Objective Necessity, Meaning and Importance of Alternative Financing

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Annotation: The article discusses the nature, purpose and value of alternative financing. A systematic analysis of the mechanism of functioning of the market of alternative financing. Considered types of crowdfunding. Four main types of fundraising chicks and variations of alternative financing models were analyzed.

Key words: alternative financing, financial engineering, project, crowdfunding, donation-based crowdfunding, rewards-based crowdfunding, equity-based crowdfunding, p2p lending

INTRODUCTION

The financing market is a mirror of capitalism. It reflects all the realities of the relationship between financial owners (like shareholders, who want to give money) and those who are looking for financing for their business. Therefore, it is directly related to the stages and forms of this market, its development and the state of market relations in the economy.

Over the past 10-15 years, the words alternative financing, financial engineering, financial innovation, FinTech have been included in the discourse of researchers and practitioners in the financial market.

This is indirect evidence of the rapid development of new financial instruments and technologies of exchange trading, as well as significant technological modernization of the Bank and other financial services. This, in turn, is characterized by two parallel and competing trends:

a) the modernization of activities and formats for the provision of services to existing financial intermediaries;

b) the development of alternative financing and increased demand at a new level.

At the same time, it can be assumed that both trends are associated with the use of social and economic network formats.

ANALYSIS OF REFERENCES

Foreign scientists such as R. Costa, S. Suvorov, J. Howe, I. A. Tyan, P. Bayek, P. Bellefalym, E. Panova, T. Lambert, G. Khmeleva, G. Otlivanskaya, made a great contribution to the development of the scientific concept of crowdfunding.
For example, G. Ottlivanskaya and P. Bellefalym studied in their scientific publications the differences between types of crowdfunding by sorting them [1,3]. P. Bayek's studies contain a very detailed analysis of the mechanism of functioning of the alternative financing market [2]. Having explored the phenomenon of crowdfunding, Costa analyzed the level of sustainable development of crowdfunding and the growing interest of researchers and the public in alternative financing. The end result of this shows that crowdfunding leads to changes in the traditional financial system [4]. The categories of crowdfunding and their use by small businesses have been carefully studied and analyzed by E.A. Panova. The strengths and weaknesses of crowdfunding were identified, and prospects for the development of the crowdfunding market were studied taking into account international experience [5].

METODOLOGY

This article uses comparative and scientific methods of analysis based on logical thinking. The analysis was also carried out in sections, parts and directions using methods of analysis and synthesis. The main focus is on identifying the whole, mechanism and relationships of crowdfunding by dividing it into an object, a certain part, section and direction. In the end, the conclusions and opinions made using the synthesis analysis method were summarized. The goals and objectives of the system were divided into parts and elements, after what the real state of crowdfunding was compared with the whole system. Therefore, the synthesis method in the article is closely related to the concept, purpose and objectives of a scientific article. Taking into account the research of the aforementioned scientists, our article is devoted to the analysis, study and further development of the conceptual, theoretical and practical aspects of crowdfunding market reform in the alternative financial market. At the same time, we tried to give a number of conclusions and suggestions on improving the financial stability of the state by improving the foundations of the alternative financial market.

ANALYSIS AND RESULTS

What is the essence of good alternative financing?

What are the mechanisms and importance of its functioning?

At the same time, we should not forget that alternative financing markets differ from traditional bank financing or capital market financing systems in that there is “eliminate intermediation”, that is, third-party investments between investors and technology-based lenders are involved, which, in turn, it reduces transaction costs and increases the efficiency of the financial market. The alternative financing process is shown in Figure 1. In other words, this process is divided into five stages.
Mechanism of Alternative market financing [2]

Alternative financing makes it possible to directly finance loans to private and institutional investors through alternative financial platforms (next: platforms). For investors, this represents new asset classes. The easiest way to compare a portfolio of corporate bonds, an alternative financing platform is especially useful when lending to individuals and small enterprises. We can analyze an alternative financing mechanism based on Figure 2.

Step 1: Entrepreneurs or startups who want to use an alternative financing mechanism for their projects will place their projects on the platform they want. Analyzing the most successful projects, in turn, we can say that those ones were first of all well and tactfully prepared for the presentation of the project and the planning process.

Step 2: The design of the platform will be considered, studied and reviewed in accordance with the criteria of the platform. Depending on the platform, financing model, and type of work with projects, the verification process varies greatly. Reward-based funding platforms such as Indiegogo and Kickstarter have very few restrictions (with the exception of projects that are legally regulated or potentially dangerous). Other platforms allow only certain types of projects such as video games, fashion, art and social projects.
Step 3: The type of project financing is placed on the selected platforms depending on the purpose. The project description, the purpose of financing, the time frame for the project, the initial cost of the project and the ways of returning to investors (based on Figure 4, it can also be shown the types of financing) will be shown to the public (usually with a short video or image).

Step 4: The process of collecting the necessary funds begins. The time required to finance a project is partly platform dependent and can often be determined by fundraisers. For example, the Kickstarter fundraiser can choose on their own. Funding can last from one to 60 days. If the project reaches its financial goal, the project will receive the collected money and the project will be put into production. In case of failure, the project will not be funded through the platform, and the funds will be returned. Some platforms provide fundraising, even when the project does not reach its financial goal.

Step 5: Using the funds raised, the project will be implemented, and the sponsors will return the promised rewards (money) at the end of the project.

With regard to crowdfunding, it is divided into four types by scientists: donation-based crowdfunding, reward-based crowdfunding, equity-based crowdfunding (equity-based crowdfunding), Credit-based crowdfunding (P2P lending). (Figure 2)

![Types of Crowdfunding](Image)

Figure 2: 4 types of Crowdfunding .[2]

Let’s separate them: donate-based crowdfunding finances social projects of people and no financial income or interest is taken for this. Usually this is an example of a concert program for elephants, which we considered as an example in our foreground.

In reward-based crowdfunding, people participate in projects and receive non-financial rewards or products.

Equity-based crowdfunding is invested in a share of a business and comes income equal to that share.

According to loan-based crowdfunding (P2P Lending), those who wish to take out a loan apply for a loan through an alternative financing platform and publicly finance a small part of the project, and then
benefit from the loan.

Figure 3. Range of crowdfunding models [3]

By analyzing the above, we can divide crowdfunding models into ranges. Each type of crowdfunding is different in terms of motivation and purpose of investors. The aim of investors in crowdfunding models based on collective loans and equity is to obtain economic benefits.

In crowdfunding models, based on rewards and donations, they are guided by the internal and social goals of their investors, and in some cases just a participation in the project is considered as a reward for them (Figure 3).

The functioning mechanism of the alternative financing market (Fig. 1) shows that from the choice of an entrepreneurial platform to the process of project profitability, it is transparent and without any intermediaries. This allows the financing process to be carried out without taking into account bank interest, services, initial payments, in other words, transaction costs, which, in turn, reflects the net cost of a product or service (Figure 4).

According to the chain, financing from banks, corporations, payment funds, investment banks goes through at least 6 processes, and alternative financing provides direct funds to the recipient or recipient through platforms.
Regarding the need and importance of alternative financing, based on A. Chekhov’s phrase “Sister of Intelligence,” let’s take a look at the definitions that world-class publishers like Everest provide for this method.

Fred Wilson, a well-known venture capitalist: "If the Americans invested only 1% of their investment assets in the world of crowd business, they would have an investment flow of 300 billion dollars." - The Economist[9].

“We can achieve the level of revolution in alternative financing for the small business sector. Millions of users of social networks, such as Facebook, can become venture capitalists and help realize valuable business ideas that need money” - The Wall Street Journal[10].

“Shouldn't we encourage such innovations? Unlike exotic derivatives and the most reliable trading algorithms, crowdfunding creates capital to create jobs for small businesses.” - The New York Times[11]

At the same time, according to other experts, the opposite position in the spectrum is the possibility of fraud, hopeless expectations of investors and inexperienced participants in the financial market.

Wil Schroter, Founder and CEO of Fundable Pöple:

“The alternative financing honeymoon is drawing to a close. There is a very big risk associated with investing at an early stage, whether it be a donation or a product, and investors understand that they are not buying a new Amazon”[12].

According to a CNNMoney poll, 84% of 50 Kickstarter-funded projects missed their estimated delivery time. [13]

CONCLUSIONS AND OFFERS

Given the polarized debate about the benefits and risks of alternative financing, it is surprising that the US, the birthplace of crowdfunding, is enacting legislation to develop crowdfunding while financing socially significant and interesting projects.

April 5, 2012, Barack Obama passed the Jobs Act (we will consider this law separately). It was a law for alternative startup financing. This law was intended to allow companies to attract primitive investments in a simplified manner. The new law has attracted the attention of businessmen around the world and is of particular interest to the IT community. [14]

The first step in this area in Uzbekistan is reflected in the measures approved by PR-3832 “On the development of the digital economy in the Republic of Uzbekistan”. In other words, one of the most important tasks for the further development of the digital economy is the introduction and development of technologies, such as crowdfunding finance.

It is clear that the state is also interested in the development of crowdfunding in Uzbekistan. It should be noted that financing this business or idea in this way does not require budgetary allocations and does not increase costs, which is a positive factor in the economy. On the other hand, crowdfunding as one of these alternative financial market instruments is interesting and beneficial for small enterprises - it allows them to raise additional funds.
The essence of the alternative financing market in Uzbekistan can become a catalyst for partial solution of key economic problems. First of all, this concerns the role of infrastructure platforms that provide incentives for projects that need funding, and for those who are looking for investment.

Crowdfunding platforms will help small and medium-sized businesses grow and develop, and the development of alternative financing will help create new jobs and solve the problem of unemployment.

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Jumpstart Our Business Startups Act (JOBS)