

Challenges of venture capital in supporting startups and ways of its success: A case study of Saudi Arabia and its dropped on Algeria

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Abstract:

The objective of this study is to highlight the venture capital as a mechanism of funding developed to support and finance start-ups and the role played by venture capital in alleviating the burden in terms of financing. Especially because start-ups are considered the problem of financing that prevents them from achieving their goal. We have studied the reality of the Saudi experience as a model. We found in this study that the Kingdom of Saudi Arabia ranks second in terms of venture investment according to the report of the first half of Venture investment in the Kingdom of Saudi Arabia for the year 2023, due to government support and economic development, which allowed an increase in the number of investors in the venture capital and when it was dropped on Algeria. Venture capital is still beginning despite the State's endeavours to promote it.

Keywords: venture capital; Kingdom of Saudi Arabia; start-ups; Algeria.

Jel Classification Codes: G32, G24.

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1. Introduction

In light of the economic transformations and changes in the world today, Algeria has moved towards attending to the start-ups sector because they play an active role in driving the country's economic wheel and supporting and developing the economies of the countries. Algeria is working to develop the country through the enactment of a number of resolutions and laws to facilitate the operation of these institutions.

Perhaps one of the most prominent methods of innovative financing is venture capital financing, which involves providing capital to emerging and start-up enterprises that herald their ability to grow and their high potential to develop.

Venture capital investors are people who manage investment funds that specialize in identifying future start-ups.

Venture capital is not required to be as monetary as other types of financing, but can be in the form of expertise in different sectors that contribute to an enterprise's long-term growth.

One of the leading experiences in the field of venture capital, we find the Saudi experience occupies the first ranks in this field, due to the increase in the number of investors in this field and the availability of the right environment for investment.

From the foregoing, the research problem can be formulated as follows:

Can Venture Capital support Algeria's start-ups like it does in Saudi Arabia, and what are the challenges they face in achieving success?

A number of sub-questions include the following:

- What is the legal framework governing the operation of Algeria's venture capital?
- What role does Algerian Financial Participation (finalep) play in Algeria?
- What role does Saudi Arabia's venture capital play in financing and supporting emerging institutions as a useful model?

This study aims to:

- Highlight the concept of bold capital and emerging institutions.
- Identify the main challenges facing Algeria's bold capital.
- Recognise the reality of the concept of bold capital and how to benefit from the Saudi experience.

In light of the subject matter of the study and in response to the requirements for achieving its objectives, the study's hypotheses may be formulated as follows:

- Venture capital in Algeria is still in its infancy, so the Algerian state must give it greater importance.
- The Kingdom of Saudi Arabia is well-examined among the countries of the region in terms of the volume of investment in venture capital and the government initiatives that stimulate this system.

To achieve the objective of the study, the descriptive curriculum was based on the concept of venture capital, start-ups and a reality study in the Kingdom of Saudi Arabia, bringing it down to Algeria and highlighting Algeria's most important challenges.

In order to achieve the study's objectives, it will be divided into the following axes:

The first axis: start-up: venture Capital Basic Concepts.

The second axis: The reality of Saudi capital in financing start-ups.

The third axis: The challenges of Algeria's venture capital and its successes.

2. Start-ups venture capital: basic concepts

2.1.1 Definition of start-up:

The concept of start-up has received great attention from researchers due to the role it plays in developing and developing the economies of countries.

The start-up is defined as:

- ✓ A startup is a young, dynamic company built on technology and innovation wherein the founders attempt to capitalise on developing

a product or service for which they believe there is a demand. (Surbhi , 2016)

✓ A start-up is a company, partnership or temporary organisation designed to search for a repeatable and scalable business. Due to the future of a start-up is to stop being a start-up and become part of a large company or fail and move to another opportunity (Cobanoglu & Della Corte, 2021).

✓ The Algerian legislature did not give an explicit definition of startup enterprises, but rather defined them through the conditions for granting a startup enterprise label. These standards, according to Executive Decree 254/20, are:

- The age of startups does not exceed 8 years.
- The business model of organisations depends on innovative services, products or ideas.
- The amount determined by the National Committee may not exceed the annual turnover.
- At least 50% of the company's capital must be owned by investment funds accredited by other institutions that hold the start-up label or by natural persons.
- The growth potential of the organisation should be large enough (artical11, 2020)
- The number of workers does not exceed 250 workers .(artical11, 2020)

Accordingly, it can be mentioned that start-ups in Algeria, through these criteria, are defined as “every institution subject to Algerian law, whose growth rate is high, depends on an innovative idea, and whose number of workers does not exceed 250 workers.”

Through the above, start-ups can be defined as “newly established institutions, characterised by rapid growth, working to innovate a new product.”

2.2.2 The characteristics of a start-up

The start-up is distinguished from other institutions by a set of characteristics namely Temporary, Looking for a Business Model,

Industrialisable, Scalable. These characteristics can be expanded or reduced, depending on the source, but the ones listed above are the most common, and this can be mentioned Bellow: (chivalier, 2023)

• **Temporary:** to turn an idea into a business, to find a new way to render a service, to create value a start-up is not destined to remain so all its life. Being a start-up is not an objective in itself. A start-up is a particular phase, and the main goal is to get out of it.

• **Looking for a Business Model:** the challenge of a start-up is to find and build the Business Model that goes with it. A Business Model that is not modelled on an existing structure, and is not necessarily obvious at the launch of the structure, and being a start-up is bringing value to customers with a product or service that no one has ever done before.

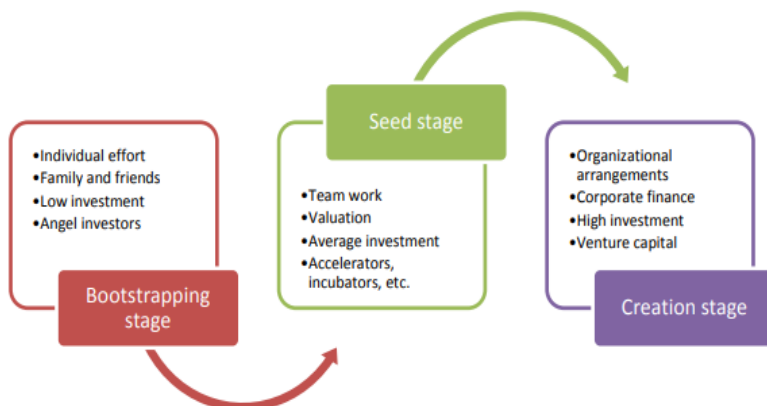
• **Industrialisable /Reproducible:** This means that a start-up is looking for a model that, once it works, can be done on a larger scale, in other places, or be done by others.

• **Scalable (for exponential growth):** The other feature of a start-up is its scalability. Having a model where the more customers you have, the greater the margins. The first customers cost more than the next ones, and so on. It is this scalability, and the fact that the model is reproducible, that allows start-ups to grow so fast and so far, in a short time, compared to a more traditional company.

2.1.3 The lifecycle of start-ups

Start-up differs from other institutions by a life cycle that can be explained in the following figure (Salamzadeh & Kesim, 2015)

Fig.1. Lifecycle of startups



Source: (Salamzadeh & Kesim, 2015).

• Bootstrapping stage:

The purpose of this stage is to position the venture for growth by demonstrating product feasibility, and customer acceptance, cash management capability.

In this very early stage, the entrepreneur himself/herself initiates a set of activities to turn his/her idea into a profitable business. However, he/she considers a higher risk or even uncertainty level, continues working on the new venture idea, makes a team, uses personal funds, and asks family members and friends for their investment in the idea. Bootstrapping is sometimes defined as highly creative ways of acquiring the use of resources without borrowing.

• Seed stage:

For most start-ups, the seed stage is a mess and is construed as highly uncertain a great number of start-ups fail in this stage. Since they could not find support mechanisms in the best case they would turn to a low-profit company with a low rate of success. On the other hand, those who succeed in receiving support would have a higher chance of becoming profitable companies. It goes without saying that valuation is normally done at the end of this stage This stage is characterized by prototype development, teamwork, entry into a market, valuation of the venture, seeking for support mechanisms

such as accelerators and incubators, and average investments to grow the startup.

• **Creation stage:**

Corporate finance is considered the main choice for financing the firm. Venture capital could facilitate the creation stage, by funding the venture.

Creation stage occurs when the company enters into the market, and hires first employees, sell its products, at the end of this stage, an organisation/firm is formed.

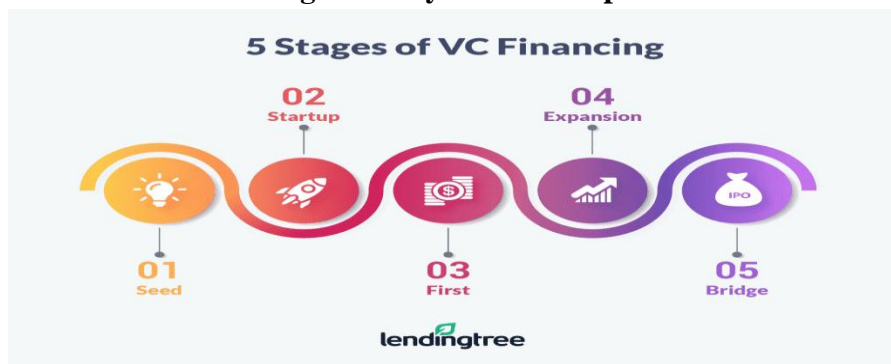
2.2.1. Definition of venture capital:

The term venture capital (or risk capital) can be used in a broad sense, to include all types of capital invested in high-risk projects, including resources from entrepreneurs (miheala, 2012). Venture capital is an alternate source of finance for startups. It is private equity financing provided by investors to start-ups where they see long-term growth potential (FINFIRST, 2023) is a form of business financing in which funding is obtained in exchange for ownership in the company. Rather than borrowing from a bank or alternative business lender and paying back your debt, you could receive money from an investor who would help expand your business while earning a share of the profits (Wylie, 2022).

2.2.2 The stages of venture capital

The stages of VC financing are typically broken down into five phases can be explained in the following figure: (Wylie, 2022)

Fig.2. Lifecycle of startups



Source: (Wylie, 2022).

- ✓ **Seed stage:** Seed-stage Venture Capitals invest in businesses that are still just an idea for a product or service. If the idea has growth potential, the Venture Capital would finance early product or business plan development or market research. They may also help set up a management team for the company.
- ✓ **Startup stage:** Once a start-up has a business plan and product prototype to show investors, Venture Capitals would supply cash to cover start-up costs, such as advertising and marketing. The business could obtain money from the same VCs that financed the seed stage, or the business could bring on new investors.
- ✓ **First stage:** Venture Capitals would provide capital for manufacturing and sales as the company becomes operational.
- ✓ **Expansion stage:** After the business starts selling products and services, Venture Capitals could help grow the business by investing in marketing expansion or a new product line.
- ✓ **Bridge stage:** The business could transition to a public company after reaching maturity. At this stage, Venture Capitals could provide financing to support a merger, acquisition or initial public offering (IPO), and then sell off shares to exit the company and earn a return.

When a Venture Capital makes an investment, the business owner receives the funds in a lump sum. Venture Capital is milestone-

driven and during each stage, you would determine how much funding is necessary to bring your business idea to fruition. You would receive the money upfront and then seek additional funding as the business moves into different stages. More will be raised later in different rounds based on hitting milestones.

Venture capital financing can be a risky arrangement for both business owners and investors. Venture Capitals typically invest in quite a few businesses with the expectation that several will fail. They look for companies that could have a big payoff to offset the anticipated loss.

2.2.3 The characteristics of a venture capital

Venture capital as a source of financing is distinct from other sources of financing because of its unique characteristics, as set out below: (Suraj, 2023)

- ✓ Venture capital is essentially financing of new ventures through equity participation. However, such investment may also take the form of a long-term loan, purchase of options or convertible securities. The main objective underlying investment in equities is to earn capital gains thereon subsequently when the enterprise becomes profitable.
- ✓ Venture capital makes long-term investments in highly potential ventures of technically savvy entrepreneurs whose returns may be available after a long period, say 5-10 years.
- ✓ Venture capital does not confine to supply of equity capital but also supply of skills for fostering the growth and development of enterprises. Venture capitalists ensure active participation in the management which is the entrepreneur's business and provide their marketing, technology, planning and management expertise to the firm.
- ✓ Venture capital financing involves a high-risk return spectrum. Some of the ventures may yield very high returns to more than

Compensates for heavy losses on others which may also have earning prospects.

2.2.4 The importance of venture capital is: (bottazzi, 2009)

- ✓ Venture capital is a specialised form of financial intermediation its success in supporting innovative companies.
- ✓ Venture capital concentrates on startup firms and uses their knowledge of industries and markets to evaluate and mentor entrepreneurs.
- ✓ Venture capital also plays an important role in the process of going public. Their experience helps companies choose the most favourable time for their IPOs and experience lower.
- ✓ Attracts companies which already have good growth opportunities so that venture investors would mainly need to bring them to a successful existence.
- ✓ Finance companies whose innovation strategies are already well-developed

3. The reality of Saudi capital in financing start-ups

3.1. The emergence of venture capital companies in Saudi Arabia

The Saudi Venture Investment Company is a government investment company established in 2018 and affiliated with the Small and Medium Enterprises Bank, one of the development banks affiliated with the National Development Fund.

This company aims to stimulate and sustain financing for start-ups from the pre-establishment stage until before the initial public offering by investing in funds and participating in start-ups in order to fill the financing gaps for emerging enterprises capable of rapid growth and small and medium enterprises capable of growth.

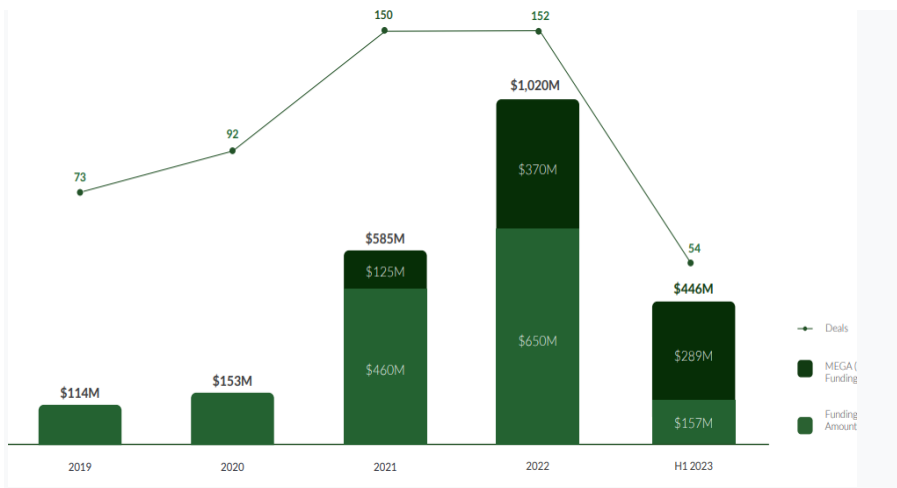
3.2 Evaluation of the financing of venture capital companies in the Kingdom for start-ups for the first half of 2023

venture capital companies will be evaluated through a range of points: (Abdulrahman M, et al., 2023)

3.2.1 Yealy Funding Evolution 2019-1H2023

The Saudi venture capital space started 2023 strong with the announcement of two MEGA deals worth 289\$ M in February pushing funding up to 446\$ M in 1H2023 can be explained in the following figure.

Fig.3. 5YR venture funding evolution in Saudi arabia by amount an number of deals

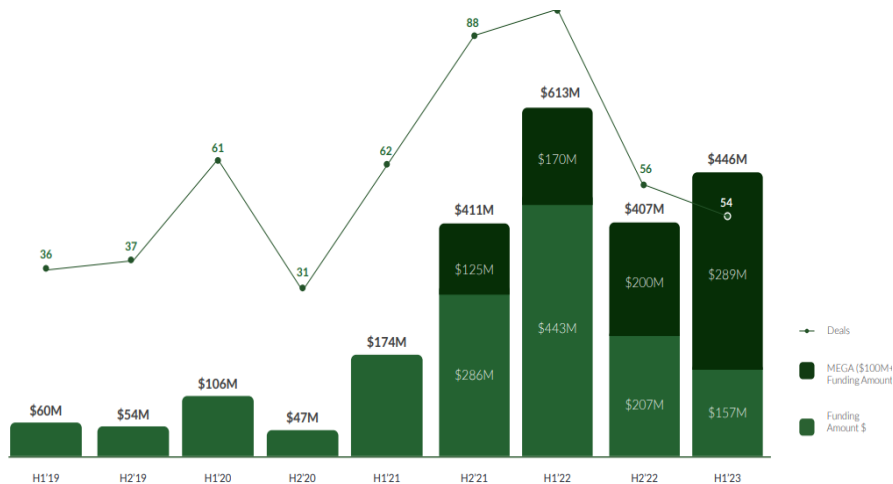


Source: 1H-2023 Saudi Arabia Venture Capital Report.

3.2.2 Half yearly funding evolution /1H-2023

On 2023 saw the second consecutive half yearly decline in both deals and non –MEGA deal funding can be explained in the following figure.

Fig.4. 9H venture funding evolution in Saudi Arabia by amount and number of deals

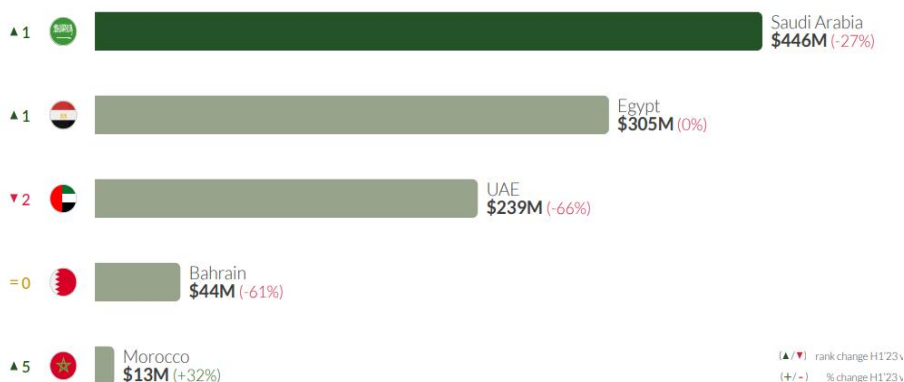


Source: 1H-2023 Saudi Arabia Venture Capital Report .

3.2.3. Top countries by total funding in MENA in 1H 2023

Saudi Arabia was the most funded country in the MENA region followed by Egypt, which came second and the UAE which landed third can be explained in the following figure.

Fig.5: Top countries by total funding in MENA in 1H 2023

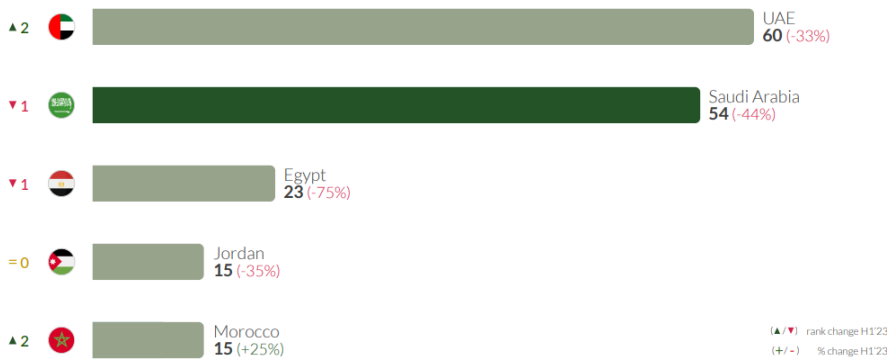


Source: 1H-2023 Saudi Arabia Venture Capital Report.

2.2.4 Deals By Comparison Country MENA - 2023 1H

Closed deals total the of 28% for accounting, region MENA the in-country transacted most second the as landed Kingdom The .difference deal six a with Kingdom the of ahead coming, deals 60 with countries MENA topped UAE - .year last of period same the in difference deal five a to compared 2023, 1H in deals 31 of gap remarkable a with ranking in Arabia Saudi followed Egypt can be explained in the following figure.

Fig.6: Top countries by Number of deals in MENA in 1H 2023



Source: 1H-2023 Saudi Arabia Venture Capital Report.

2.2.5 Top industries by total funding in Saudi Arabia in 1 H 2023

Deals MEGA two then to due mainly funding in expansion YoY 245% a with 2023 in Kingdom the in industries of star rising the was Retail/Commerce-E can be explained in the following figure.

Fig.7. Top industries by total funding in Saudi Arabia in 1 H 2023

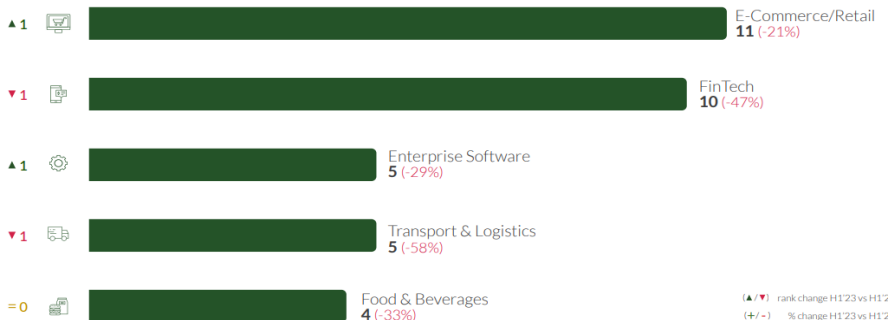


Source: 1H-2023 Saudi Arabia Venture Capital.

2.2.6 Top industries by number of deals in Saudi Arabia in 1 H 2023

can be explained in the following figure.

Fig.8 Top industries by number of deals in Saudi Arabia in 1 H 2023



Source: 1H-2023 Saudi Arabia Venture Capital Report.









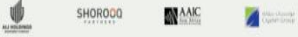
2.2.7 Disclosed Funding Rounds in Saudi –Based Startups 1H 2023 Top 5 Deals

-Top five deals closed in Saudi Arabia in 1H2023 captured 79 of capital deployed in the country with E-Commerce/Retail reigning over the top three.

-The Kingdom came ahead of the overall MENA region 61% and UAE 62% in the share of top five deals of total funding.

-Floward s’Saudi& s’Nana” C “Series MEGA rounds along with s’Sary M\$50 funding round were among the top five funding rounds in the MENA region. can be explained in the following figure.

Fig.9. Disclosed Funding Rounds in Saudi –Based Startups 1H 2023 Top 5 Deals

		Amount Raised	Funding Stage	Month	Industry	Investors
1		\$156M	Series C	Feb	E-Commerce/Retail	STV 
2		\$133M	Series C	Feb	E-Commerce/Retail	
3		\$50M	Undisclosed	Jan	E-Commerce/Retail	VSC 
4		\$8M	SEED	March	Travel & Tourism	Undisclosed
5		\$7M	Pre-Series A	March	Healthcare	

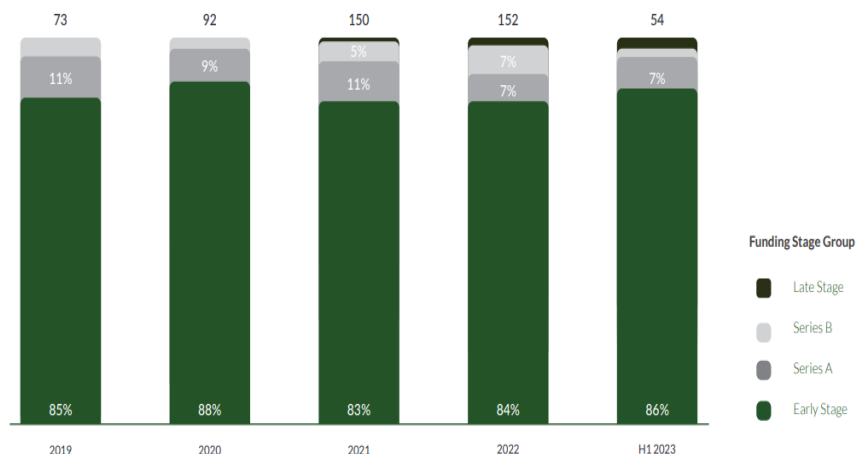
Source: 1H-2023 Saudi Arabia Venture Capital Report.

2.2.8 Saudi Arabia venture capital Funding By Stage in 1H2023

- Early stage pre- SEED Pre to –Series A (deals continued to capture the lion’s share of 86 % of the total 54 deals closed in 1H2023.
- The concentration of the kingdom's deals in the Early stage was similar to that of the overall MENA region and the UAE which saw 89 %and 90% of the deals in the Early stage.
- Interestingly the share of late-stage rounds stood at 5 in 1H 2023 The highest it has ever reached.

can be explained in the following figure.

Fig.10. Yearly VC deals in Saudi Arabia by stage (%)



Source: 1H-2023 Saudi Arabia Venture Capital Report.

- The interest of local investors was elevated with Saudi –based investors capturing a dominant share of 67 % in the first half of 2023 the highest it has been since 2020-2023.
- The participation of international investors decreased to account for 15% in 1H-2023.

During the first half of 2023, venture capital companies contributed to:

- Saudi Arabia captured 28% of total deals in the MENA region in the first half of 2023.
- The first half of 2023 broke the record of the kingdom's MEGA deal funding which stood at 289\$ M.
- Commerce/retail was the industry of choice for investors in Kingdom s’ vc space by funding and by deals in 1H 2023.
- the kingdom surpassed Egypt and UAE in funding with the gap in funding between the kingdom and the UAE exceeding 200\$ in the covered half.
- Saudi Arabia became the top-funded country and secures the second-highest transaction in the MENA region during 1H 2023.

I am backing Saudi-based startups retreated by 41% yoy to stand at 54 %investors in 2023.

4. The challenges of Algeria's venture capital and its successes

4.1 Legal Framework for Algeria's Venture Capital Activity

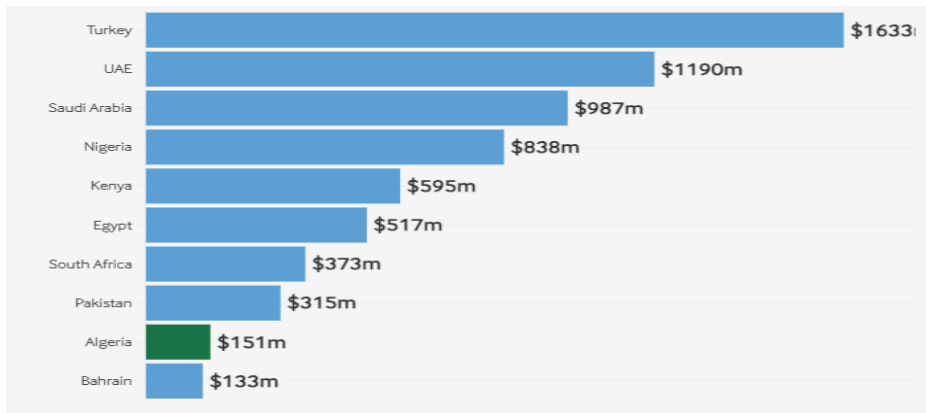
Institutions venture capital were a financial institution subject to the Cash and Loan Law 90-10 of 14 April 1990, Or it is a business that is subject to commercial law that has been dealt with under Law 06-11 which sets out the conditions and the way of establishing and operating a venture capital institution, Decree No. 93-10 of 23 May 1993 establishing the supervisory authority.

Act No. 06-11 refers to tax incentives provided to venture capital institutions.

Executive Decree No. 08-56 of February 2008 exempting venture capital institutions from paying tax on corporate profits. The remainder of the revenue is subject to a rate of 5 provided that the enterprise is obliged to maintain the invested funds for at least five years. (ninine , 2022)

405% in venture funding between 2021 and 2022, Algeria still lags many other emerging markets, including Egypt. And the next figure shows that.

Fig.11. venture capital funding in 2022



Source : (Alex, 2023).

4.2 Venture capital companies active in Algeria

There are many venture capital companies active in Algeria we can explain as following:

4.2.1 Financial Company of Investments SOFINANCE spa

SOFINANCE Spa, a Financial Company of Investments, Participations and Placement, is a public financial institution approved by the Bank of Algeria on January 9, 2001. It has a share capital of 10,000,000,000 DA.

SOFINANCE was created at the initiative of the National Council of State Participations (CNPE) with the main mission of supporting the modernisation of the national production tool and the development of new financial products. Its corporate purpose includes all the businesses developed by universal banking, excluding customer deposits and the management of means of payment.

Its scope covers financial activities such as:

- Leasing financing
- Equity participation
- Classic credit and commitments by signature
- Business advice and assistance. (sofinance.dz, 2023)

4.2.2 The Financier Algerian of Participation - FINALEP Spa-

A true pioneer of private equity in Algeria, FINALEP Spa is the first experience in this field.

The Financière Algérienne of Participation - FINALEP Spa (Ex. Financière Algéro-Européenne of Participation) was created on June 30, 1991, in the wake of the reforms undertaken in the Algerian banking and financial system to promote Private Equity.

Its share capital has seen several successive increases and adjustments to reach the level of 3,200,000,000 DA.

The FINALEP Spa operates throughout the national territory and contributes to the development of Small and Medium-sized Enterprise -SMEs, in particular, that have an industrial character.

The new strategic reorientation policy of FINALEP Spa and its redeployment in the sphere of the economic and financial landscape stems from its strong desire to position and strengthen its collaboration with its relations and partners.

The new strategy of FINALEP Spa is also reflected in its desire to distinguish its perception and distinction on an increasingly demanding economic relief and on which it exponentially strengthens the deployment of its commercial action, reflecting the evolution of its latest performance figures. (finalep.dz, 2023)

-The main objective of Finlep is to obtain social quotas by contributing to the capital of SMEs.

-It is therefore able to intervene in various stages of the company's life through the following forms:

- Venture capital
- Development Capital

In order to make contributions to corporate capital, Finalp can use its own funds as well as external resources: state investment funds established by public authorities, under the Supplementary Finance Act 2009 (finalep.dz, 2023)

Characteristics of Finalp's contribution portfolio:

- 64 % Entry into operation: Nearly 64% of the investments have returned to operations .The rest of the portfolio will be operational to a large extent during the 2023 financial year.
- 36% from start-ups: The FINALEP Spa portfolio is made up of 36% of participations at the creation stage (start-up), with the financing of certain unique projects.
- 87% Contributions made since 2016: The FINALEP Spa portfolio has been built up in a very sustained manner since the 2016 financial year, synonymous with a confirmed commercial and communication effort. (finalep.dz, 2023)

Fig.12. Finalp Contribution Portfolio.



Source: (<https://www.finalep.dz>).

4.2.3 The Algerian Saudi Investment Company (ASICOM)

The Algerian Saudi Investment Company (ASICOM) was created in 2008 by a signed agreement between the Kingdom of Saudi Arabia and Algeria. Its head office is in Algiers, Algeria. The declared capital is eight billion Algerian dinars (8 000 000 000 DZD - that is 75 000 000 USD) held equally and paid fully.

ASICOM intervenes in the promotion and financing of projects in all kinds of sectors. Its activities consist of:

- taking part in active or newly set up companies;
- Financing combined current accounts.

The company is managed by its Board of Directors, composed by six members, three Saudi nationalities and three Algerian ones. The Board is chaired by a Saudi member. The General Management is assured by an Algerian member. The Board of Directors meets at least quarterly and shall act on all investment operations. (asicom.dz, 2023)

4.3 The Challenges of venture capital companies in Algeria

The challenges of venture capital companies in Algeria are as follows:

- Venture capital firms do not have guarantee mechanisms Therefore, it does not cover the risks of its operations, which constitutes an obstacle to its expansion.
- Absence of appropriate exit mechanisms which is the most important determinant of the success of venture capital operations.
- shortage of specialized human resources Because this industry requires skills in all fields of legal and economic management
- Algeria's economic and financial culture depends primarily on indebtedness.
- No Professional Association for Investors.
- Weakness in potential customers of establishments with high preparations for technological growth.

- Lack of valuation of scientific research results and innovations (krivare, hassan , & barbri, 2022).

4.4 Conditions for the Success of the Venture Capital in Algeria

The conditions for the success of the venture capital in Algeria are as follows:

- Establishment of a securities market through which to trade the securities and shares of these companies.
- Promotion of the establishment of checks in Algeria regardless of its founder and nationality.
- Establish a centre to provide information to investors on all aspects of economic activity.
- Establishing training and research centres that finance and assist startups in evaluating investments and following up their activities.
- Seek to support partnerships with foreign Venture Capital institutions that possess high technology (krivare, hassan , & barbri, 2022)

5. Conclusion

Based on what has been studied through the various axes of this paper, it turns out that venture Capital is a type of financing that guarantees a capital for start-up enterprises. It is one of the most common types of funding in the Kingdom of Saudi Arabia. It is used as an effective and reliable means to achieve. Unprecedented growth in investment volume returns.

The presence of venture capital companies in Saudi Arabia is a major factor and the cause of the rapid growth of the country's venture capital sector. There are many venture capital companies in the country for example: Ventures grew, which can meet clients' capital needs in an integrated manner. The high value of transactions in the venture capital market is an indication of the existence of many high-value investment companies in the country. The presence

of venture capital companies in the State is therefore a key factor supporting the increasing spread of venture capital as a source of financing for local businesses.

-To work tirelessly to stimulate investment financing for start-ups and the Saudi Investment Company's bold commitment to invest in stimulating private investors to support start-ups so that they can grow rapidly and diversify the national economy.

-The Kingdom's launch of several government initiatives that stimulate the bold investment system within the framework of Vision 2030

-Growing numbers of active private investors and innovative entrepreneurs Developing a future vision of increasing the contribution to GDP to 35 by 2030.

This study also allowed us to learn about the most important obstacles and challenges facing venture capital in Algeria. Among these obstacles, we find the lack of a suitable investment climate that allows these companies to operate in Algeria.

The results of the study are:

▪ A venture capital is a well-known financing method in Saudi Arabia. Government programs and high investor expectations are major reasons for the spread of finance through bold, capital and increase its prominence and are the reason for the establishment of our funding fund in the name of Nama Ventures. The presence and increasing number of start-ups and investment companies, all of which lead to the growth and strengthening of the bold capital sector in Saudi Arabia.

▪ The venture capital in Algeria is still at the beginning it must provide the right climate for investment

Based on the foregoing and the results of the study, a set of recommendations can be proposed as follows:

- Establishment of a securities market through which to trade the securities and shares of these companies.

- Promotion of the establishment of checks in Algeria regardless of its founder and nationality.
- Establish a centre to provide information to investors in all aspects of economic activity.
- Establishing training and research centres that finance and assist startups in evaluating investments and following up their activities.
- Seek to support partnerships with foreign venture capital institutions that possess high technology.

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