changed to a visual display of the proposed projects through the availability of internet technology.

There are few crowdfunding platforms operating in Sri Lanka. The first crowdfunding platform in Sri Lanka is Help.lk launched in 2015. The aim of this platform is to attract foreign exchange to the country in terms of investment in donation projects. In the same year, a platform called 'Tribefunds.lk' was launched for basically donation and reward crowdfunding. Later it was expanded for equity crowdfunding also. Additionally, 'crowd island.lk' is another platform specialized for technological equity crowdfunding projects. There are certain projects operated in Sri Lanka which generated funds through these two platforms and Kickstarter (American based platform). For instance, CrisCrush-a digital gaming platform, WST- a platform connecting parents, students, tutors, and educational institutes, Goodnessme-online healthy lifestyle store, Gradchat-campus communication, and networking solution (Crowdisland.lk), apihappi- ergonomically shaped, hand-loomed Cotton Beanbags, made in Sri Lanka (Kickstarter.com) and eLearning.lk- a local language e-learning platform for students in Sri Lanka (Tribefunds.lk) are some of the successful projects operating in Sri Lanka.

3. Materials and methods

In the process of accepting new technology to a particular country, it is needed to assess the current technological and economical background of the country. Accordingly, this analysis is based on the crowdfunding self-assessment tool proposed by the World Bank (Best et al., 2013). It consists of four major areas that the readiness of a country that can be assessed for accepting crowdfunding. They are technology readiness, entrepreneurial culture, capital and regulations. According to their conceptualization, readiness can be measured using four main factors namely, technology readiness, entrepreneurial culture readiness, regulatory readiness, and capital availability. Technology readiness explains the level of technology and education necessary for the application of crowdfunding. Secondly, the culture of entrepreneurship in the country is assessed as a critical factor as the society identifies entrepreneurship as a reputable career or not. The third dimension is the regulations that may enable or deter entrepreneurship and crowdfunding in the country. Finally, the capital represents the availability of financial resources for the development of entrepreneurship in the country provided by government or non-governmental entities.

There are 26 items in the questionnaire of crowdfunding self-assessment index. The first 6 items measure the level of technological developments, the next 11 items measure the level of entrepreneurial culture, the next 4 items measure the regulatory background of the country, and the last 5 items measure the capital availability of the country to facilitate entrepreneurship. Scores are given from 0 (the lowest level) to 10 (the highest level). The scores obtained from the survey were calculated as average values to get the score for each dimension. Based on the score of each dimension, the spider web chart was formulated in Excel charts.

It is recommended to use not less than 20 participants from different fields to fill out the self-assessment questionnaire. The group of participants includes policymakers, NGOs, investors, and entrepreneurs (Best et al., 2013). Accordingly, this self-assessment questionnaire was sent to different participants purposely to collect the responses. Accordingly, this analysis is based on 78 responses received from an online survey which is done with a purposely selected sample. Among the respondents, 42 (54%) were entrepreneurs, 16 (20%) were investors (bankers, lecturers, other professionals who are capable of investing) and 20 (26%) were business consultants. Based on the recommendation of the Self-assessment tool, the results received for each criterion were further elaborated in the discussion with other secondary data from reputed reports which provided cross-country information.

4. Results and discussion

The responses received for the online survey were then used to formulate the spider chart which shows a clear picture of the present readiness conditions in the country to accept crowdfunding. Figure 1 shows the spider web chart of the crowdfunding self-assessment. The overall readiness ranking is 4.075 considering all the four pillars of ranking. According to recommendations from a self-assessment tool (Best et al., 2013), if this cumulative index value is between 4-6, it shows that there is a good chance crowdfunding can be successfully implemented in the country. Thus, there are good opportunities for implementing crowdfunding in the country. This can be further elaborated and explained with individual scores for four indicators. According to the values received for each dimension of the self-assessment tool, the readiness for accepting crowdfunding can be explained.

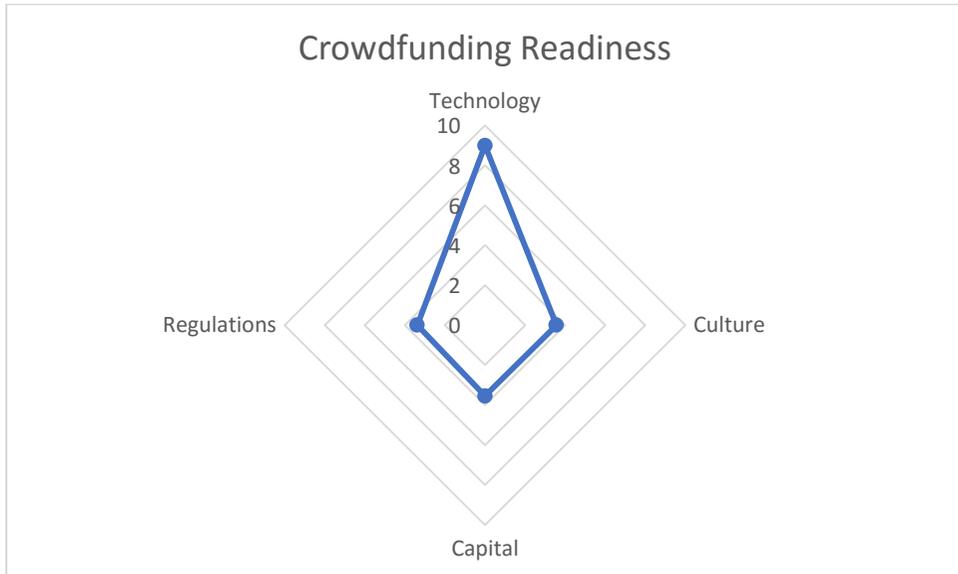


Figure 1: Crowdfunding Self-Assessment Values

4.1. Technology readiness

This indicator includes both technology and education as necessary components for accepting crowdfunding. It has got the highest ranking among the four dimensions reflecting a value of 8.99. This value indicates that web/mobile technology is seen as a mechanism for communication and collaboration, and thus the environment is ready to engage in entrepreneurship and investment through internet-based platforms. This figure indicates that as a country, Sri Lanka is considerably satisfactory in terms of technology to accept crowdfunding. Thus, the technology is readily available in the country, where technology and social media can be easily utilized for promoting crowdfunding and crowdfund investing as a mechanism for promoting entrepreneurship (Best et al., 2013).

The technology readiness of the country can be further shown through the Network Readiness Index (Dutta & Lanvin, 2020). Network Readiness Index for 2020 was formulated with four pillars as technology, people, governance, and impact. According to the report, Sri Lanka was ranked 83 out of 134 countries and it is quite higher than the countries in the lower-middle income group average.

4.2. Culture readiness

This dimension is formulated to measure whether a culture of entrepreneurship exists and whether the culture accepts entrepreneurship as a reputable career. This fact is important since it reflects cultural readiness for generating ventures. The value for the culture is 3.56, which means that there is limited understanding of risk capital and entrepreneurship (Best et al., 2013). Further, it reflects that there is a need for encouraging the risk-taking abilities of entrepreneurs in society so that they choose the risk of accepting new methods for fundraising. Entrepreneurial culture is important for an economy for the development of entrepreneurship which may ultimately contributes in generating income, employment, and foster innovations. Entrepreneurial culture reflects “a society that depicts the exhibition of

the attitudes, values, beliefs (attitude or mindset) and behaviors associated with entrepreneurs by individuals in such a society which distinguishes them from others” (Brownson, 2013).

Sri Lanka has a fair culture that fosters entrepreneurship. The government of Sri Lanka has consistently implemented a range of programs for encouraging an entrepreneurial culture in society. Recently the ‘Innovation and Entrepreneurship Strategy 2018-2022’ has been put forward by the government with the aim of fostering entrepreneurship in the country (Wijesinghe, 2019). The strategic objectives of this five-year plan include, 1) support SMEs to innovate and become more competitive in domestic and export markets, 2) build the ecosystem for scaling up growth-oriented start-ups, and 3) modernize and re-align the R&D sector to be more enterprise-oriented. In addition, there is a range of programs implemented by the government such as Enterprise Sri Lanka with the goal of creating an entrepreneurial culture within the country. Moreover, the Ministries of Rural Development and Youth Affairs and Sports, National Enterprise Development Authority are some of the regulatory bodies which are engaging in a range of programs for creating an entrepreneurial culture in the Sri Lankan economy.

4.3. Capital readiness

The capital readiness dimension shows the availability of financial resources in the market for initiating entrepreneurial interventions. The value for this dimension is 3.54. According to the crowdfunding self-assessment tool recommendations (Best et al., 2013), this value reflects that the availability of private capital in the business environment but necessarily not a robust market exists. Further, it reflects that in the country, the government should reconsider the restrictions for generating private capital. When there is too much bureaucracy and regulations and high costs for generating private capital in the economy, there is less room for implementing alternative sources of financing such as crowdfunding.

4.4. Regulation readiness

The final dimension of the self-assessment tool is regulations. Economic regulations are an important element for enabling new investment models in the economy. The value for this dimension is 3.38 which is the lowest value among the dimensions. This means that there is a fair amount of regulation in the economy, but the government is required to analyze the existing securities laws for ways to enable business and capital formation.

An effective regulation regime will minimize fraud and maximize transparency in crowdfunding while keeping the transaction cost low (Weinstein, 2013). In some countries there are certain regulations governing crowdfunding activities. It is needed to have a certain regulatory framework to protect unsophisticated investors as well as entrepreneurs and to avoid the risk of using crowdfunding for generating funds. But there is no such direct regulation for crowdfunding in Sri Lanka. To some extent regulations related to e-commerce transactions cover some aspects of crowdfunding, especially, payments methods, etc. In the backdrop of this fact, there are only a few crowdfunding platforms available in Sri Lanka. One of the reasons for the less popularity might be the lack of regulations for governing the activities.

5. Conclusion

This paper aimed to investigate the readiness in introducing crowdfunding in Sri Lanka. In this regard, a survey method was used for gathering data for the assessment. The World Bank

Publication 'Crowdfunding's Potential for Developing World (Best et al., 2013) was used as it is one of the two institutional reports covering crowdfunding in developing contexts. Accordingly, a self-assessment tool was used for ranking the country's readiness assessment and four dimensions of crowdfunding ecosystems proposed in the report were used for presenting the facts that are related to the crowdfunding ecosystem.

The overall readiness ranking shows that Sri Lanka needs some changes in the financial, economic, entrepreneurial cultural sectors to implement crowdfunding successfully. But in terms of technology, Sri Lanka is at a very satisfactory level because technology is readily available in the country. Changes in culture and regulations which are conducive for crowdfunding are important for the adaptation process. Creating a strong entrepreneurial culture through entrepreneurial education is important for building trust, risk-taking, entrepreneurship, and collaboration. This will facilitate both entrepreneurs and investors to accept the benefits of crowdfunding while bearing the risks such as plagiarism risk, market risk, transaction risk, financial risk which are inherited for crowdfunding. Accordingly, the overall ranking of the self-assessment also shows a satisfactory level where it needed certain adjustments for the existing conditions to successfully implement crowdfunding.

The result of the study provides insights for policymakers to reconsider implementing policy frameworks for encouraging alternative financing sources as the country is at a satisfactory level of readiness in accepting such methods. Entrepreneurial culture should be created through educational programs since it is still lacking in the society. To achieve that, educational reforms may require to enhance creativity and innovation among students. It may finally create a generation who are willing to accept entrepreneurship as their first career choice. Further, considering the entrepreneurial culture, there are certain programs operated by government entities to foster entrepreneurship in the country, which can support implementing such newer financing sources among interested parties. The index shows that regulations are not enough to implement crowdfunding in Sri Lanka. In such a situation, policy makers are required to start their work on developing and implementing such regulations to encourage this alternative method of financing since it provides benefits for start-ups. Further, platform owners or operators can initiate their projects in the country since there are satisfactory conditions in the country.

The current study consists of several limitations. The sample was limited to 78 responses. Even though the study used the self-assessment tool recommendation for getting the sample purposely, the assessment may be comprehensive with more responses from different participants. Moreover, it is recommended (Best et al., 2013) to compare and concise the results of the self-assessment tool with other related reports of each indicator. Due to the unavailability of island-wide data related to the same indicators such as entrepreneurial culture, regulations, and capital; the study lacks the comparison of its findings in the Sri Lankan context.

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