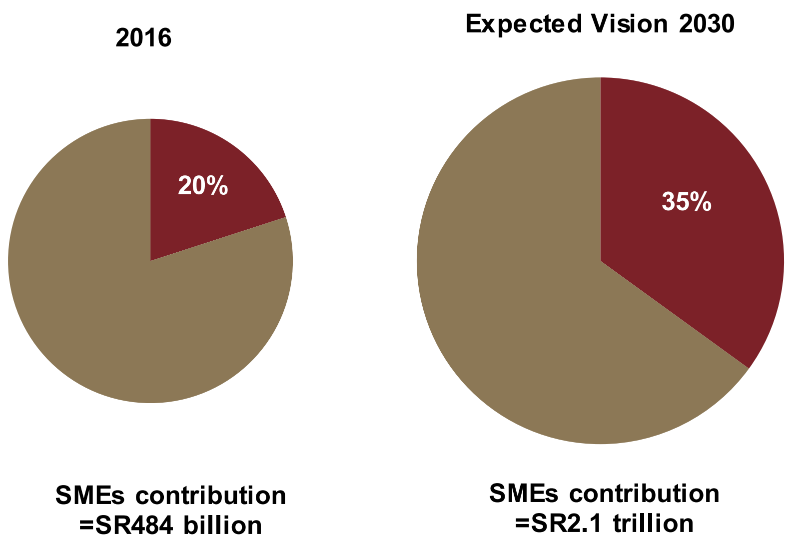
March 2019

SMEs and Vision 2030

Smaller Units for a Larger Economy

- Numerous examples across differing countries show how vital small and medium enterprises (SMEs) are in supporting economic development and growth, as well as fueling job opportunities.
- Currently in Saudi Arabia, according to data from the General Authority for Statistics (GaStat), around 950 thousand SMEs were registered for business purposes in the Kingdom, all the while providing one million Saudis with employment.
- One of key objectives outlined in the Saudi Vision 2030 (Vision) relates to raising the level of SME's contribution to GDP. Specifically, the target refers to raising the current contribution of 20 percent of GDP to 35 percent by 2030 (Figure 1).
- In fact, raising the contribution of SMEs in the local economy is mentioned in several Vision Realization Programs (VRPs), such as the Financial Sector Development Program (FSDP) and the Public Investment Fund (PIF) program.
- Accordingly, and in line with Vision targets, a number of major reforms and initiatives have been implemented to support the development of SMEs in the Kingdom.
- Overall, the government plans to introduce previously absent sectors into the economy, which will not only help economic diversification efforts, but also provide sizable opportunities for entrepreneurs.
- As these reforms begin to take shape, and the business environment for SMEs improves, we expect to see the overall contribution of SMEs to rise in the local economy over time.

Figure 1: Expected contribution of SMEs in GDP



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Overview

SMEs are an important pillar in all economies, as a vital way to economic growth and job creation.

The role of small and medium enterprises (SMEs) is continuously mentioned as an important pillar in both developing and developed economies, as a vital way to spur economic growth and job creation.

For example, amongst the member countries of the Organization of Economic Cooperation and Development (OECD), SMEs account for approximately 99 percent of total enterprises, and provide the main source of employment, accounting for about 70 percent of jobs. In addition, SMEs are major contributors to value creation, generating between 50 and 60 percent of value-added in the OECD .

In the EU, where SMEs make up 99 percent of all enterprises, non-financial SMEs account for about 57 percent of value added.

In the European Union (EU), where SMEs also make up 99 percent of all enterprises, non-financial SMEs account for about 57 percent of value added (Figure 2). This percentage, however, varies across European countries, rising to more than 80 percent in Cyprus and Greece, where tourism dominates the non-financial services sector. Moreover, between 2008 and 2017, non-financial SMEs accounted for slightly more than half (52 percent) of the total increase in employment in the EU.

One of the United Nations (UN) sustainable development goals is to fulfill the rising demand on jobs by achieving full employment for both men and women, including senior citizens, youth and persons with disabilities. One way to attain this goal is to promote self-employment and the creation of new work opportunities through SMEs. Since SMEs create a broad range of employment opportunities across sectors and geographic areas, they offer a wide variety of jobs, including jobs for people with low or limited skills, all of which can help develop the workforce's skillset.

SMEs contribute 45 percent of total employment and 33 percent of GDP in emerging economies.

In emerging economies, SMEs contribute up to 45 percent of total employment and 33 percent of GDP. But when taking into account SMEs indirect contribution into account, this rises to more than half of employment and GDP in most emerging economies. Moreover, SMEs can contribute to economic diversification, especially in resource-rich countries that are particularly vulnerable to commodity price fluctuations, such as Saudi Arabia and other Gulf countries. In the Kingdom, according to the Small and Medium Enterprises Authority (Monsha'at), SMEs contribution to the Kingdom's non-oil GDP is around 21 percent, which is lower than the average of 46 percent amongst the 15 largest global economies (Figure 3).

Figure 2: SMEs and large enterprises in the EU non-financial business sector, 2016

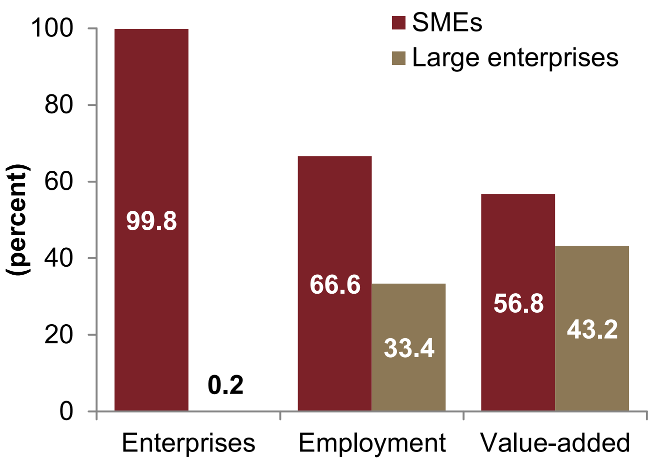
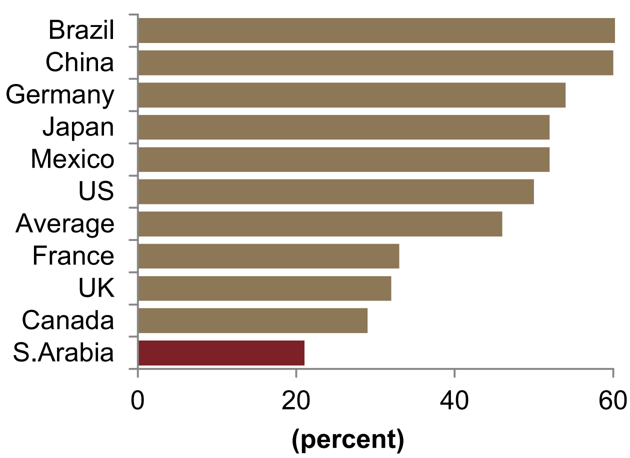


Figure 3: SMEs contribution to Saudi non-oil GDP vs. global peers



SMEs in the Kingdom

Historically speaking, it was generally acknowledged that SMEs were important contributors to diversifying the economy.

In Saudi Arabia, historically speaking, whilst it was generally acknowledged that SMEs were important contributors to diversifying the economy, framed policies were only initially introduced on a limited scale in the fifth development plan (1990-1995). The plan included developing rules and regulations to enhance SMEs contribution in the industrial sector only, which was probably driven by the remarkable growth of the petrochemical sector during the 1980s. In the sixth development plan (1995-2000), recommendations were drawn up in order to facilitate higher levels of credit for SMEs, and to launch a separate entity to overlook the sector.

Various development funds have been providing support and finance for SMEs in different ways since the early 1960s.

Separately, various development funds have been providing support and finance for SMEs in different ways since the early 1960s. For example, the Agriculture Development Fund has been providing loans and support for farmers since 1962, and the Saudi Development Bank since 1971 (previously known as the Saudi Bank for Lending and Saving), and the Saudi Industrial Development Fund (SIDF) has been supporting manufacturing enterprises since 1974. Over time, a number of other entities have emerged to provide financial support, training and advisory to SMEs, such as Abdullatif Jamil in the private sector, and Sabic and Aramco from the public sector.

SMEs in the Kingdom reached a total of around 950 thousand enterprises by the end of 2017…

...employing 1 million Saudis, and 3.7 million foreigners by the end of 2017.

Currently in Saudi Arabia, according to the General Authority for Statistics (GaStat), around 950 thousand SMEs are operating in the Kingdom at the end of 2017, with 88 percent of these enterprises classified as 'micro', employing between 1-5 employees (Figures 4 & 5). The same data shows that SMEs employed circa 1 million Saudis, and 3.7 million foreigners by the end of 2017, representing 32 percent of all Saudis, and 46 percent of all foreigners, in the labor market. Of the one million or so Saudis employed in SMEs, around 33 percent are employed in wholesale and retail SMEs, and 10 percent employed by SMEs operating in the manufacturing sector. In terms of Saudization, SMEs in the finance and insurance sector hire the biggest share of Saudis with 61 percent, followed by real estate at 48 percent (Figure 6).

GaStat data shows that Saudis working in SMEs, on average, received a monthly salary of SR6.6 thousand, compared to SR9.9 thousand per month received by Saudis working in larger

Figure 4: SMEs in KSA by size
(number of employees)

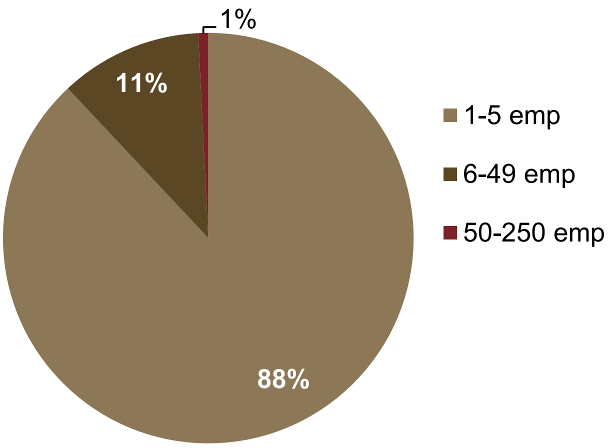
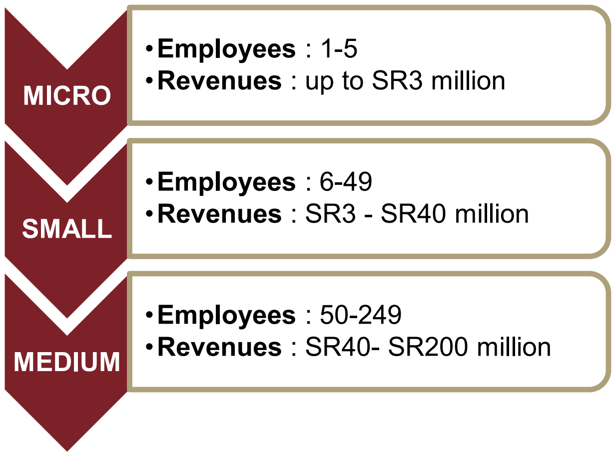


Figure 5: Monsha'at's classification for SMEs



During 2017, Saudis working in SMEs received an average monthly salary of SR6.6 thousand.

enterprises. However, the data show that some SMEs offer higher salaries than larger enterprises in the same sector, which is seen in manufacturing, transport and IT, trade, and education sectors (Figure 7).

Around 41 percent of Saudis working in SMEs range between 26-35 years old.

Moreover, GaStat data shows that 41 percent of all Saudi workers in SMEs range between 26-35 years old, accounting for the largest share amongst all age groups, with a total of 411 thousand workers (Figure 8). In fact, the percentage of 26-35 year old working in SMEs is higher than in the overall labor market average, which suggests that SMEs have the potential to create a higher number of job opportunities for Saudi youth vis-vis other types of employers.

Two-thirds of all SMEs' customers are individuals.

Looking at the consumption side, GaStat data shows that SMEs customers are predominantly individuals as opposed to corporates, with two-thirds of all SMEs' customers being individuals. Additionally, around 20 percent of customers are from the private sector compared to 14 percent from the public sector. However, this percentage varies among sectors, such as electricity and gas, and oil and minerals, where customers from the private sector represent the majority, at 57 and 36 percent, respectively.

In addition, some sectors have higher than average percentage of customers from the public sector, such as financial services and IT services, at 24 and 23 percent, respectively. Going forward, we expect the share of customers from the public sector to grow gradually, following an initiative that was announced during the year to engage more SMEs in government tenders contracts, which offers easier financial terms for SMEs.

Recent reforms for SMEs

A number of initiatives were announced to support SMEs as part of the SR200 billion private sector stimulus package.

As part of the Vision's goal to enable SMEs growth through reforms, Monsha'at and the Local Content and Private Sector Development Unit (Namaa) -which has been lately transformed into an authority according to a royal decree - announced four major initiatives to support SMEs in the Kingdom (Box 1). Collectively, these initiatives aim to regulate and develop the private sector in general, while increasing SMEs' contribution to the local economy.

Figure 6: Number of employees in SMEs by sector

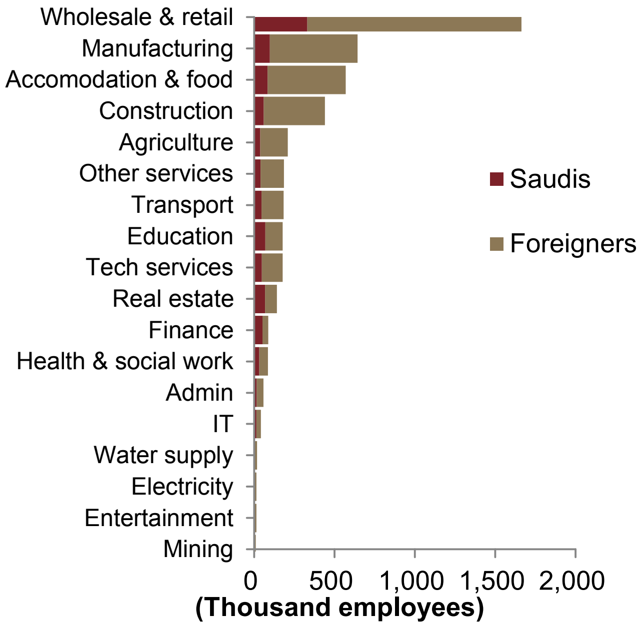
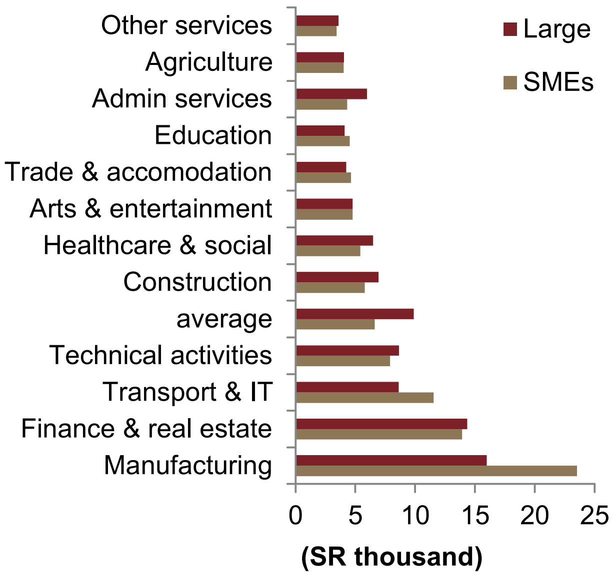


Figure 7: Average salary for Saudis in SMEs



In December 2017, the government announced a SR72 billon program to stimulate private sector growth.

...including reimbursement of some government fees, indirect funding, raising the capital of Kafalah, and a venture capital fund.

Lately, Namaa announced that the third stage of the stimulus package for the year 2019 will be announced before the year-end.

Box 1: Recent reforms to support SMEs

In December 2017, the government announced a SR200 billon four-year program to stimulate private sector growth, with SR40 billion of this being expended in 2017 and SR72 billion in 2018. The package includes 17 initiatives directed towards a number of sectors, such as manufacturing, exports and housing, as it aims to boost growth in the private sector, especially after a relative slowdown in the local economy in the past two years. The package includes SR10 billion for mega private sector projects, SR5 billion for an export bank and SR5 billion for an investment program.

As for supporting SMEs, the package provided four major initiatives:

1. **Reimbursing the government fees** paid during the SMEs' first three operational years, for enterprises registered between 2016 and 2021. The budget allocated for this initiative is SR7 billion and will reimburse fees including the issuance and renewal of commercial register; Chamber of Commerce registration; Saudi national domain registration; municipality licensing and other commercial activities.

2. **Indirect funding**, with SR1.6 billion to provide different funding channels to investment institutions, other than banks, in order to provide funding with a lower cost to SMEs.

3. **Raising the capital of Kafalah**, a Saudi Industrial Development Fund (SIDF) backed initiative to promote the participation of commercial banks in SME lending. Whilst the program has seen a decent level of success (Figure 9), ironically, its success highlights one of the main reasons for the lack of SME financing by banks in the first instance. This is because the Kafalah program encourages financing of SMEs which cannot provide guarantees or financial records for themselves. A budget of SR800 million was dedicated to this initiative, targeting enterprises in 11 different sectors.

4. **Venture capital fund** targeting startups, aiming to bridge the investment gap and spurring more SME investments. The initiative costs SR2.8 billion.

Lately, Namaa announced that the third stage of the stimulus package for 2019 will focus on non-oil manufacturing projects in the private sector. Moreover, the MLSD launched the "collective invoice" initiative in January 2019, which will help SMEs through reimbursing the difference in payments of expat fees made during 2018.

Figure 8: Saudis working in SMEs, by age group, compared to total labor force

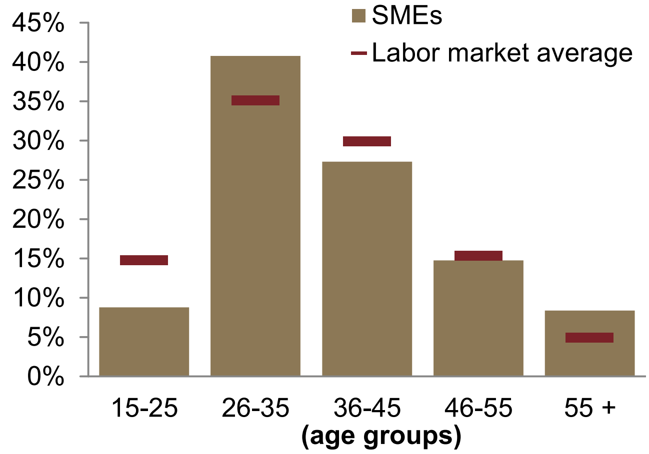
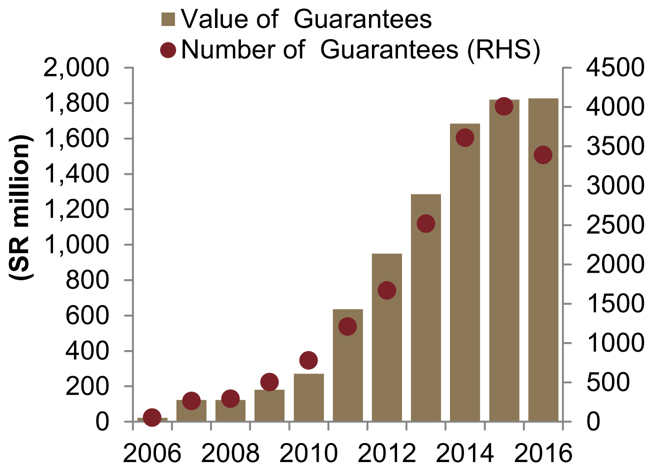


Figure 9: Number and value of SME guarantees under Kafalah program



Barriers facing SMEs in the Kingdom

GaStat's latest SMEs survey for 2017 shows that most SMEs find that electricity tariffs as the biggest obstacle for starting a new business…

GaStat's latest SMEs survey for 2017 shows electricity tariffs as the biggest obstacle to starting a business (Table 1). That said, we find some divergence in barriers, depending on the size of SMEs.

For instance, electricity tariffs seem to be a more significant barrier for micro enterprises (12 percent of micro enterprises) than medium-size enterprises (10 percent). Meanwhile, the availability of skilled labor is more significant for medium-size enterprises (8 percent) than micro enterprises (6 percent).

...followed by government regulations and licenses.

Following electricity tariffs, government regulations and licenses are the second major obstacle, by 8 percent. In the OECD, the total number of procedures needed to start a business is six, lower than the MENA average of eight procedures (Figure 10). That said, under a new initiative, all government procedures needed to start a business are planned to be expedited through the "Meras" platform. The platform aims to ease the process of starting a new business through integrated, online services, which has been launched by "Tayseer"- an initiative by a group of 20 government entities brought together to support growth in the private sector (Table 2).

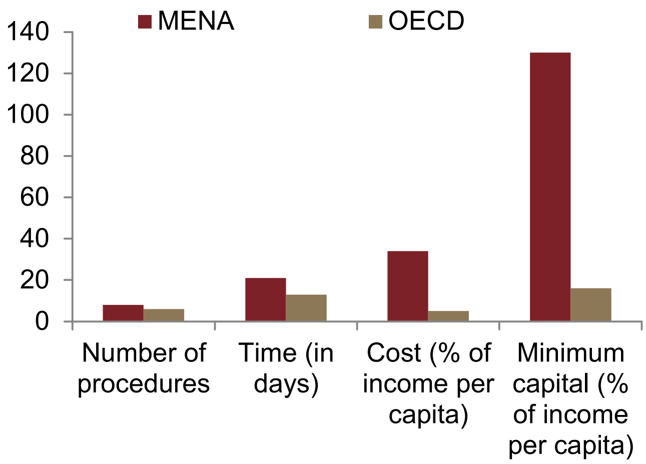
Only 2 percent of SMEs in the Kingdom identified access to finance as a main barrier to start a business.

Although only 2 percent of SMEs in the Kingdom identified access to finance as a main barrier to start a business, a study by the IMF found that more than 50 percent of firms in MENA do not have access to credit, and 30 percent of these firms identify lack of access as a major constraint. Several reports by the IMF and the World Economic Forum (WEF) argue that SMEs face such obstacles in borrowing because banks are reluctant to lend as they find these enterprises small, less diversified, and have weaker financial structures, resulting in higher borrowing risks. Meanwhile, these reports find that financing alternatives outside the banking sector are limited, and other non-bank financial institutions such as microfinance institutions, leasing companies, private equity or venture capital firms are underdeveloped in the region.

Table 1: Barriers facing SMEs in KSA, percentage:

Barriers	%
Electricity tariffs	12%
Labor laws & regulations	8%
Licenses & permits	8%
Electricity supply (without Interruption)	7%
Location & rentals	6%
Security & stability	6%
Government inspection procedures	6%
Availability of skilled labor	6%
Water tariffs	6%
Governmnet procedures & bureaucracy	6%
Water supply (without interruption)	5%
Fuel price	5%
Customes / Tarde laws & regulations	4%
Access to telecommunication (phone & internet)	4%
Fuel supply (without interruption)	4%
Access to technical support (training & services)	3%
Access to finance	2%
Ability to export	1%
Other (not mentioned)	1%
Total	**100%**

Figure 10: Cost and difficulty in starting a business (WEF)



Entities supporting SMEs in the Kingdom

Although Monsha'at is the main enabler of SMEs in Saudi Arabia…

Although Monsha'at is the main enabler of SMEs in Saudi Arabia, the scale of the change that the Kingdom intends to make in the SMEs sector requires integrated and harmonized efforts from a number of organizations (Table 3). In addition, the Saudi General Investment Authority (SAGIA) has been playing a role in supporting local and international SMEs in the Kingdom (Box 2).

...the SMEs sector needs harmonized efforts from a number of organizations.

Box 2: Foreign Direct Investments and SMEs

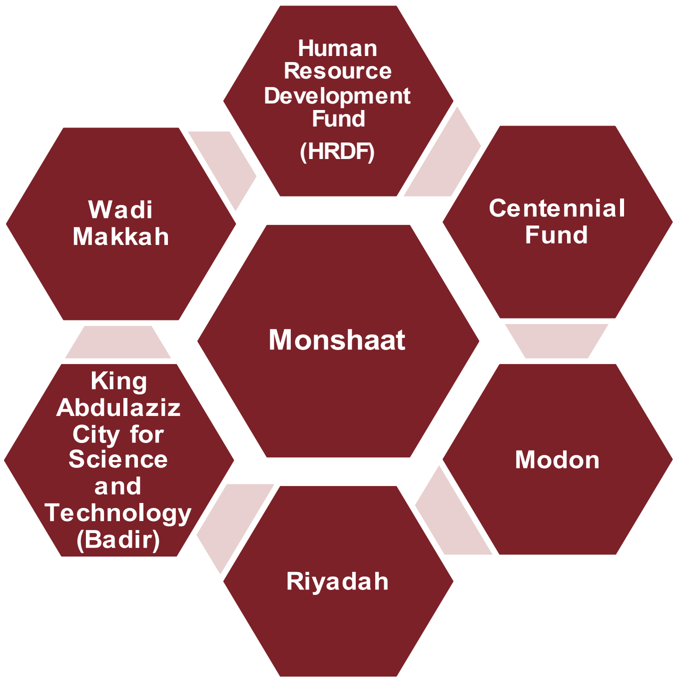
A study found that most of FDI businesses can be classified as SMEs, as of 2012.

According to a study by Riyadh Economic Forum, apart from some construction and large manufacturing projects, most of the foreign direct investments (FDI) in the Kingdom can be classified as coming SMEs. As of 2012, the study finds that almost 70 percent of FDI licenses fell under the services sector, and 30 percent in manufacturing.

Added to that, SAGIA has recently introduced a number of initiatives aiming to attract 200 international SMEs and 50 venture capital companies into the Kingdom with 100 percent ownership. Among sectors SAGIA aims to attract SMEs to are IT, FinTech, technologies in entertainment, sports and healthcare. These sectors have already been embraced by the Vision and the VRPs as part of diversifying the local economy through developing new sectors.

Table 2: Meras, first phase:

Table 3: Some entities supporting SMEs in the Kingdom



One of the key goals of the Vision is to raise the level of SME contribution to GDP from 20 to 35 percent by 2030…

...which is mentioned in several VRPs.

The FSDP, one of the VRPs, emphasized the role of SMEs in the local economy through a number of initiatives.

SMEs in Vision 2030

One of the key goals of the Vision, in relation to SMEs, is to raise the level of SMEs contribution to the Kingdom's GDP, from 20 percent currently up to 35 percent by 2030. In fact, the Vision acknowledges the current difficulties associated with SMEs in the economy and states that SMEs can still endure unnecessarily slow and complex legal and administrative procedures. It goes on to say that SMEs could, therefore, also struggle to attract the necessary skills, capabilities and funding.

Raising the contribution of SMEs in the local economy is mentioned in several VRPs (Table 4). In particular, the Financial Sector Development Program (FSDP) pays particular attention to SMEs and outlines a whole number of initiatives, as we show below. Additionally, in a recently published update, the National Transformation Program (NTP) listed a number of initiatives to improve SMEs contribution to the private sector (Table 5).

The FSDP and SMEs:

The FSDP provides two specific initiatives for SMEs (For more on this, please see our report on the *FSDP Delivery Plan*, published in June 2018):

1. Improving the SMEs financing ecosystem, through several programs which are also listed in the NTP update (Table 5).
2. Communicating lending targets to banks by 2020.

In order to assess the progress of the two initiatives, the program has introduced four related metrics:

1. SME loans as a percentage of total bank loans

Metric Name	2016	2018	2019	2020
SME loans as a percentage of bank loans	2	2	3	5

Table 4: Related Vision Realization Programs (VRPs)

The Public Investment Fund (PIF) Program	• Boost SMEs funding and venture capital investments through establishing the fund of funds, with capital of SR4 billion
The Quality of Life Program	• Providing SR440 million of funds to 600 SMEs in different regions in the Kingdom by 2020, focusing on regions with less commercial capabilities
The Financial Sector Development Program	• Incentivize the financial sector to finance SMEs (Box 3)
The Housing Program	Support higher participation of SMEs in the real estate sector

As a 2010 joint report by the World Bank and Union of Arab Banks pointed out, a lack of SME transparency and the weak financial infrastructure (weak credit information, weak creditor rights and collateral infrastructure), was one of the main obstacles for further engagement in SME finance by banks. Seemingly with this in mind, the FSDP highlights the need to establish an 'ecosystem' prior to incentivizing banks. Whilst part of this includes restructuring of Kafalah program as we show above, it also stresses enabling the two Saudi credit bureaus, Bayan and SIMAH, in collecting and updating comprehensive SME data (Box 3).

The FSDP highlights the need to establish an 'ecosystem' prior to incentivizing banks to finance SMEs...

Overall, whilst guarantee schemes, such as the Kafalah, have played an important role in providing finance to SMEs, the FSDP charter emphasizes that the strengthening of credit information systems and creditor rights will be the priority item going forward.

Box 3: Incentivize Financial Sector to Finance SMEs

Two specific initiatives are outlined to incentivize financial services providers to engage with SMEs:

1) Improving the SMEs financing ecosystem through
- Strengthening the legal framework
- Restructuring the Kafalah program
- Government committing to allocate more contracts to SMEs
- Enabling Bayan and SIMAH to collect and update comprehensive SME data
- Establishing a local rating agency for SME credit assessment
- Providing alternative SME funding options (e.g. PE and VC)

2) Communicating lending targets to banks by 2020

...and communicate lending targets to banks by 2020.

2. Value of SME Funding through Private Equity/Venture Capital

Metric Name	2016	2018	2019	2020
Value SME Funding through Private Equity/Venture Capital (SR bn)	-	-	13	23

The FSDP also aims to increase funding options for SMEs, through private equity and venture capital.

Another recently launched initiative that aims to boost SME financing is the Musharakah program. This program can be seen as directly helping with FSDP metric related to raising the level of private equity and venture capital financing to SME funding. The Musharakah

Table 5: Updated NTP initiatives for SMEs: Some of the entities related with these initiatives: Ministry of Commerce, Ministry of Planning, Ministry of Justice, Ministry of Labor, Monsha'at and SAGIA

- Design policies of SMEs and facilitate the procedures of registeration and promote innovation
- Develop financing solutions for SMEs through government financing and the private sector
- Increase SMEs in all regions of the Kingdom, to spur growth in less developed regions
- Support SMEs in accounting, Zakat and taxation
- Improve SMEs resources and productivity by training programs
- Build a research center to provide accurate indicators and statistics on SMEs
- Launch e-applications to support SMEs, by providing e-training, consulting services, and a job platform

program, which is part of a larger government-backed SR4 billion fund, aims to develop a system where the required types of capital for all stages of an SME lifecycle are made available on a Shariah compliant basis. The Musharakah program specifically aims to facilitate funding from venture capital, debt, mezzanine and private equity funds and therefore is hugely relevant in achieving this particular metric.

FinTech is defined as new technologies whose applications may affect financial services, artificial intelligence, big data, biometrics, and blockchain.

3. A minimum of three licensed FinTech players by 2020:

Metric Name	2016	2018	2019	2020
# of Fintech players	-	-	-	3

According to the International Monetary Fund (IMF), financial technology (FinTech) is defined as new technologies whose applications may affect financial services, artificial intelligence, big data, biometrics, and blockchain.

Globally, FinTech firms have attracted substantial investment in recent years...

On a global level, in the last decade at least, there has been a rapid acceleration in a broad range of FinTech products and services. This, in turn, has given rise to new technological applications which have simplified day-to-day financial processes such as making payments, saving, borrowing, managing risk and getting financial advice (Table 6). Concurrently, FinTech firms have attracted substantial investment in recent years. According to figures cited by the IMF, total global investment in FinTech companies increased from $9 billion in 2010 to over $25 billion in 2016. Venture capital (VC) investment has also risen steadily, from $0.8 billion in 2010 to $13.6 billion in 2016.

… but the progress within the Saudi FinTech space has been limited to-date.

Despite the developments on a global level, the progress within the Saudi FinTech space has been limited to-date. As the FSDP charter highlights, Saudi Arabia is one of the only countries, amongst the leading FinTech countries, to disallow non-banking licenses for FinTech companies. That said, weeks prior to the unveiling of the FSDP, SAMA launched the FinTech Saudi initiative which lists many of the targets identified within the charter as its objectives. Moreover, moving forward, FinTech Saudi is expected to launch a number of workshops, educational and awareness activities to help spur innovation in the FinTech space.

Table 6: Financial Technology (FinTech), Vision 2030 and SMEs:

FinTech is defined as new technologies whose applications may affect financial services, artificial intelligence, big data, biometrics, and blockchain.

EXAMPLES

- Simplifying day-to-day **financial processes:** making payments, saving, borrowing and financial advice

SIZE

- Global investments in FinTech increased from **$9** bn in 2010 to over **$25** bn in 2016

VISION 2030

- **FSDP** aims to have 3 FinTech players by 2020
- **PIF program** aims to help develop digital banking ecosystems

SMEs

- FinTech helps SMEs to **reach financing** and financial advice more easily
- FinTech is a **new sector** for SMEs to explore and invest

The PIF is expected to be a key investor in FinTech, at both home and abroad.

Saudi Arabia's FinTech ambitions will also be supported by the PIF, which has in the recent past demonstrated its willingness to invest in such ventures. The PIF's own Vision 2030 program, outlines the sovereign fund's role in, amongst other things, developing the Kingdom's technological expertise. Specifically, one of PIF Program's objectives is to help develop digital banking ecosystems and support banks in their digital transformation plans in line with global trends and practices. With this in mind, the PIF is expected to be a key investor in FinTech, at both home and abroad.

4. Raising the number of listed micro/small companies

Metric Name	2016	2018	2019	2020
Number of micro/small companies listed as percentage of total listed companies	34	>=36	>=39	>=40

The FSDP aims to raise the number of listed SMEs in the Nomu market.

Back in Feburary 2017, the CMA officially launched a parallel market (Nomu) in the Kingdom and we see this as being the driving force behind this particular metric being achieved. Whilst Saudi Arabia is the first country in the Gulf region to launch a parallel market, such markets have existed since the 1970's in many mature economies. Perhaps the best example of a parallel market is the US NASDAQ, which was set-up in the early 1970's. During the mid to late 1990's, many European exchanges also went about launching their own versions of a parallel market, including AIM (UK), Neuer Markt (Germany) and the Nouveau Marché (France).

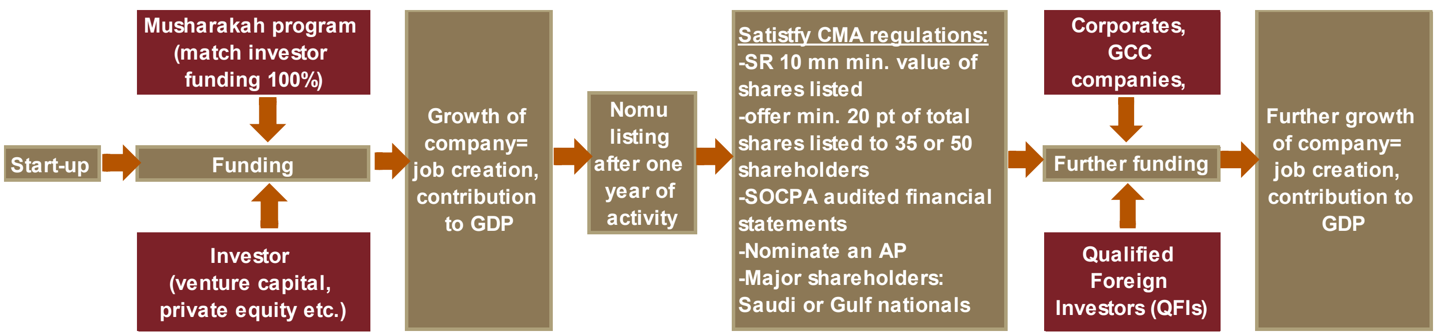
By in large, global parallel markets have been a relative success, helping spawn a number of prosperous companies, which have ultimately sought full listing in the main market. In the same way, Nomu presents the possibility for companies to transition into the main market (Table 7). To help SMEs through this path, Monsha'at introduced a separate initiative "Tomoh", to provide support and business solutions on growth and market listing requirements.

SAMA has lately indicated that financing SMEs in the local market rose from 2 percent of total lending in 2011 to get closer to 5 percent by the end of 2018.

Saudi Arabia ranked 92 out of 192 countries in terms of "ease of doing business" in 2019, up from 96 in 2015.

Overall, we can see the focus in the Vision on finding and enabling new financing solutions for SMEs, such as the indirect funding and venture capital initiatives discussed above (Table 8). As a result, SAMA has lately indicated that financing SMEs in the local market rose from 2 percent of total loans in 2011 and got closer to its 2020 target of 5 percent by the end of 2018. All of these measures could help improve the local business climate and result in improving the Kingdom's "Doing Business" rank, an annual report published by the World Bank. In its latest release, Saudi Arabia ranked 92 out of 192 countries in terms of "ease of doing business", improving from 96 in 2015. That said, SAGIA aims to get the Kingdom in the top 20 in the next few years.

Table 7: The path of an SME from start-up to Nomu listing



Challenges and Opportunities

The rout to economic diversification should provide sizable opportunities for entrepreneurs.

As the government introduces new sectors in the local economy on route to its drive for diversification, this should provide sizable opportunities for entrepreneurs. For example, tourism is one of the sectors that the Vision is aiming to expand. Whilst tourism enterprises constitute 60 percent of total SMEs in the EU, the share is only 12 percent in the Kingdom (Figure 11). Moreover, within tourism enterprises, there is a big divergence between the proportion of art, entertainment and recreation enterprises between the EU (47 percent of total SMEs) and Saudi Arabia (0.2 percent of total SMEs), offering a great potential for growth for these SMEs in the local economy, with the anticipated expansion in the sector. As we showed in our report on *Tourism and Entertainment* (published in April 2018) vital opportunities are likely to arise from building public-private partnerships, providing extensive training and learning by doing, which would help in supporting SMEs. For example, the government can help through initiating partnerships between regional hotels, tour operators, transport providers, vendors, entrepreneurs and related government departments to address obstacles and build partnerships. Eventually, SMEs could benefit from the growing tourism and entertainment market and from the economies of scale provided by the emerging tourism and entertainment sector, helping the local economy to reach the goal of economic diversification.

Technology can also play a big role in defining SMEs in the Kingdom.

Technology can also play a big role in defining SMEs in the Kingdom. Recent studies by the World Economic Forum (WEF) found that technologies have a greater return on investment in countries with high labor costs, as producers are more encouraged to seek out technologies that boost labor productivity. In 2015, North America and Europe together made up 80 of the wearable technology market and almost 70 percent of industrial 3D printing units, as both technologies showed a correlation with raising labor productivity in several ways. Moreover, 70 percent of the record 250 thousand industrial robots sold in 2015 went to five countries: four with predominately high labor costs: Germany, Japan, South Korea and the United States (Figure 12). With relatively high labor costs in the Kingdom, the recent interest in FinTech could play a vital role in defining future investments by SMEs. As discussed above, FinTech can help SMEs in many business aspects and financial solutions.

There seems to be a rising opportunity for Islamic finance products for SMEs.

In addition, as a financing alternative for SMEs, there seems to be a rising opportunity for Islamic finance in the local market. A study by the International Finance Corporation (IFC) in 2014 finds that there

Table 8: Main recent reforms to support SMEs in the Kingdom:

- **Reimbursing government fees, such as expat levies, which showed the highest share in fee costs.**
- **Indirect funding, to provide funding with a lower cost to SMEs.**
- **Raising the capital of Kafalah, a program designed to support financing SMEs through the banking system through guarantees.**
- **Government venture capital fund targeting startups.**

As Nomu listed SMEs increase in size, a move to the main market could result rising profits.

A gradual increase in the contribution of SMEs in the local economy is in the horizon.

is high demand for Islamic products among SMEs in the MENA region. In the Kingdom, the IFC study conducted a survey and found that up to 90 percent of SMEs are looking for Shariah-compliant banking services. The study finds a number of Islamic financial products suitable for SMEs in the Kingdom, such as Mudarabah and Musharakah, two dominant participatory schemes, which allow Islamic banks to lend on a longer-term basis to projects with higher risk-return profiles, and leasing, which avoids the problem of collateral. This provides a rising opportunity for the local financing companies participating in the indirect funding initiative, as most of these companies provide Shariah-compliant financing products.

Another opportunity in front of SMEs, is the support to get listed in Nomu, the parallel market, as discussed above. As Nomu listed companies increase in size, a move to the main market could result in an accompanying increase in its profile as well as increased equity analyst coverage, both of which may help ensure higher demand for the company's securities. Looking at the Musharakah program and Nomu together, we can see the strategic thinking behind government policy in trying to develop a path for SMEs that allows them to progress from a small scale start-up to a listed entity.

Moreover, the Vision, through the PIF program and the FSDP program, outlines a number of solutions to incentivize financial services providers and to improve the SMEs financing ecosystem. For example, strengthening the legal framework, enabling Bayan and SIMAH to collect and update comprehensive SME data, and establishing a local rating agency for SME credit assessment. To follow up the progress, the FSDP suggests communicating the lending targets to banks by 2020.

With new reforms to enhance the business environment, and various initiatives to facilitate financing solutions, we expect to see a gradual higher contribution of SMEs in the local economy, especially with the high local demand and level of consumption derived from the large population in the Kingdom. In addition, and along with the structural changes in the labor market, many job opportunities can be found the SME sector, especially for the youth.

Figure 11: Share of tourism enterprises in total SMEs, EU and KSA

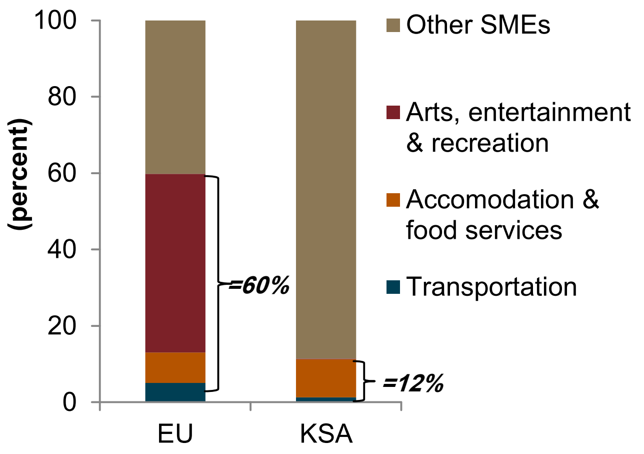
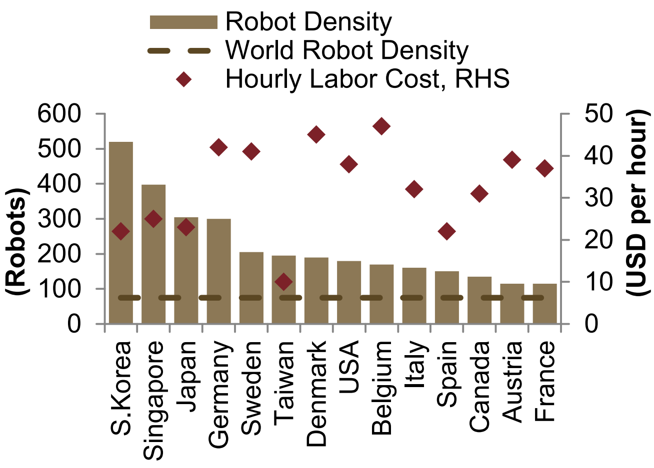


Figure 12: Robot density in countries with highest labor cost
(Robots per 10,000 manufacturing workers)



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