Competitiveness from innovation, not inheritance

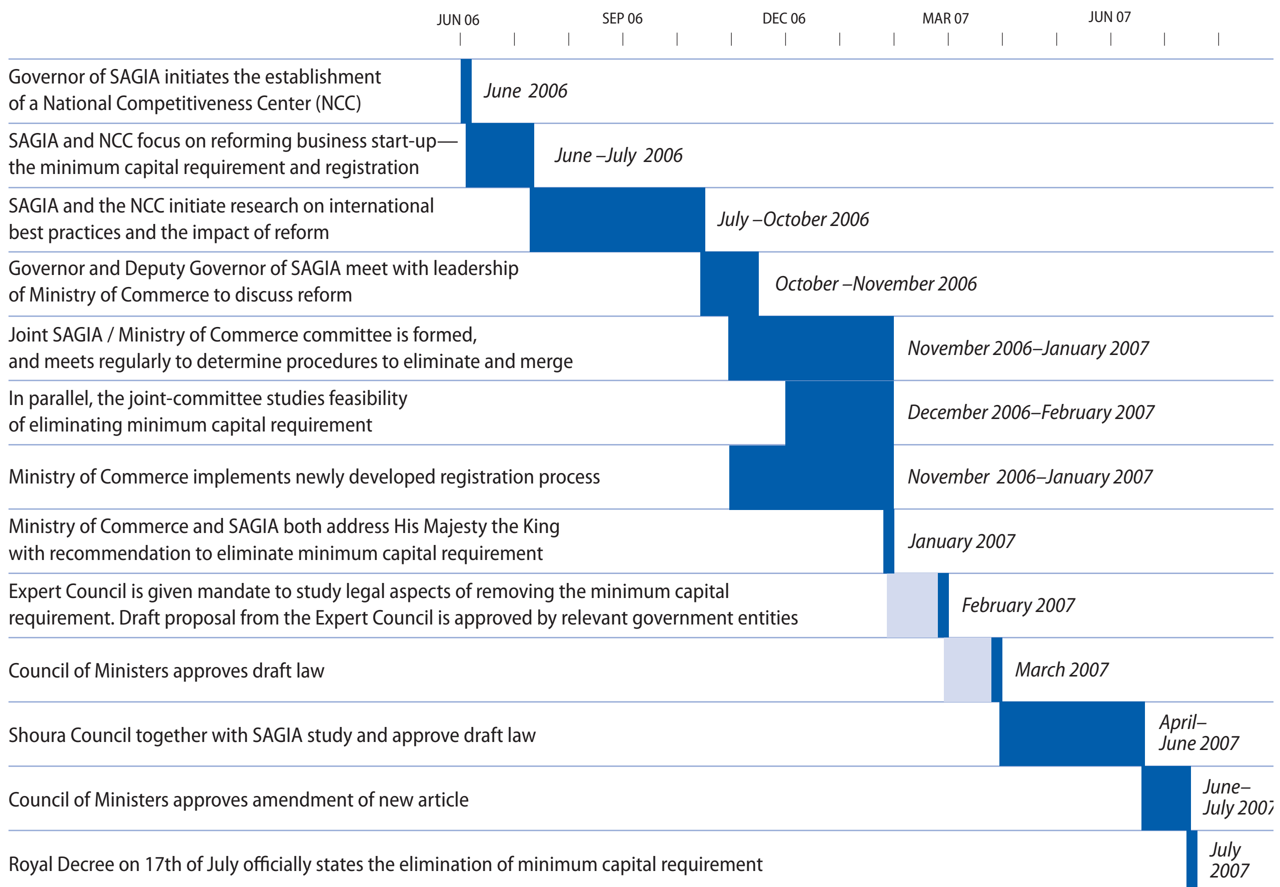
Karim Ouled Belayachi and Jamal Ibrahim Haidar

Starting a business in Saudi Arabia used to be limited to those who could afford one of the highest minimum capital requirements in the world—$125,000 for limited liability companies. In July 2007 Saudi Arabia slashed the minimum capital requirement and simplified business startup procedures. What once required 13 procedures now takes only 7. The time to start a business fell from 39 days in 2006 to only 15 in 2007. According to *Doing Business*, the country's ease of starting a business ranking soared from 159 in 2007 to 36 in 2008.

The need to transform the Saudi economy was clear—from one based on inherited wealth to one based on innovation. The oil sector makes up more than half the gross domestic product (GDP) but employs only 2% of the workforce. Even if oil maintained its high price, the sector would not generate the new jobs

FIGURE 1
Timeline of business start-up reform in Saudi Arabia

Source: Doing Business database.



to satisfy the growing workforce. The country's population is young, with 49% younger than 20, and a large share will soon enter the labor market. That could fan unemployment.

How to reform fast? Political commitment

After seeing that the country was not the best in the Middle East and North Africa region and compared poorly with the rest of the world, King Abdullah of Saudi Arabia said in 2006, "I want Saudi Arabia to be among the top 10 countries in *Doing Business* in 2010. No Middle Eastern country should have a better investment climate by 2007." This drove the creation of the 10 by 10 Initiative, with a goal to place Saudi Arabia among the 10 most competitive economies by 2010. The political structure of Saudi Arabia made it possible to start the reform right away.

Saudi Arabia's reforms began in 2003, spurred by a desire to join the World Trade Organization. The agency responsible, the Saudi Arabia Government Investment Authority (SAGIA), improved Saudi Arabia's investor rights and protections in 2003 and enhanced its competitiveness with accession to the World Trade Organization in 2005. But the $125,000 minimum paid-in capital requirement put Saudi Arabia among the lowest 20 countries in *Doing Business*'s starting a business indicator in 2006. After the success in 2003–05 SAGIA executives got direct responsibility for reforming the business entry process to encourage domestic investment.

First, they realigned their agency's mission statement to become "to position Saudi Arabia among the top 10 most competitive economies in the world by 2010 through the creation of a pro-business environment, a knowledge-based society, and by developing world-class economic cities to enhance economic development across the country." Public advertisements seek to include every citizen in that mission.

To analyze performance and promote improvements, the National Competitiveness Center created benchmarks aimed at remodeling the business entry process and rubbing out its rough bureaucratic edges. It used *Doing Business*'s "starting a business" methodology to measure results.

Collaboration, teamwork, and leadership were key to the reform's success. SAGIA's governor, Amr Dabbagh, and deputy governor, Awwad Al-Awwad, spearheaded the reform program because of their backgrounds. Dabbagh brought extensive private sector experience—he was a former chief executive of the Dabbagh Group, with previous work in telecommunications, media and technology, energy, and other major industries. Al-Awwad brought public sector experience,

as an official across several government entities. Together, they proved invaluable in lobbying private and public stakeholders to support change.

An outside agency, SAGIA was not directly responsible for business registration. Its board of directors included representatives from each ministry and 2 members from the private sector nominated by SAGIA's governor. Their diagnosis: entrepreneurial activity in Saudi Arabia was limited, mainly because the process to start a business was long, costly, and required a high minimum capital. The complex business entry process stifled entrepreneurship and innovation. Unlike in other rich countries, small and medium-size businesses did not contribute much to GDP.

Facing opposition

The main arguments for keeping a minimum capital were protecting creditors and protecting companies against insolvency. The argument was not based on specific events, but on a larger view of what would be best for the country.

From November 2006 through January 2007 SAGIA tailored business cases to address these arguments. Their point: a minimum capital requirement made little sense because capital structure depends on a firm's operations and because creditors are protected by the mark-up in asset values.

The reformers challenged their detractors: If a high minimum capital requirement is good, why don't the rich countries require such large amounts? Why does economic informality spread in parallel with the required minimum capital? Why would a company that designs software have the same capital as a highly leveraged company that transports radioactive waste? If capital requirements reflect creditor risks, shouldn't they differ across sectors? SAGIA also benefited from internal *Doing Business* research that showed that minimum paid-in capital does not prevent bankruptcy.

What gets measured gets done

After the announcement of the 10-by-10 Initiative, SAGIA set up a system of key benchmarks, with targets for each year based on an aggressive goal to be among the top 10 countries by 2010. The goal was not only to improve, but to improve compared with others. So, international benchmarks were the targets. The end-of-year bonuses of SAGIA's executive staff depended on achieving or surpassing an overall *Doing Business* rank below 40 in 2006, 30 in 2007, 25 in 2008, 15 in 2009, and 10 in 2010.

SAGIA reported its progress directly to King Abdullah, every quarter. The king wanted briefings on successful collaborations with other ministries—and on the obstacles SAGIA encountered. The system made everyone accountable to the highest levels of government, creating an urgency and sense of responsibility. In 2006 the team missed the annual target, so it faced significant political pressure to make sturdy progress the next year.

The reforms encompassed many agencies and departments outside SAGIA. So, for every significant step forward, SAGIA used a media campaign to thank the relevant ministries or departments, with television spots, newspaper announcements, and awards ceremonies. “It is important to let people know that everyone is part of the 10-by-10 Initiative and that everyone is a winner,” says Al-Awwad.

Quick wins to create momentum

Major legal changes do not happen quickly. To re-engineer business registration, SAGIA created momentum by advocating for smaller, simpler reforms. Eliminating the minimum capital would have to wait for later. The reformers identified quick reforms—procedures with little function that could be easily eliminated without objection from the entity that administered them.

An example was the procedure that required the Chamber of Commerce to stamp the company books. The procedure served no real purpose, and the Chamber of Commerce agreed to eliminate it. Also reformed were steps that could be merged together.

In the old registration process the company name and a summary of the articles of association were submitted separately for publication in the Official Gazette. No rationale other than historical protocol justified the separate submissions. The Ministry of Commerce was thus open to a single submission. Technocrats from SAGIA and the Ministry of Commerce implemented the reforms. These quick reforms brought momentum that made it easier for SAGIA to advocate more challenging reforms, such as reducing costs for business registration. The General Organization of Social Insurance’s plans computerize its registration procedure and go online further streamlined and simplified business startup.

Meetings at the ministerial or deputy levels became the basis for memorandums of understanding between the organizations—to formalize the agreed reforms. These became a reference point to create pressure and ensure commitment.

Piggybacking? Only if it works

Navigating government agencies was a challenge, but it built understanding of how to promote reforms. Legislative reforms required much more creativity. Discovering that the Ministry of Commerce had already drafted a new Companies Law, SAGIA "piggy-backed" on the new law and received the ministry's support to add Article 164, eliminating the minimum capital requirement.

From January to May 2007 the Ministry of Commerce and the governor of SAGIA lobbied the Supreme Economic Council, the Council of Ministers, and the Shura Council to pass the new law. But the process began to slow. Making use of the new law had originally accelerated matters, but questions arose about articles unrelated to the minimum capital requirement. SAGIA and the Ministry of Commerce agreed that Article 164 could still be fast-tracked if stripped from the new law. The legislative creativity worked. Within a month Article 164 won passage through all legislative bodies and the king's signature. Reflecting on the experience, the deputy governor Al-Awwad of SAGIA says, "it is sometimes important not to wait until you have the whole perfect picture. Instead focus on what works."

Leveraging international experience

Early in the implementation phase, the king sent a memo instructing SAGIA to hold workshops with every related agency in Saudi Arabia on how to improve its ease of *Doing Business*. At these workshops SAGIA and others elaborated clear responsibilities, timetables, action points, and benchmarks.

To benefit from international experience, in June 2006 reformers contracted with consultants from Monitor Group—a global strategic consulting firm that specializes in national economic development—to learn more about best practices for business entry around the world. Monitor Group brought analytical expertise and strategy assistance. And it was a useful outside player to assess current conditions and future requirements. In collaboration with the Ministry of Commerce, it developed a performance measurement system for ministry staff, highlighting the importance of results.

Since its formation, the Ministry of Commerce has been keen to foster the domestic private sector. SAGIA benefited, spotlighting how the ministry's strategic vision aligned with its own. Within a few months the ministry became a partner in championing the reform.

Making the reforms sustainable and responsive to the private sector was imperative because stakeholder views change over time. So, the National Competitiveness Center established a second level of work at the cluster level—a platform for members of the private and public sectors to meet, discuss, and resolve issues, with the National Competitiveness Center just a facilitator.

More outreach needed

Dabbagh and SAGIA have tried to communicate the reforms broadly, but much more can be done. In this country—of more than 27 million inhabitants, where small and medium-size enterprises contribute only 28% of GDP—a stronger media campaign is needed to motivate would-be entrepreneurs to create their businesses and to join the formal sector. The team is reaching out to those people to trumpet the opportunities.

A senior Saudi official who was directly engaged in the reform says, "We are not just content to rest on the accomplishments. We know there is a great deal more work to be done to achieve our 10-by-10 objective, but we like to look at our goal as Michelangelo did when he said, 'The greatest danger for most of us is not that our aim is too high and we miss it, but that it is too low and we reach it.'"