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Trust isn't blind: Exploring Visual Investor Cues in Equity Crowdfunding

Short Paper

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Abstract

Overcoming informational uncertainty and financial risk remains a challenge for crowd investors to trust and interact within the equity crowdfunding (ECF) market. Based on the theoretical lens of herding behavior, we demonstrate that visual cues in investor profiles impact the investment decision of subsequent investors. Specifically, this paper provides preliminary evidence on the effect of investor profile images and badges on investment behavior and campaign funding. In a first study, we draw on a dataset of over 30,000 individual investment observations from a leading ECF platform to show that profile images in particular exert positive effects on subsequent investments. Study 2 will build on these findings through a discrete choice experiment. Our results indicate that herding is driven by the perception of credible investors triggered by heuristic cues. Implications for platform operators are discussed in the paper.

Keywords: Equity crowdfunding, herding, trust, visual cues, badges, profile images

Introduction

Crowdfunding changes – some dare saying “democratizes” (e.g. Cumming et al. 2018) – how capital is raised and invested. Rooted in the concept of crowdsourcing and microfinance, crowdfunding allows projects and institutions to get funded by a large base of investors (crowd) online with relatively small individual contributions (Mollick 2014). Typically, a digital platform (i.e., the intermediary) orchestrates the match-making between capital demand and supply by providing the technical and legal infrastructure for financial and informational exchange (Ordanini et al. 2011). While crowdfunding was first launched in the non-profit and art sector in 2006, its descendant *equity crowdfunding* (ECF) entered the entrepreneurial finance market shortly after. ECF is discussed as a viable alternative to traditional seed and startup capital provided by business angels and institutional venture capitalists (Block et al. 2018). In return for their investments, investors acquire the right to participate in a startup’s increase in value, future profits, or exit price (Hornuf and Schwenbacher 2018). However, investing in early-stage companies is connected to high levels of uncertainty and risk, information asymmetries, as well as agency costs (Block et al. 2018). Due to venture capital transactions taking place in an online setting, especially less-experienced investors seem to select from a “lucky bag” of risk and return. Research on ECF aims to build knowledge on how informational uncertainty and financial risk can be overcome. In this respect, *trust*, that is, the willingness to depend on others (McKnight et al. 1998), was found to be the fundament of online transactions (Gefen and Straub 2004). Previous work indicates a lack of trust-building measures in ECF, impeding its wider adoption and the opportunities for capital-seekers (Gerber and Hui 2013). In the attempt to identify determinants of funding success, crowdfunding research to date has mainly focused on project quality signals (e.g. human capital, retained equity, co-investors), and the question *how* projects should present themselves in order to receive funding. Other than project-generated signals, information on previous investments may aid decision-making by indicating popularity or quality of a project. One factor commonly overlooked here is *how, that is, by which elements investors are represented* on the platform.

A growing number of studies illustrates that investors possess the power to impact others' decision to invest (Belleflamme et al. 2015; Vismara 2018). Yet, the underlying decision mechanisms are not well understood. Moreover, research on peer effects and investor decision-making is limited to "hard" content, and neglects "soft" contextual factors such as how personal information on other investors is perceived (see Hoegen et al. 2018 for a review). For each active crowdfunding campaign, the information on *previous* crowd investments is mostly available to all registered users on the platform. Typically, investment information is presented along with personal information such as name (or alias), location, and profile images of the respective investors. Whether and how this information is displayed is not in the hands of project initiators as they cannot affect a) *who* invests and b) *how* these investors are represented on the platform. Rather, the platform operator is responsible, among other services, for maintaining investor profiles. This may include the straightforward idea of enabling investors to upload a profile image (and to prompt them to actually do so) but also more complex means of differentiation such as badges. These represent a user's activity history and may be awarded, for example, to the most engaged, successful, senior, or distinguished investors (Hamari 2013). Similar to the well-established effects of visual cues in other contexts such as in accommodation sharing (i.e., "superhost" badge; Teubner et al. 2016), profile images and badges are likely to facilitate perceptions of credibility and thus trigger a decision heuristic of how persuasive an information is perceived.

Despite their potential economic relevance and trust-building effects, very few studies have considered the impact of visual cues (e.g. project logos, Mahmood et al. 2019) in crowdfunding. With this research project, we hence seek to address the question *how images and badges in investor profiles drive the perception of credibility and how this, in turn, affects campaign funding.*

Theoretical Background and Hypotheses

While project characteristics have long played a central role in ECF research, a growing literature stream has found evidence of various influential phenomena among crowd investors, including a social pattern known as *herding* behavior (Agrawal et al. 2014; Bikhchandani et al. 1992). Just as in traditional financial markets, herding serves as a heuristic or "rule of thumb" and is likely to occur when the activities of others are observable and take place sequentially over a period of time (Bikhchandani et al. 1992; Devenow and Welch 1996). Based on this heuristic, later investors may be led to disregard own knowledge on the investment opportunity at hand, leading to information cascades (Vismara 2018; Vulkan et al. 2016). Recent work highlights that the likelihood of herding largely depends on the timing and size of initial campaign investments (Hornuf and Schwiendbacher 2018). Moreover, disclosing personal details of investors has been shown to drive such behavior (Kim and Viswanathan 2019; Li et al. 2016). Specifically, research indicates that the perceived level of *expertise* of former investors, as for example signaled by investment experience or ability, influences the extent to which other investors, and subsequent investments, follow suit (Kim and Viswanathan 2019). For instance, Moritz et al. (2015) suggest that investors evaluate the expertise of other investors based on the latter's past activities on the platform, such as the size and/or volume of their overall portfolio. This indicates that previous investments, unless hidden, are evaluated by prospective subsequent investors. Thus, investors are *personally* subject to a credibility assessment which, under certain conditions, may be key for facilitating subsequent investors' decision-making.

Research Model

For several decades, research in the fields of social psychology, marketing, and communication has been looking for answers to the mystery of social judgement and the persuasiveness of information. The theory of source credibility has established as a concept used to explain how the characteristics of an information *source* affect the persuasiveness of the information presented (Hovland et al. 1953). According to this theory, an information source *perceived as credible* increases the chances that the information is accepted and/or followed (Ohanian 1990). Credible information go hand in hand with the perceptions of *expertise* and *trustworthiness*, whereby a trustworthy source is perceived as honest or sincere, while an expert source is perceived as being knowledgeable or capable to make valid statements (Ohanian 1990). Practical evidence for the source credibility theory was found both in traditional and computer-mediated communication (Pornpitakpan 2004; Wathen and Burkell 2002). Due to the high density of information on websites, the use of heuristics has become pervasive in order to assess credibility (Metzger et al. 2010). In order to efficiently decide, for instance, which website to trust, any perceivable information that a medium provides

may serve as a cue to assess credibility (Fogg 2003). In particular, the presence of *visual* cues is proven to induce credibility and, in turn, to a greater willingness to engage in online interactions (Sundar 2008).

Dual-process theories provide an attractive framework to explain perceptions of investor credibility triggered by visual cues. Widely used models, including the *heuristic-systematic model* (Chaiken 1987) and the *elaboration likelihood model* of persuasion (Petty and Cacioppo 1986), distinguish between a cognitively effortful (“systematic” or “central”) route and a cognitively effortless (“heuristic” or “peripheral”) route of information processing. This approach predicts that limited ability and/or motivation to apply issue-relevant thinking leads to heuristic decision-making, and vice versa (Petty and Cacioppo 1986). Furthermore, it states that heuristic information processing is cued by accessible information from the decision context (Chaiken 1987). Conceptualized this way, investment information, and moreover personal *investor* information, constitutes such heuristic cues, since it may indirectly serve the investment decision without providing investment-relevant “facts”. According to this theory, assessing investor credibility can thus be defined as a heuristic process whose impact on later investors’ funding decision relies upon the motivation and/or ability of such investors. Figure 1 summarizes these relations. We derive our hypotheses in the following subsections.

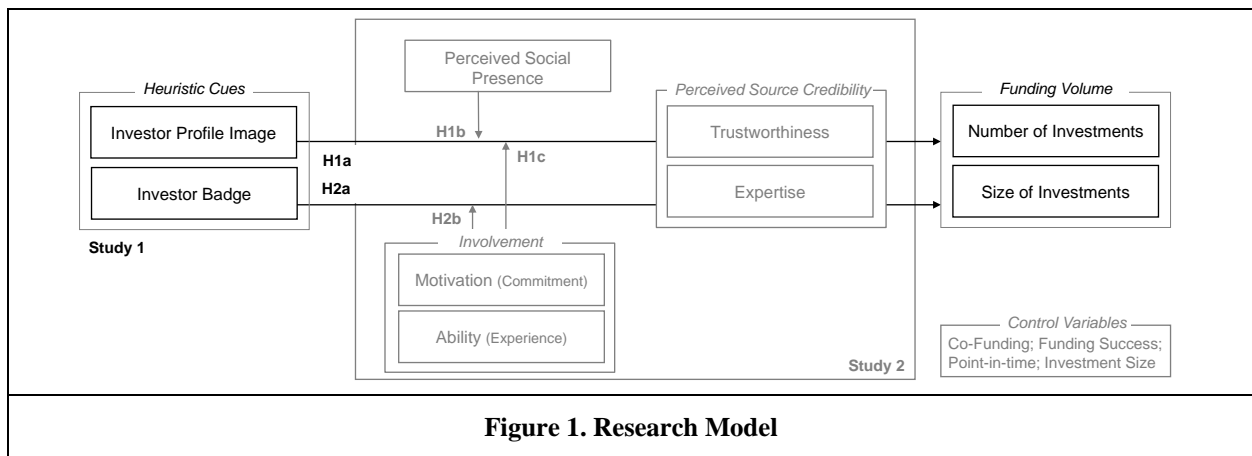


Figure 1. Research Model

Impact of Investor Profile Images

Visual elements, such as images or videos, are widely used on crowdfunding platforms. Findings from the field of marketing illustrate that images (“pictorial stimuli”) play an important role for the persuasiveness of information and the perception of product quality (Miniard et al. 1991). For e-commerce, an extensive literature stream has provided evidence that user profile images in particular can build trust in other market participants and stimulate interactions (e.g. Duarte et al. 2012). Typically, profile images represent the person who owns the profile, either by displaying the face or an avatar automatically assigned to or selected by the person. The profile image provides the ability to identify, recognize, and evaluate other users by inferring personal characteristics such as gender, age, or attractiveness. It can, therefore, result in a positive assessment of previous investors’ credibility by (potential) subsequent investors. This, in turn, would result in increased subsequent funding. Overall, our first hypothesis states:

H1a: *The presence of investor profile images yields an increased volume of follow-up funding.*

Following up on the idea of source credibility, an important factor of enhancing trust online is providing the user with a feeling of *social presence* or the perception of human contact in the absence of face-to-face interaction (Gefen and Straub 2004). We hence hypothesize:

H1b: *The effect of profile images on follow-up funding is positively moderated by social presence.*

Furthermore, we assume that investors with *low* involvement (i.e., low ability and/or motivation), as defined by their financial commitment and investment experience, *positively* respond to profile images. Conversely, investors with high involvement (i.e. high ability and/or motivation) are assumed to ignore or negatively respond to this information. Accordingly, we hypothesize:

H1c: *The effect of profile images on follow-up funding is negatively moderated by involvement.*

Impact of Investor Badges

In addition to profile images, cues generated by the platform system, in particular *badges*, may establish and enhance trust within ECF (see Moritz et al. 2015). On most platforms, badges are automatically awarded to the most active investors (over a period of time) to signal a high level of transaction experience. The badge, thus, relates to membership of an investor status group (see Companisto 2019). As soon as awarded, the badge becomes part of the investor profile, that is eventually visible to peer investors in the case of an investment. Research shows that badges have a great persuasive power, since they allow users to compare their own standing in relation to others (Hamari 2013). Given that investor badges indicate the membership in an exclusive club of “superior” investors, they will most likely be associated with perceptions of high performance, success, and reliability by other members of the community. Accordingly, also highly involved investors might positively respond to them. Our next hypotheses thus state:

H2a: *The presence of investor badges yields an increased volume of follow-up funding.*

H2b: *The effect of badges on follow-up funding is positively moderated by involvement.*

Empirical Data Analysis (Study 1)

In this first study, we set out to empirically investigate how visual investor cues affect subsequent funding. Particularly, the study tests the overall effect from the treatment variables (profile images, badges) to the main dependent variable (follow-up funding) empirically (see Figure 1). Our approach allows us to examine investments at the individual level. To do so, we collected data from a leading German ECF platform specialized in private venture capital for startups and growth companies (*Companisto.com*). Naturally, this approach is limited in terms of uncovering *how* or *why* the artifacts’ effect is conveyed specifically (e.g. via perceptions of source credibility). This step will be subject to *Study 2*. As of April 30, 2019, the platform has attracted 96,000 registered members, supported 119 funding campaigns, and raised a total of 63,000,000€. Using a web crawler to query the platform, we collected openly accessible data for a total of 54 campaigns with between 40 and 2,059 individual investments (31,584 overall) in March 2019. Figure 2 provides a screenshot of a typical project campaign page with several previous investors, their investments, and profile information. Figure 3 displays the share of badges and images and the number of investments at the project-level. The figure reveals a slightly negative correlation between profile images and badges for the respective projects.

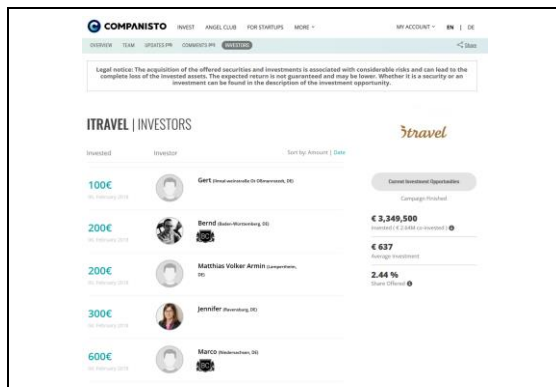


Figure 2. Screenshot (Investors/Investments)

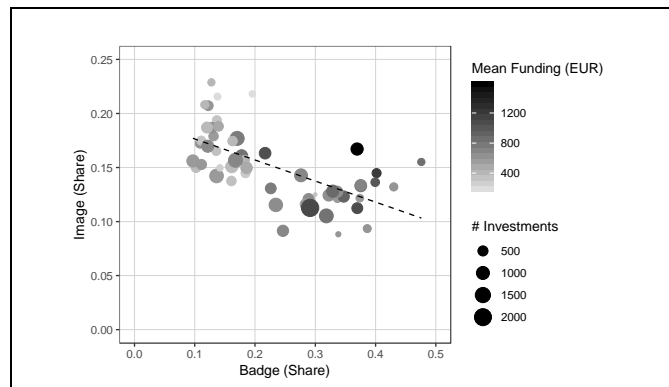


Figure 3. Investments with Badge/Image (Project-level)

The following information was collected for projects: Project name, date and size of the investments, as well as rank, first name (i.e., alias), location, badge (“Business Club”), and profile image of investors; the latter allows us to identify whether the investor has an avatar or a customized profile image (for further analysis). We focus on the amount of funding that occurs *after* an investment made by an investor with profile image and/or badge and compare these values to their direct counterfactuals (i.e., no profile image/badge). This enables us to develop an understanding of how visual investor cues are being used in practice and hence informs the design of our experiment (see *Study 2*).

Until March 2019, the platform awarded the “Business Club” (BC) badge to the most active investors, which is based on the amount and volume of their latest investments, among other factors (Companisto 2019). The badge serves as a *relative* measure of investment activity on the platform. Rather than achieving a pre-set goal, investors must remain active in relation to other users to be in the top ten percent of all users. Since the “BC” badge represents the *current* activity status and we use historic data, some investors may have earned the badge at the time of their investment but have meanwhile lost it. Since this could lead to a distorted picture for long-past projects, we consider projects listed on the platform between January 2016 and March 2019. Moreover, we focus on funding campaigns providing capital for *startups* and *growth companies*, based on the most common contractual type of *subordinated profit-participating loans* in Germany at the time. Moreover, we exclude the platform’s novel “real” equity campaigns, which were introduced after legal deregulation in 2019 and serve as a professional complement to *quasi-equity* financing by “small” investors. In addition, on a campaign-level, we exclude investments made in the first four days, as during this period *only* investors with the “BC” badge were granted access to the project’s “campaign preview” to invest; thus, the investment opportunity was not open to the general public.

For analysis, we consider investments as atomic units. For each investment, there is information available on the *invested amount* (€) as well as on 1) whether the investor uploaded a *profile image* and 2) whether they had the “BC” *badge*. Moreover, we also retrieved timestamps of the individual investment (on day-level) and the precise order in which the investments occurred. We also computed a *normalized time variable*, accounting for the fact that the projects had varying length. This time variable ranges between 0 and 1, where “0” indicates that an investment is made on the very first day of the project campaign and a value of “1” represents the very last day. Overall, the data can be characterized as follows:

- Invested amounts ranged from 5€ to 100,000€ with a median value of 250€ and a mean of 712€,
- 14.5% of all investments were made by investors who had uploaded a profile image, and
- 23.4% of all investments were made by investors who had the “BC” badge.
- Mean invested amounts are 420€ (no cue), 382€ (profile image only), 1,150€ (both badge and profile image), and 1,763€ (badge only),
- Mean follow-up funding (same day) ranged from 5,603€ (no prior cue), 6,769€ (image only), 7,736€ (badge only), and 8,636€ (badge and image) (Figure 4a)

As our main dependent variable, for each individual investment, we consider the *follow-up funding* for different time horizons. Specifically, the follow-up funding is defined as the sum of all investments that occurred *after* the respective investment until a certain point in time (cutoff). We use “end of *same day*” as our main cutoff. Naturally, longer time spans are conceivable, but effects are likely to disperse for higher values. First, both images and badges yield positive overall effects on follow-up funding while there does not seem to occur any interaction between these variables (Figure 4a). Note that the charts look very similar for other cutoff points such as when including the next one or two days. Second, follow-up funding is also driven by the base investment (i.e., how much the represented investors invested themselves), an effect which is specifically pronounced when both cues are present (Figure 4b).

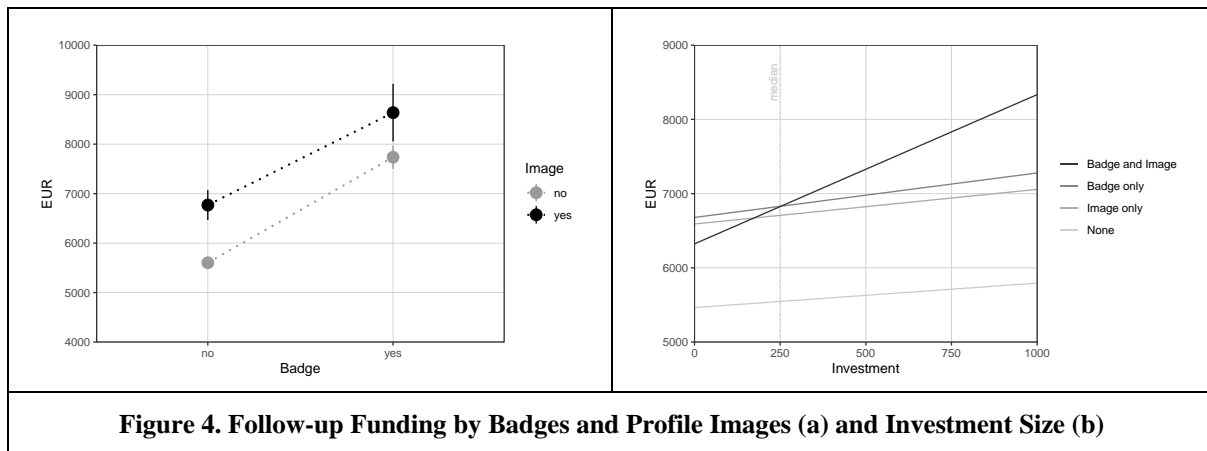


Figure 4. Follow-up Funding by Badges and Profile Images (a) and Investment Size (b)

To assess these first visual impressions statistically, Table 1 summarizes a set of panel regression models for follow-up funding as the dependent variable, using fixed effects to account for project-specific

heterogeneity (i.e., cross-sectional variance). Note again that we obtain very similar results when using “end of next day” as cutoff. As can be seen in Model I, both badges ($b=403.19$; $p<.05$) and profile images ($b=1,098.47$; $p<.001$) are associated with higher follow-up funding. The effect of images also holds when controlling for time and further variables (Model II-V) whereas the effect of badges does not prove robust against these factors. Noteworthy, follow-up funding exhibits a general decrease over time, which is generally consistent with the well-researched dynamics of crowdfunding campaigns (see Hornuf and Schwienbacher 2018). Testing for non-linear time effects shows that this decrease is somewhat dampened towards the end of campaigns. As suggested by Figure 4a, we do not observe a significant direct interaction between badges and profile images (Model III; $b=2.70$, $n.s.$). Also, neither the presence of a badge nor of a profile image is correlated significantly with a user’s invested amount. Now, when controlling for the investment amount itself, we find that higher investments attract follow-up funding (Model IV; $b=.09$; $p<.05$) and that the general effect of images persists. An interesting finding is revealed by Model V, where we control for interactions between the investment amount and the cues (see also Figure 4b). Generally speaking, higher investments trigger higher follow-up funding only when profile images are present (Badge: $-.06$, $n.s.$; Image: $+.50$, $p<.001$), which is mainly driven by the case in which *both* cues are present. Note that we abstain from adding the triple interaction into the regression, as Figure 4b exemplifies this well.

IVs	(I)	(II)	(III)	(IV)	(V)
Profile Image	1,098.47 *** (195.46)	887.77 *** (193.15)	887.05 *** (225.43)	904.85 *** (193.30)	602.82 ** (211.08)
Badge	403.19 * (166.87)	204.23 (164.93)	203.79 (179.37)	93.48 (172.51)	130.64 (186.07)
Time		-6,229.01 *** (219.27)	-6,229.02 *** (219.27)	-6,230.57 *** (219.25)	-6,228.84 *** (219.22)
Badge × Image			2.70 (435.08)		
Investment				.09 * (.04)	.09 (.07)
Inv. × Badge					-.06 (.09)
Inv. × Image					.50 *** (.14)
N	31,584	31,584	31,584	31,584	31,584

Controlling for cumulative funding shows that there is a negative and significant effect of this variable and that it does not alter the main coefficients (profile images, badges) in terms of magnitude, sign, or significance. Using log-transformed values for follow-up funding shows similar results where here, also the badge coefficients in models II and III become positive and significant.

Online Experiment Design (Study 2)

The purpose of our second study is to explore how participants respond to visual cues in investor profiles regarding perceived source credibility and the individual decision to invest in ECF projects. In order to do so, we set out to conduct a discrete choice experiment in which participants choose to invest in one out of two investment projects, applying a 2×2 design with the independent variables *badge* and *profile image*.

Sample — Participants will be recruited in cooperation with a partner platform through a link to the experiment on their website. In addition, registered platform users will be invited to participate via the platform’s newsletter. Since participants are sampled from this pool of registered users, they are familiar with ECF and hence represent a highly suited sample. To further encourage participation, invitees are offered a monetary reward in form of an investment voucher to be raffled among the participants and summary of the results.

Task — Two (hypothetical) investment opportunities are presented to participants, which resemble actual ECF projects in graphical and textual terms and have similar probabilities of successful funding (Figure 5). The project overview includes the following elements: textual (short) description, title image, funding goal,

current status of funding, remaining campaign time, and number of investors. In addition, the most recent five investments are displayed along with the (hypothetical) investors. This representation is varied at random, where we focus on *profile images* and *badges*. There are two different scenarios for each variable (i.e., “high”=3 and “low”=0 number of badges and/or images). This yields four different constellations per project and hence 16 treatment constellations overall. All other factors such as investor gender, names and investment amounts are varied randomly, similar to the actual distribution of what we empirically observe on the platform examined in *Study 1*. For profile images we will use stock material. For investor names, we will draw on common first names. After having decided for one project, participants are asked to invest any amount of their virtual budget of 1,000€ into this project, starting from the minimum investment amount (250€). To account for the high level of risk related to venture capital, we randomly assign the participant’s return on investment, where total loss of invested capital is the lower bottom, and tripling the invested amount is the top. Participants’ overall outcome (i.e., 1,000€ – investment + return) will be converted into lottery tickets for the price draw. To create incentives for “reasonable” investment decisions, participants are instructed to judge the probability of project success based on the provided project information.

Measures — After completing the discrete choice and investment tasks, participants will be surveyed on a range of constructs as outlined in Figure 1, including perceived social presence (adapted from Xu 2014), source credibility (adapted from Bhattacharjee and Sanford 2006), and involvement (adapted from Zaichkowsky 1994). All constructs will be operationalized by established items, measured on standard Likert scales. Importantly, beyond these self-reported (rather tentative) measures, we will also be able to draw on their project choices and investment decisions, representing more reliable behavioral measures as these will be directly linked to participants’ expected payoffs. Control variables include manipulation checks, trusting disposition (adapted from Gefen and Straub 2004), as well as basic demographic information.

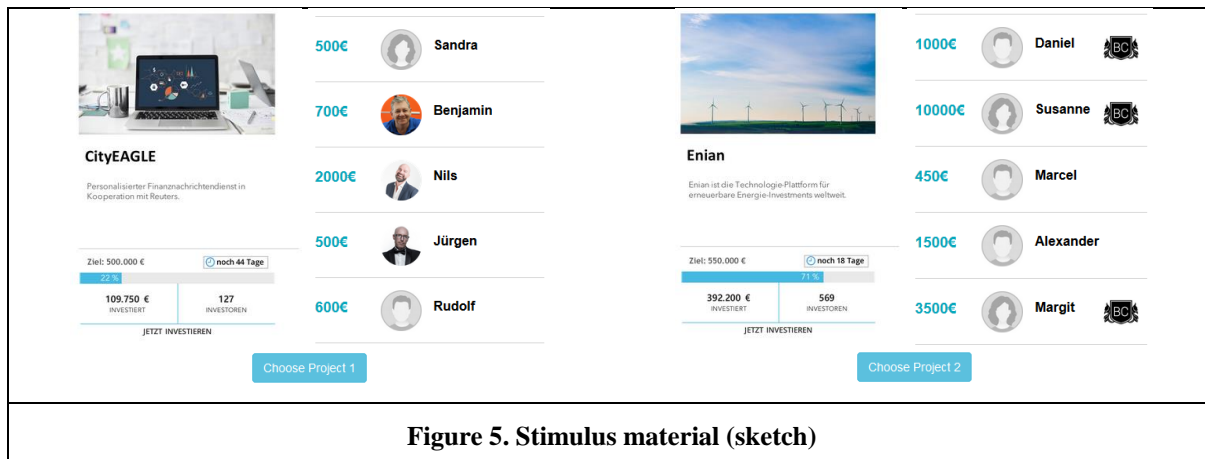


Figure 5. Stimulus material (sketch)

Discussion and Implications

Limitations and Suggestions for Further Research

With this paper, we set out to explore visual cues in investor profiles to understand how information on earlier investments impact subsequent investors’ decision-making. We contended that earlier investors impact the decision of later investors to financially engage in a project, based on how credible they are perceived. We furthermore argue that the persuasiveness of listed investments is induced by images and badges in the respective investor profile. Aiming for a multi-study approach, we tested the overall “end-to-end” effects of our main research hypotheses and found marked empirical support. Specifically, *Study 1* used field data from a leading German ECF platform to investigate the impact of profile images and badges on subsequent investments. We are able to show that, while controlling for investment timing and size effects, profile images (H1a) exert positive effects on subsequent funding while badges do not (H2a). In line with previous work (Wallmeroth 2019), we find that profile images are used by a small proportion of investors who contribute relatively small amounts. Although previous work states that investor profile images are uploaded for emotional reasons (Wallmeroth 2019), our results indicate that they are also of significant economic impact.

Our work extends existing studies on herding behavior in ECF that focus mainly on identity information and indicators of investor expertise, as for example work experience (e.g. Kim and Viswanathan 2019; Vismara 2018). In addition, we contribute a first *investor-centered* study to the crowdfunding literature on visual cues. However, the findings of *Study 1* must be interpreted with caution. There is no conclusive evidence of the underlying causal effects between visual cues and subsequent funding. We cannot rule out the possibility that, for instance, investors on the platform knew each other at the time of investment, nor can we ensure that later investors paid attention to the profiles of their predecessors. In addition, we did not control for confounding effects resulting from other available investor information (e.g. location, other badges), or different perceptions of images (e.g. quality, attractiveness, face visibility and emotionality). To address these concerns and extend the findings of *Study 1*, we plan to conduct a controlled experimental study (*Study 2*) in which the credibility assessments are combined with incentivized investment decisions. This will allow us to document the mechanisms underlying the effects of visual cues on perceptions and investment decision-making. For future work in this field, we consider drawing on *cue diagnosticity* (Purohit and Srivastava 2001) as an alternative theoretical framework, well-suited to examine the interaction effects between *multiple* cues. The effect of visual cues on funding already extends scholarly understanding of crowdfunding dynamics, as in related fields of digital finance.

Practical Implications for Platforms

On crowdfunding platforms, images represent a pervasive type of cues of high persuasive power. However, platform operators have so far applied a trial-and-error approach to user interface design and user representation, taking little to no account of the dynamics resulting from these (missed) decisions. Whether investors are represented with a personalized (facial) image, and whether their participation is incentivized with badges are examples of questions that platform operators need to address. By systematically integrating gamification and personalization elements, platforms possess a powerful means to drive campaign funding success, improve user experience, and build trust in an otherwise and notoriously high-risk environment.

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