

Crowdfunding as an Alternative Financial Innovation for Startup Funding

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Abstract

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The development of financial technology has driven the emergence of various alternative financial innovations, one of which is crowdfunding. Crowdfunding has become a potential solution to overcome the limited access that startups face in obtaining funding from traditional sources such as bank loans or venture capital. This study aims to explain the role of crowdfunding as an alternative financial innovation in supporting startup funding through a systematic review of 12 international academic articles. The results show that crowdfunding is not merely a funding tool, but also serves as an instrument for financial democratization, accelerates startup growth, and encourages community participation in the business innovation process. However, challenges such as regulatory uncertainty, fraud risks, and limited financial literacy among investors remain obstacles to optimizing crowdfunding platforms. This research contributes to a broader understanding of the alternative funding landscape and supports the development of strategic policies to foster the growth of innovative entrepreneurship.

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1. Introduction

In recent decades, the emergence of startups has become a key catalyst in driving global economic growth, particularly in sectors heavily reliant on technological innovation and digital services. Startups are often seen as the engine of industrial transformation due to their significant potential in creating creative and flexible solutions to problems that established companies cannot resolve. Flexibility, rapid adaptability, and the utilization of the latest technology are core advantages inherent in startups (Sreenivasan & Suresh, 2024). However, behind this potential, there are structural and systemic obstacles, one of which is limited access to stable and sustainable funding sources. The issue of funding remains a dominant factor hindering the survival and scalability of many startups, especially those in the early stages of product or service development.

Traditional funding sources such as bank loans, formal financial institutions, and venture capital typically demand quite stringent prerequisites, such as asset collateral, credit history, or a proven business portfolio. Unfortunately, most early-stage startups lack these elements, making them administratively less viable in the eyes of conventional financing institutions. In response to these challenges, the emergence of crowdfunding as an innovation in alternative finance offers new hope that is more inclusive and responsive to the unique needs of startups. Crowdfunding is a fundraising mechanism carried out by collecting financial contributions from a large number of individuals through digital platforms openly. This mechanism comes in several main models, including donation-based, reward-based, lending-based, and equity-based crowdfunding (Mollick, 2014).

In practice, especially in the context of startups, crowdfunding opens direct access between entrepreneurs and the wider community as potential investors or contributors, who not only provide funds but also play a role in shaping the early market and building brand image. This innovation reflects a fundamental shift in the modern financing landscape, from a centralized and institutional financial system towards a participatory and open financial model. This transformation aligns with the global shift towards total digitalization in financial services, driven by two main factors: the rapid advancement of information and communication technology, and changes in consumer attitudes towards personal financial management and investment. Crowdfunding creates opportunities for the public to be directly involved in the value creation process, strengthening collaboration between businesses and their supporting communities.

Nevertheless, the adoption process of crowdfunding as an alternative financing instrument still faces various significant challenges. From a regulatory perspective, the lack of a uniform and established legal framework in many jurisdictions creates legal uncertainty for the parties involved. Investors also face legitimate concerns regarding the risk of project failure, potential fraud, and limited transparency from campaign organizers. Meanwhile, for businesses, the success of a crowdfunding campaign is heavily influenced by their ability to construct a convincing narrative, build credibility, and implement effective digital marketing strategies. Several previous studies reveal that crowdfunding has enormous potential in expanding financial inclusion, accelerating the growth of small and medium-sized

businesses, and supporting economic democratization in a fairer and more equitable manner.

Therefore, it is important to understand more deeply how crowdfunding can function as an effective alternative financial innovation in supporting startup development, as well as to identify its effectiveness and the challenges faced in its implementation in various contexts. This paper presents the results of a literature review of selected relevant academic articles, published during the period 2020 to 2024. This study aims to construct a conceptual framework regarding the functions, working mechanisms, strategic benefits, as well as risks and obstacles of crowdfunding practices in supporting startup funding. Through this approach, it is hoped that a more comprehensive and applicable understanding can be generated, which is not only academically beneficial but also practically useful for startup actors, potential investors, and policymakers in formulating sustainable financing strategies.

2. Literature Review

2.1. Basic Concepts of Crowdfunding and Financial Innovation

Crowdfunding is one of the tangible results of advances in digital-based financial innovation that has successfully brought together entrepreneurs and the general public directly in an open and participatory collective financing ecosystem. Along with the rapid advancement of information technology and the digitalization of the global financial system, the crowdfunding mechanism has evolved into four main forms, each with distinct characteristics: donation-based, reward-based, lending-based, and equity-based crowdfunding (Ziegler et al., 2020). These four

forms offer diverse financing mechanisms and varying risk profiles according to project needs and characteristics, but generally have the advantage of opening up funding opportunities that do not depend on the involvement of formal financial institutions such as banks or institutional investors.

In a comprehensive review conducted by Hoque (2024), crowdfunding is highlighted as an instrument that promotes financial disintermediation, which is the elimination of the role of traditional financial intermediaries that have historically been major barriers to financing access for startups. In addition, crowdfunding also provides positive impacts in the form of early market validation and customer involvement in the business process from the product development phase, making crowdfunding an effective tool for testing the viability of ideas before entering a wider market. The main characteristics of alternative financial innovations such as crowdfunding are flexibility, scalability, and their participatory nature. Modern crowdfunding platforms are even capable of segmenting investors based on risk preferences and specific thematic interests, thereby creating a more inclusive financial system that adapts to the dynamics of market and startup needs.

2.2. The Role of Crowdfunding in the Startup Ecosystem

In the dynamic and competitive startup ecosystem, crowdfunding not only serves as a means to provide initial capital but also plays a strategic role in strengthening the credibility and reputation of newly established businesses. This is because success in raising funds from the general public through crowdfunding platforms can reflect market support and initial trust in the business idea. A study by Xiao (2020) shows that startups successful in running crowdfunding campaigns

tend to gain additional trust from institutional investors. This is due to crowdfunding's ability to function as an early success indicator or success signaling, which is a sign that the business idea has received social validation and has potential for growth.

Crowdfunding is an instrument that actively accommodates a bottom-up financing approach, where the general public not only becomes a source of funds but also acts as a stakeholder. In this context, community involvement can create a network effect that accelerates the organic spread of information, while increasing the attractiveness of the startup in the eyes of the public and other potential investors. Meanwhile, Corsini and Frey (2024) adds that crowdfunding has high strategic value for startups targeting niche markets or developing innovative products that are not yet widely known by the market. In many cases, crowdfunding campaigns are even more effective than conventional market research as a tool to validate consumer interest and demand for new products or services.

2.3. Challenges and Risks of Crowdfunding Implementation

Although crowdfunding provides significant benefits for the startup financing ecosystem, this approach is not without risks and challenges that need serious consideration. One of the main challenges that often arises in crowdfunding implementation is regulatory uncertainty and a lack of adequate legal oversight in many jurisdictions. The absence of clear rules and standard guidelines makes the crowdfunding process vulnerable to misuse. According to Ibrohimbek et al. (2024), the lack of strict and uniform operational standards can open loopholes for fraud,

where investors face a high risk of fictitious projects or manipulative and non-credible campaigns.

Besides legal aspects, the risk of project failure is also a significant obstacle. Kubo et al. (2021) highlights that this risk often causes psychological concerns among retail investors, especially those who lack experience or in-depth understanding of business analysis. Many startups that successfully raise funds through crowdfunding campaigns turn out to lack adequate managerial capacity or a tested business model, so even if the fundraising is declared successful, the execution and business implementation phase may fail entirely. Kaur and Srinivas (2024) also emphasize the existence of information asymmetry between businesses and potential investors. Information imbalance and limited transparency make it difficult for investors to objectively assess project viability. The lack of independent audit systems to verify the validity of funded projects also increases the likelihood of financial losses for investors.

3. Method

This research uses a systematic literature review approach designed methodologically to identify, select, and synthesize scientific articles discussing the topic of crowdfunding as a form of alternative financial innovation, particularly in the context of startup financing. The secondary data used in this study comes from international journal articles accessible online through the Google Scholar platform, with a publication time frame limited to remain relevant to recent developments. The article selection process was carried out in stages to ensure that the sources used

have high scientific quality and direct relevance to the research focus. The first stage was an initial search using the keywords “crowdfunding and financial innovation and startup funding” filtered by publication year. After the initial data was collected, the second stage involved applying inclusion criteria which included: articles must be peer-reviewed, written in English, and thematically closely related to the topic of startup financing through crowdfunding.

Articles that only discussed legal aspects narrowly or focused on overly specific local case studies were excluded from the analysis. From the initial selection, 42 articles were obtained, which were then further reviewed based on the depth of analysis and relevance, resulting in 12 main articles used as primary sources in this study. The analysis of the selected articles was conducted with a descriptive qualitative approach. Each article was analyzed in depth to extract information related to crowdfunding forms and models, the role of crowdfunding in startup financing, and challenges in its implementation in the field. The researchers also examined the methodological approaches of each article, whether empirical studies, systematic reviews, or case studies, to broaden understanding from various perspectives.

Triangulation method was used to compare findings between articles, identify consistency and variations in research results, and construct the main thematic categories used in writing the literature review and discussion. The limitations of this research lie in its reliance on English-language articles and sources that are only available online. Therefore, the findings obtained cannot be universally generalized but are more appropriately considered as conceptual constructs describing global

dynamics in general. Nevertheless, this literature review approach still makes an important contribution to building a comprehensive understanding of the landscape of startup financing through digital-based financial innovations such as crowdfunding.

4. Results

Crowdfunding has shown very significant performance in addressing the classic challenges of funding access that are often and persistently faced by early-stage startups across various sectors. These startups, which typically lack collateral, credit history, or proven profitability, often find themselves excluded from traditional financing mechanisms such as bank loans and venture capital investments. From the synthesis carried out on 12 relevant international academic articles, the majority of studies firmly conclude that crowdfunding is not merely an auxiliary aid or supplementary option, but has gradually and effectively evolved into a robust and dynamic complement to the more rigid and institutionalized conventional financing systems, which are widely deemed to be exclusive, bureaucratic in nature, and often less responsive if not entirely inaccessible to unestablished business models that are rooted in innovation and risk-taking.

In the context of startup funding specifically, the two most widely adopted and applied crowdfunding models that have gained significant traction and practical usage are reward-based and equity-based crowdfunding. Reward-based crowdfunding is strategically utilized as a practical and low-barrier means to attract early buyers, build initial traction, and obtain direct and authentic feedback on the

products or services being offered. This approach not only brings in early capital but also enables entrepreneurs to engage their potential market from the earliest development stages. This dual purpose simultaneously serves as an initial step to test market interest and evaluate product-market fit prior to embarking on a large-scale commercial launch, which would typically involve higher costs and greater financial exposure.

Meanwhile, equity-based crowdfunding provides a fundamentally different alternative by offering opportunities for capital acquisition from public or retail investors, with the return not in the form of goods or rewards, but in actual equity ownership or shares in the company. According to Hoque's findings (2024), this equity crowdfunding model has the transformative potential to reshape and restructure the traditional capital architecture of startup companies. It does so by reducing the over-reliance and often-dominant influence of large institutional investors, and instead opening up more democratic pathways for public participation as shareholders. This shift ultimately serves to expand the support base and build broader stakeholder engagement for the entrepreneurial venture, especially in its formative phases.

The effectiveness of a crowdfunding campaign, however, does not merely depend on the quality of the business idea, innovation, or technical feasibility of the product or service being proposed. It is also significantly influenced by a range of non-technical factors that are equally, if not more, important. These include elements such as the strength of the campaign's narrative, the personal credibility and background of the business founders, and the emotional connection that the

entrepreneurs can successfully establish with the supporting community and potential backers. Convincingly that qualitative elements like compelling storytelling, transparency of information, and alignment of values are critical determinants in attracting supporter interest and encouraging them to contribute. Therefore, strong digital communication capabilities, or what is often referred to as soft skills, become indispensable assets and determining factors in the overall success and reach of crowdfunding campaigns.

Additional findings from the research conducted by Stevenson et al. (2024) further validate the strategic role of crowdfunding, particularly in the early stages of product development when a startup is still operating at the minimum viable product (MVP) stage. At this critical juncture, the need for financial resources to support initial production, build prototypes, and conduct market validation is typically very high. Unfortunately, access to capital from formal financial institutions remains extremely limited during this phase due to the perceived high level of risk and lack of historical data. Crowdfunding, in this scenario, emerges as an ideal and innovative option, as it enables startups to secure funding without incurring debt obligations or sacrificing operational control. At the same time, it facilitates real-time testing of market reactions, allowing startups to make data-driven adjustments before scaling further.

The social aspect of crowdfunding also carries significant and undeniable economic implications that go beyond the immediate act of financing. Crowdfunding platforms also play a pivotal role in accelerating financial inclusion, particularly for startup founders coming from underrepresented social backgrounds

or those operating in non-conventional, high-risk, or niche sectors that are often marginalized in traditional formal financing systems. These findings illustrate that crowdfunding serves not only as a catalyst for economic growth in a broad sense, but also as a vehicle for fostering more equitable access to financial opportunities. In other words, crowdfunding actively contributes to the creation and development of a financial system that is not only inclusive but also fairer and more socially just contributing directly to the pursuit of economic justice on a wider scale.

However, the results of this study also highlight several structural and systemic obstacles that continue to hinder the full realization and optimal expansion of crowdfunding's potential role, especially at the global level. One of the most persistent and widely recognized challenges is legal and regulatory uncertainty across various jurisdictions, which causes both entrepreneurs and investors to adopt a cautious and sometimes skeptical approach when it comes to utilizing crowdfunding platforms. Without harmonized legal standards or sufficient protective frameworks, the ecosystem remains fragmented and underdeveloped. Xiao (2020) suggests that in the absence of a strong and clearly defined legal infrastructure, as well as adequate investor protection mechanisms, both sides of the crowdfunding equation namely, the businesses seeking capital and the investors providing it are likely to be hesitant, reluctant, or even completely unwilling to engage in this community-based form of financing on a meaningful scale.

In addition to legal uncertainties, issues related to reputation, credibility, and public trust in crowdfunding platforms also represent substantial challenges. According to analysis by Kubo et al. (2021), more than 40% of crowdfunding

campaigns fail to reach their funding targets, which reflects inefficiencies in project design, marketing strategy, or target setting. Moreover, even among the subset of campaigns that do manage to reach or exceed their funding goals, only a small portion successfully transition into long-term sustainable business entities. These findings indicate that the current mechanisms used for selecting and curating projects to be featured on crowdfunding platforms remain relatively weak and inadequate. This situation underscores the critical need for crowdfunding platforms themselves to take on a more active and responsible role in curating submissions, assessing the technical and commercial feasibility of proposals, and conducting thorough early-stage verifications to ensure that only high-quality and credible projects are introduced to the public.

Another persistent challenge that consistently emerges in the context of crowdfunding is the problem of information asymmetry. This occurs when there is an unequal distribution of information between entrepreneurs and potential investors, often resulting in the latter lacking the tools, skills, or knowledge required to make informed and objective investment decisions. Many individual or retail investors participating in crowdfunding do not possess advanced expertise in financial or business analysis, which leaves them vulnerable to biased information, overly optimistic projections, or even deceptive campaigns. In response to this challenge, some crowdfunding platforms have begun to implement structured solutions, such as introducing standardized project rating systems, offering regular and transparent progress reports, and integrating with supporting fintech services designed to assist investors in risk assessment and decision-making processes.

Ibrohimbek et al. (2024) emphasize that such systematic approaches hold great potential to significantly enhance overall market confidence and trust. By improving transparency, accountability, and investor education, these efforts can encourage wider and more active public participation in the startup funding ecosystem through crowdfunding (Logue & Grimes, 2022).

In conclusion, the collective body of evidence presented in these 12 studies underscores that while crowdfunding continues to face notable regulatory, operational, and informational challenges, it nonetheless represents a powerful and transformative financial innovation. It not only addresses funding gaps but also democratizes capital, fosters early market engagement, and promotes inclusive economic growth. With continued regulatory support, technological refinement, and ecosystem-wide capacity building, crowdfunding can serve as a critical pillar in the future architecture of startup financing.

5. Discussion

Based on the comprehensive findings obtained from the literature analysis, it can be concluded that crowdfunding holds an increasingly strategic and influential position in supporting the overall growth and sustainability of startups, particularly during their early stages of development. These initial stages are generally the most vulnerable to business failure, primarily due to the limited access to conventional capital and the rigid criteria imposed by traditional financial institutions. In this regard, reward-based and equity-based crowdfunding models emerge as the two most suitable and widely adopted formats for assisting startups, owing to their

inherently flexible nature, their orientation towards market testing, and their capacity to open up alternative, non-traditional channels of financing that were previously inaccessible to most early-stage ventures.

Reward-based crowdfunding offers dual and complementary benefits. In addition to raising the necessary capital to support initial business activities, it simultaneously serves as an effective early-stage marketing and customer engagement tool. Entrepreneurs can use this model not only to secure funding but also to gauge public interest, validate product ideas, and build a community around their brand. Equity-based crowdfunding, on the other hand, represents a structural breakthrough by opening up investment opportunities to the general public an opportunity that was historically limited to institutional investors or high-net-worth individuals. This contributes significantly to the democratization of startup investment and promotes broader community ownership (Farè et al., 2023)

In terms of campaign effectiveness, the success of a crowdfunding initiative is heavily dependent on the entrepreneur's capacity to construct a strong, emotionally engaging narrative that resonates with the target audience. Digital communication proficiency, clarity of the overall business vision, and the trustworthiness and credibility of the execution team are among the most critical determinants of campaign outcomes. Campaigns that merely focus on showcasing the product without adequately considering the elements of trust-building and community participation often fail to gain traction or support. This highlights the fact that within the realm of crowdfunding, social and emotional dimensions are just as crucial as technical and financial considerations.

Nonetheless, the discussion surrounding the promise of crowdfunding cannot be meaningfully separated from its associated risks and structural limitations (Kim et al., 2022). Regulatory uncertainty remains a persistent challenge that requires serious and proactive attention from policymakers across jurisdictions. Without clear, consistent, and enforceable regulations, hesitation and doubt will continue to overshadow the confidence of both investors and businesses. Furthermore, risks related to project failure and the potential for fraud may severely damage the overall credibility and long-term sustainability of crowdfunding platforms if not addressed through robust protection mechanisms.

Another important concern is the issue of information asymmetry, which often arises due to the lack of adequate investor knowledge and access to objective project assessments. Small and individual investors who constitute the majority of crowdfunding participants frequently lack the tools, frameworks, or analytical capabilities to properly evaluate the feasibility and risk profiles of the projects they support (Gupta et al., 2024). To address this, the implementation of objective rating systems, the provision of regular performance and development reports, and collaboration with independent audit bodies can serve as effective mitigation strategies. In addition, strengthening financial literacy through targeted education and the development of investor protection features are also essential in building lasting trust and credibility within the ecosystem. Considering all these interconnected findings, it can be strongly affirmed that despite the existing challenges and limitations, crowdfunding remains a highly promising and

transformative financial innovation that warrants continued development and support.

6. Conclusion

Crowdfunding has proven itself as a relevant, innovative, and inclusive funding alternative for startups, especially in the early stages of business development. This approach is able to bridge the funding gap that cannot be met by traditional financial systems, which tend to be selective and bureaucratic. In addition to being a fundraising tool, crowdfunding also functions as a means of market validation, early product promotion, and community empowerment in the innovation process. A literature review of various international scientific articles shows that the success of crowdfunding is influenced by various factors such as the campaign model used, digital communication skills, the credibility of the startup team, and active community involvement. Reward-based and equity-based crowdfunding are the most widely used models by startups due to their flexibility and strategic benefits.

However, despite its great potential, crowdfunding still faces various significant challenges, such as regulatory uncertainty, the risk of fraud, project failure, and information asymmetry between businesses and investors. To optimize the use of crowdfunding, collective efforts are needed to strengthen platform governance, formulate innovation-friendly policies, and provide financial literacy education for potential investors and startup actors. With a more comprehensive understanding of these dynamics and challenges, crowdfunding has the potential to become a main

pillar in the modern financing ecosystem that supports the growth of innovation-based entrepreneurship.

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