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# Venture Capital In Saudi Arabia

## Venture capital and efficient business development

In the United States of America, venture capital activity began in the 1950s in response to the financing needs of small and medium-sized enterprises, relying on new technology, particularly in the computer and electronics and information technology industries, relying on ideas that are not worth anything, regardless of how important and valuable investment and economic developments were.

It is a wide range of private equity sub-categories that refers to making an investment in stocks for early development or expansion of business activity, usually in small businesses. New technology, new marketing concepts and new products that have not been verified are being introduced in risky investments. Objectives of venture capital to finance research and development for new projects or new techniques before the start of an active useful life and to finance the creation of new projects (fixed capital-working capital) and where adequate financial resources are not available to investors

Considered venture capital financing provided by investors to start-ups and small businesses that is considered to have the possibility of long-term growth, and generally venture capital, usually from high-level investors or from any other financial institution, however, is not always monetary, but can be formed in the form of technical expertise or management. Although it may be risky for investors who put up funds, the potential returns above average are the attractive reward, for companies and new projects that have a history of running a limited (less than two years) and have become the risk of capital financing is common and capital increases are increasingly necessary, especially if they are unable to access capital markets or bank loans or debt.

Fundamentally venture capital differs from the credit or loan where, in the first case, the creditor is entitled to claim his money regardless of the company's status or financial stability, whereas the investor in venture capital receives the investment in the company and receives a share thereof, thus relying entirely on the project's growth and its ability to achieve it.

Since venture capital is turned into investing larger sums of dollars in a smaller number of companies, the background of the business research is extremely important, as most of the venture capital experts they have previous experience with the investment, often like local research, property rights, and others are graduating in business administration, as well as characterizing expert risk management. Once you have completed the procedures to meet the requirements, the company or investor will learn how to invest capital in exchange for the company's ownership rights and that these funds are provided once, but typically provide capital in stages, and then take the company or the investor as an active part as possible in the company, watching their progress before releasing additional capital.

Most corporate foundations think their ideas are astonishing and worth financing. The fact is that most ideas deserve some kind of funding, not necessarily venture capital. Different firms have different possibilities, so the amount of logical capital to invest in them varies. If the

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business is small as such, a bank loan can be obtained, but no financing is bold in this case because the potential increase in the value of the financial upside is usually a few.

## **Venture capital activity**

Various types of venture capital activities include:

- A. Providing financial support, technical and administrative projects showing that these institutions can be divided into two main types by high risk and potential growth and profitability:
  - a) Independent institutions that raise capital from potential investors, depending on their fame, specialization and experience.
  - b) Subsidiary institutions are branches of financial institutions that set them up and provide them with the capital they need.
- B. Taking care in trouble of new high-risk projects and existing ones.
- C. Financing investment projects with a high-risk profile but with high potential prospects for growth.
- D. Participation in the plan's projects by providing financial, technical or administrative support, even if the best project was entitled to high-return venture capital from the Company to sell its share of a profit commensurate with the degree of risk.

## **Venture capital companies and the banking system**

The banking system usually benefits in many ways from the establishment of venture capital firms. Benefit of the banking system generally by setting up venture capital companies from several main aspects to help banks dismiss their buyers by providing them with additional financial resources where banks (in some cases) are unable to lend or contribute to projects because of the constraints imposed by banking systems.

Also financing the application of new innovations to the software industry, and is no longer attractive to banks either because of the high level of risk or lack of financial capacity, safeguards for project owners, and then requires an innovative application to help venture capital companies, in case of success, banks can access free financing for these projects and afterwards.

It provides complex technical and administrative work for banks where the banks have the means to provide this aid and, in addition to financing small projects which have the potential for growth and development while lacking adequate guarantees to borrow from the banking system, the device can then bank into the financing of these projects at a later stage. Venture capital helps restructure the companies of the public enterprise sector if they are included in the privatization program that leads to their repositioning and repayment of their debt to the banks.

Lastly, traditional means are not in line with the needs and objectives of small and medium-sized enterprises (SMEs) with the development and transformation of the small and medium-sized enterprise sector. For their advantages and speed of procedures and facilities, the latter are oriented towards innovative alternatives. Capital risk financing is the optimal variant, which is in line with the characteristics of small and medium-sized enterprises, considered to be capital risk financing, new technology for small and medium-sized enterprises.

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Many large investors started investing in the early stages of start-ups and promising companies to lower their competition with small investors, who were the first to take the lead, although the risk is higher. However, the factors that mitigate their investment risks over time must be identified by these investors. In the advanced stages of expanding and increasing the growth of the company, large investors can invest in companies. Overall, the obstacles they face for the large investments they can make through these businesses can be overlooked by small capitalists. In addition, traditional investors are not at risk for traditional or pre-existing investments. Because risk can be a deterrent to investors of this type, seeing investors and others at major risks is achieving profits and returns.

## **The stages and roles of venture capital financing**

First one is first seed funding, and it is when a small investment of at most a few hundred thousand euros allows the regulator to check whether the project is economically attractive. Venture capital helps to explore the project's feasibility at this stage. Then it is the startup financing which is the investment used to operate the company by attracting the necessary staff and executives, developing a prototype and / or implementing marketing tests. At this stage, the capitalist may participate in organizing the company. And its contribution to the formation of corporate strategy is strongly concrete at this stage. The third one is expansionary financing which is the investment that aimed at manufacturing, upgrading production facilities and attracting more staff. Venture capital can help find additional funding at this stage and help the company connect with customers and suppliers. It can also help recruit marketing staff and other non-technical executives as the company grows and its revenue needs. Lastly is the later finance which is the investment that is aimed at helping the company grow fast enough to become a market leader and unleash its earning potential and make it ready to trade, sell or list. Venture capital can help pave the way for an initial sale or public offering at this stage

## **Saudi Market and opportunities**

The Saudi Arabia market is mainly characterized by the small company sizes in the stock exchange (refer to figure 1) as well in sense of startups, according to the SME Saudi Authority, Saudi Arabia's private sector is generally comprised 99% of the SMEs. This forms a great deal of opportunities for PE investors, as well the great potential development of both the entrepreneur, the investor, the economy as well. As the vision is oriented to diversify away from the public sector and revive the private sector that is formed by 99% SMEs equaling a great deal of growth potential. With such alignment and support lent by the government it is inevitable that these small scoped businesses and startups will witness a great deal of expansion, with the strong governmental decisions to rectify the courses of economy and by implementing aggressive policy that is aimed to increase the transparency and the investors confidence, makes such investments and such market to any venture capitalists in Saudi Arabia attractive.

## **Saudi Development Plan**

The latest development plan, the ninth development plan of the Kingdom of Saudi Arabia (2010-2014), is an expenditure initiative worthy of SR1, 444bn (\$ 385.2bn) to achieve average annual GDP growth of 5.2 %. It is expected that GDP growth will lead to an increase in gross domestic product and per capita income from SR 46, 200 (\$ 12bn) in 2009 to around SR 53, 200 (\$ 14bn) in 2014.

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The primary contributor to this growth will be the non-oil private sector, which the government expects to grow by an average of 6.6 percent per annum over 5 years from 48 percent to 61 percent. The SR137 allocated \$6 billion (\$ 36.7 billion) for the development of human resources and SR9bn (\$ 2.4 billion) for the development of education. These spending plans include building community colleges and more institutes for vocational training, as well as setting up additional public schools and technology facilities. These types of spending initiatives will ensure that a highly skilled and motivated Saudi workforce will be available in the future; however, more focused projects still need to be organized.

Other plan sectors can provide the best catalyst for Saudi Arabia's future project development. These include services related to social and health, economic resources, transportation and communications, and municipal and housing services. One example of Saudi Arabia's new business concept is the large family cultural heritage units living in the same home and healthcare sector improvements. With the beginning of the generation that initially benefited from the discovery of oil in the age of new business opportunities in the form of health care services will be established within the Kingdom. Innovators can take advantage of this opportunity by creating health services businesses that meet their own requirements and provide medical care to them. These types of health care include home health programs, retirement and auxiliary living facilities, as well as the supply and medical devices companies that will be expected to serve them.

The Saudi government has taken steps to decentralize the economy using positive examples of Western capitalism and, as a result, entrepreneurship has begun to form within the Kingdom. The number of recognized trademarks in Saudi Arabia can show evidence of this transformation. Franchising has grown tremendously over the past five years and many brand names are already well-established on the market. According to industry sources, fast food franchises already account for more than 60% of the total Saudi franchise market. American companies have a lion share with more than 70% of all Saudi Arabia franchised operations from fast food, clothing outlets, hotels, car rental, laundry and printing services.

While private business ownership is not new to the Kingdom, it has mainly focused on granting franchises so far. This resulted in a broadly diversified economy that does not contribute to the achievement of the Ninth Development Plan's objectives-sustainability through economic diversification. Thus, the main engine of economic diversification must be real innovation in the form of entrepreneurship. The use of natural hot climates in Saudi Arabia to operate a desalination plant is an example of innovation. For Science and Technology, King Abdul Aziz City is currently building Khafji, Saudi Arabia's largest desalination plant in the world.

Once the plant is completed, a new type of concentrated solar photovoltaic technology and new technology for water purification developed jointly by IBM and IBM will be used. Once the plant is completed, it will produce 30,000 cubic meters of desalinated water per day, meeting the needs of 100,000 people. This example shows how real entrepreneurship eventually reduces the need for importation while producing a product/service by using new technology that can be exported to other countries one day.

## **Saudi Government Venture Capital**

Saudi Arabia's government sees entrepreneurship as a single solution for diversifying its

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economy, reducing its rate of unemployment, and promoting economic growth. To date, oil accounts for approximately 80% of the economy of Saudi Arabia. Saudi Arabia has implemented a five-year development plan (2010-2015) to overcome the economy's shortfall.

Part of this plan is the initiative to spend US\$ 385.2 billion in various industries ranging from communications, health, housing, and transportation, resulting in an economy experiencing a 5.2 percent growth rate during the current plan if successfully implemented. Further information is included in the literature review on this five-year development plan.

In order to help realize the fruits of the plan, the Government of Saudi Arabia has established a number of funding agencies, including GVC, through various government agencies and companies, to help set up environmentally friendly projects in the Kingdom.

In their social context, entrepreneurs work. And Saudi Arabia's search for GVC as the primary source of finance is dedicated to exploring GVC funding decisions through theoretical social capital to better understand the GVC decision-making process in Saudi Arabia. Figure below denotes the volume of governmental support and inclusion in plans through the public investment funds.

## **Venture capital industry in Saudi Arabia**

In addition for government agencies that play an important role in venture capital, there is also an important and effective role for the private sector in this area. Among the most important of these institutions is the STC Ventures (STC Ventures' Fund): the company STC Ventures is a venture capital fund specializing in start-ups and small and medium-sized enterprises working in the field of information and communication technology in the Saudi Arabia and Middle East markets as well as in other international markets.

Another participant is The Saudi Aramco Entrepreneurship Center (Promising) (Wa'ed, Aramco's Entrepreneurship Arm) and it is a venture capital company's 'Promising Ventures' arm, Saudi Aramco Entrepreneurship, set up by Saudi Aramco to ignite the spirit of entrepreneurship in Saudi Arabia's Kingdom. Over the years, a promising set of programs has been released to help entrepreneurs set up, strengthen or expand their businesses.

These programs include development and financial support, including business incubation, training and training to guide and nurture entrepreneurs, seed funding and unsecured loans, and investment in venture capital (equity / debt), and supporting these programs in the development of small and medium-sized enterprises (SMEs) capable of locating and diversifying industries. Wa'ed also works with key players to create an effective environmental entrepreneurial system and interacts with them. Also Saudi Aramco Energy Venture is It is a subsidiary of Saudi Aramco, the leading energy and integrated chemicals company in the world. Its mission is to invest globally in growth companies building high-growth technology of strategically important to Saudi Aramco, to accelerate their growth and dissemination in the Kingdom of Saudi Arabia.' The company invests in the oil, gas, oil, petrochemicals, renewable energy, energy consumption and water sectors.

SABIC Ventures help innovative businesses and explore opportunities for development with them to help them accelerate their growth while building value for SAPK. Sabak vancher is

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looking for entrepreneurs with innovations in alternative energy, technology of raw materials, advanced materials, processing, energy efficiency and resources. Bellow figure illustrates the forecasts by jadwa investment on the growth of SMes by 2030.

## **Saudi venture capital investments**

Last year was the start of the recovery of investment in the venture capital of the kingdom in emerging businesses. A few pages of recent venture capital investment in the Saudi market company has been Foodics ' emerging \$4 million investment size, and investors are leading ventures, fund wind technology, and 500 startups. Another emerging company, Paytabs, was an undeclared company investing \$20 million. Another shop ideas for investing \$2 billion in fund wind technology is a small company. In 2018, according to Saudi Aramco's latest investment proposal, the National Oil Company in Saudi Arabia is exploring the establishment of a \$1 million venture capital fund to invest in global tech companies, with the Kingdom's attempts to expand its economy intensifying. Weighing Saudi Arabia's oil company fund invests millions of dollars in technologies that supplement the oil giant's activities also plans to open a Silicon Valley office or anywhere else in the U.S. to infer an agreement.

Aramco's funding is in the field of high-growth oil and gas companies startups, the \$ 500 million Saudi energy projects, and the Aramco Entrepreneurship Center, which has about \$ 200 million to implement equity to the individuals of Saudi Arabia during the first phase.

In 2015, the Islamic University for Finance industry Development (ICD), the Islamic Development Bank (IDB) of the private sector, along with Anfal Capital on setting up a venture capital fund in Saudi Arabia. The joint venture aims to foster the growth of Saudi Arabia's local venture capital market. The project is leveraging latest technology from the university.

The Loan program will seek creative and innovative venture capital prospects and will provide the intelligent and practical capital necessary to start and maintain these enterprises. The investment strategy of the Loan program is about making an investment in quality teams and advanced product lines and technologies. It will partner with experienced, vision and credibility startups and seek to recruit the best human capital to portfolio companies. Venture capital has been deemed to be the most effective tool for identifying new technologies, taking advantage of entrepreneurship, funding and starting new industries. Small medium-sized businesses run by Kingdom entrepreneurs are said to make a contribution less than 20 percent of the national economy, while technologopreneurs ' share is likely to be much narrower. this percentage can be as high as 60 to 70 percent in other developed and industrialized countries. therefore to diversify the country's economic base and labor market this untapped potential that exists within the kingdom should be supported and developed. at Anfal capital we are honored to work towards this noble cause together with two leading institutions in this field.

## **Venture capitalists & financing means**

In the light of the attractive investment opportunities that the SMEs offer, along with the governmental support, the creation of "Munshaat" has paved the way for these ventures to grow and prosper, where munshaat is can be viewed as a governmental venture capital firm working as a hub, connecting venture capital backed companies with venture capital investors.

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Eager venture capitalists can utilize munshaat as an idea origination pool, where main VCI

- ARZAN Venture Capital
- BIAC business incubators and accelerators company
- Saudi Aramco
- Wamda Capital
- Wadi Jeddah Ventures
- Oqal
- Wadi Makka ventures
- Manafa financials

All playing a big role in one of the three investment opportunity program that munchaat is providing for these VCIs via the aggressive capital governmental fund initiative.

Munshaat is soon to offer fund investment program, and cooperative investment program, that will ultimately benefit both the Venture capital-backed companies and the venture capital investors that are looking for investments.

## **Venture capital and Islamic finance**

Islamic finance has been characterized by a variety of financing forms because Islamic financing assets are due to Al-Hassan loans, Murabaha, Istisna'a, participation, Salam, and Ijarah. The closer forms of venture capital financing are the joint contract, which consists of the Mudaraba contract in Islamic jurisprudence, where the project was financed by the financial institution and the owner of the innovation is working.

By looking at one the Islamic financial institutions market, we find that financing through Mudaraba contract is weak in non-existent projects and the level of risk lower than the draft of the new innovations, but we find that the issue of support through venture capital may be weak due to the size of the risk. Therefore, Islamic financial institutions may not be the best option to finance such projects in most of their current forms. Such projects may require government support, whether through a settlement bank or the Industrial Development Fund, but should be done through Hassan or Musharaka's loan. The truth is that it is not appropriate to have the option is a Hassan loan, because the likelihood that these projects will be successful is somewhat weak, but one's success may cover the costs of previous projects and therefore the Mudaraba contract is the best option.

## **Conclusion**

Of course, no more risky investment in money is a high-risk investment, associated with a promising investment in the fields of active and profitable investment, and this means that investor companies do not file support investment decisions, as this sector investor also has no data series for a long time, making investment decisions more secure, especially in the face of responsible governance. But the challenge of resolving this issue is a real opportunity, and the acquisition of 'cream' is proof that it is difficult to refute the importance of such investment and its ability to raise equity in the short term, has a good communication company when it establishes a separate fund for this purpose, providing the fund with its flexibility and readability advantage.

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Funds provided by the investment funds bold can deal with the industry even before it is on the table, when the capital increase was first launched, the funds provided the basic startup amounts. Thus, these funds can give corporate money to the revolution's most promising investment that has achieved significant value growth. Although investment in venture capital has accelerated in the kingdom, it is still early. It will take years more than acceleration to catch up with what capital investment in the kingdom can be.

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