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The role of economic and normative signals in international prosocial crowdfunding: An illustration using market orientation and psychological capital

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ABSTRACT

Entrepreneurs in emerging nations are increasingly seeking microloans on international crowdfunding platforms composed of prosocial lenders primarily seeking non-monetary returns. Drawing on signaling theory, we posit that economic signals (as illustrated by market orientation) and normative signals (as illustrated by psychological capital) embedded within borrower narratives will influence funding time. A Computer-Assisted-Text-Analysis (CATA) of 130,964 profiles across 49 countries suggests that borrower cues of customer orientation, competitor orientation, long-term focus, profitability focus, confidence, and optimism are positively associated funding time, while cues of coordination, hope, and resilience are negatively associated with funding time. Prosocial lenders seem less inclined to lend to borrowers that exhibit a desire for economic success or normative expectations for positive outcomes in the future, while they seem to lend more rapidly to those exhibiting current hardship or a concern for people. A discussion of these findings and their implications for poverty alleviation concludes the study.

1. Introduction

Entrepreneurs in emerging nations rarely have access to traditional sources of financing such as bank loans to start their new ventures (Bruton, Khavul, & Chavez, 2011), and their lack of capital may often lead to the loss of opportunities or even venture dissolution (Van Auken, 2002). Historically, microfinance institutions (MFIs) have provided a solution, by issuing small loans to entrepreneurs in emerging nations with the hope that they will help them improve their lives and communities (Bruton, Ketchen, & Ireland, 2013). This logic relies on the idea that supporting an entrepreneurial venture does more good to someone in poverty than simply making a donation (Yunus, 1999). Recently, a new international phenomenon known as prosocial crowdfunding has impacted the microfinance industry with the arrival new funds available for lending (e.g., Allison, Davis, Short, & Webb, 2015; Allison, McKenny, & Short, 2013; Moss, Neubaum, & Meykens, 2015). This evolution has been made possible by the arrival of new a financial technology—crowdfunding platforms—which allow borrowers to fund their ventures by "drawing on relatively small contributions from a relatively large number of individuals using the internet, without standard financial intermediaries" (Mollick, 2014, p. 2).

Our understanding of how prosocial lenders select their preferred loan candidates on platforms is still limited. Early conceptual work has suggested that lenders are more likely to select borrowers who create non-monetary returns for them (Belleflamme, Lambert, & Schwienbacher, 2014), such as "special feelings" (p. 591) or "community benefits" (p. 586) (e.g., sharing a loan just made on social media). Some empirical studies have suggested that lenders prefer borrowers who use rhetoric evocative of warm-glow (i.e., a special feeling) (Allison et al., 2013), as well as human interest (Allison et al., 2015). However, we still "know relatively little" (Allison et al., 2015, p. 54) about how borrower descriptions influence the decision-making processes of prosocial lenders.

We address this gap in the literature by drawing on signaling theory to assess how prosocial lenders react to borrowers' uses of economic and normative cues in their profile narratives, as illustrated by two constructs: market orientation and positive psychological capital. Signaling theory is concerned with the reduction of information asymmetry between two parties (Spence, 2002), and we contend that economic and normative cues found in loan descriptions serve as costly signals capable of influencing lender decision-making processes. We hypothesize on why lenders may be likely disfavor cues of market orientation, a construct concerned with economic value creation

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(composed of customer orientation, competitor orientation, coordination, long-term focus, and profitability focus); and likely to react positively to cues of positive psychological capital, a construct concerned with normative value creation (i.e., social value) (composed of confidence, hope, optimism, and resilience).

Our contributions are threefold. First, we expand our understanding of the international prosocial crowdfunding phenomenon by distinguishing economic cues from normative cues and considering their effect on the decision-making processes of prosocial lenders. We argue that our findings are consistent with the view that prosocial lenders follow a donations-based logic, as they do not seem to reward cues related to economic objectives nor normative cues unrelated to a current state of hardship. Second, we add two previously unexplored constructs to current literature about the relationship between borrower narratives and lenders on prosocial crowdfunding platforms. Our study finds that every dimension of market orientation and positive psychological capital have a significant relationship with funding time, thus highlighting their importance in the crowdfunding equation. Third, we offer concrete theoretical and practical prescriptions for prosocial lenders and platforms. We argue that a borrower's economic orientation is conducive to a greater positive impact in local communities, as well as to the simultaneous creation of virtuous circles at the platform level, where repaid funds are recirculated more rapidly to other borrowing entrepreneurs in need by prosocial lenders. We therefore advise prosocial lenders to incorporate at least some level of investment-logic in how they select borrowers, and we argue that platforms should make lenders aware of high interest rates charged to entrepreneurs in need by local MFIs. We contend that when prosocial lenders are aware of the interest rates being charged to borrowers, they are better able to assess if a borrower has the adequate economic skills to be able to repay his or her loan—as a default would certainly make both the borrower and the lender worse-off. We view this third contribution of our study as highly consistent with the initial microfinance objective of poverty alleviation.

This study is organized as follows. We first review the literature and present our hypotheses. We test our contentions with Computer-Assisted-Text-Analysis (CATA) methodology and a sample of 130,964 funded microloans in 49 countries from the prosocial crowdfunding platform Kiva. We then present our results, and provide a discussion of our findings and their implications.

2. Literature review

2.1. Microfinance through international crowdfunding platforms

Individuals in emerging nations often rely on entrepreneurship to improve their lives and escape poverty (Bruton et al., 2013). Access to funding is a necessary step for most entrepreneurs (Hellman & Puri, 2000), as liquidity constraints represent a major obstacle to new venture success (Evans & Jovanovic, 1989) which may lead to longer return-on-investment periods, and a heightened risk of venture dissolution (Van Auken, 2002). The problem of accessing necessary capital to start a venture is exacerbated for entrepreneurs in emerging nations, as they rarely have access to forms of financing available in developed nations—such as bank loans, venture capitalists, and angel investors (Berger & Udell, 2003). This is because many financial institutions are reluctant to lend to individuals living in impoverished rural areas, as they may be illiterate or have no collateral (Bruton et al., 2011).

Microfinance has historically represented an important solution for entrepreneurs in emerging nations wishing to access capital to start their ventures. Microfinance is a practice which consists in issuing small uncollaterized micro debt to individuals seeking to start entrepreneurial endeavors, typically in rural areas of emerging nations (Morduch, 1999). Stand-alone microfinance institutions (MFIs) are common organizations that operate locally within specific communities with the goal of providing collateral-free microloans to individuals wishing to engage in entrepreneurship. MFIs can either be non-profit (e.g., FINCA) or for-profit (e.g., Grameen Bank), and often vary in size and focus (e.g., some operate only within a specific area of a given country, some operate across countries, some only lend to specific individuals [such as women borrowers]).

Recently, a new international phenomenon known as prosocial crowdfunding, has impacted the microcredit world significantly, by making new funds available for lending. Crowdfunding is a peer-to-peer platform-based financial technology which allows entrepreneurs to raise funds by "drawing on relatively small contributions from a relatively large number of individuals using the internet, without standard financial intermediaries" (Mollick, 2014: 2). Crowdfunding platforms come under many forms and have different purposes (e.g., equity-based, donations-based, rewards-based, and loan-based; Meyskens & Bird, 2015). The typical prosocial crowdfunding platforms uses a loan-based peer-to-peer lending system, where the borrowing needs of entrepreneurs located in emerging nations are typically met by a wide pool of prosocial lenders located in more affluent regions of the world.

Prosocial crowdfunding platforms are proliferating (e.g., Kiva.org, Zidisha.org, Milaap.org, Lendwithcare.org, Babyloan.org), however, this study's hypotheses will be specifically tested on the Kiva.org platform. Prosocial crowdfunding platforms like Kiva typically partner with small independent local MFIs or pass-through agents located in emerging nations that assist borrowers in elaborating and posting profiles on the platform for external funding (Allison et al., 2013). Once a profile is posted, the peer-to-peer lending process begins, and the borrower loan profile (and its corresponding description) is advertised to prosocial lenders registered on the platform through an open-call. For Kiva (cf. Kiva, 2016a), a loan advertised on the platform has to raise funds in under 30 days. As such, some loans are funded quickly and disbursed only after a few days of fundraising, while other loans do not gather enough funds from the pool of lenders and are canceled (thus triggering a reimbursement of any lender that would have already pledged some funds to this loan). In this study, it is argued that the content of a loan profile description is crucial in influencing the decision-making processes of prosocial lenders. In the next section, we present why specific textual cues embedded within borrower profile descriptions may be capable of influencing the speed at which a loan is funded by prosocial lenders.

2.2. Signaling theory and prosocial crowdfunding

Signaling theory is concerned with the reduction of information asymmetry between two parties (Spence, 2002). Spence (1973) first described signaling theory in an early study of job markets, proposing that the education of a job candidate served as a signal of quality sent to prospective employers in an effort to reduce information asymmetry that exists between a candidate and a company during the selection process. Information about the education of a candidate affects the decision-making processes of an employer, who is likely to interpret education as a signal of candidate quality. Decisions are typically based on two kinds of information: Free publicly available information and private information (Connelly, Certo, Ireland, & Reutzel, 2011). Information asymmetries arise when one party holds private information that could help another party make a decision (Connelly et al., 2011). Signaling theory contends that the release of a private signal by an insider (in the case of an organization, typically an executive or a manager) will influence the decision-making processes of an outsider (Connelly et al., 2011). Many scholars have devoted their scientific careers to the study of information asymmetries, which were ignored for more than a century by formal economic models' assumption of perfect information (Stiglitz, 2002). Michael Spence and Joseph Stiglitz, two scholars who largely contributed to signaling theory, received the 2001 Nobel Prize in economics as a result of their work on information asymmetry.