Competitiveness and the State of Entrepreneurship in Saudi Arabia

Professor Michael E. Porter
Harvard Business School

January 27, 2009

This presentation draws on ideas from Professor Porter’s articles and books, in particular, The Competitive Advantage of Nations (The Free Press, 1990), “Towards a New Global Competitiveness Index,” in The Global Competitiveness Report 2008 (World Economic Forum, 2008), with S. Stern, M. Delgado, C. Ketels, “Clusters and the New Competitive Agenda for Companies and Governments” in On Competition (Harvard Business School Press, 1998), and ongoing research on clusters and competitiveness. No part of this publication may be reproduced, stored in a retrieval system, or transmitted in any form or by any means - electronic, mechanical, photocopying, recording, or otherwise - without the permission of Michael E. Porter. Further information on Professor Porter’s work and the Institute for Strategy and Competitiveness is available at www.isc.hbs.edu

Version: January 24, 2009, 3pm
State of Saudi Arabian Competitiveness

• Assessing the **competitive position** of Saudi Arabia in 2009
  – Progress over the last year

• Defining the **strategic agenda**

• Igniting **entrepreneurship** and **SME development**
Competitiveness and the Global Crisis

• Governments all over the world are focused on short-term crisis management

• Short-term actions will be most effective if they are tied to long-term competitiveness improvements

• The crisis offers an opportunity for making changes that are difficult during normal times
Prosperity Performance
Selected Countries

PPP-adjusted GDP per Capita, 2007

- USA
- Norway
- Qatar ($73,079)
- Ireland
- Singapore
- Taiwan
- Switzerland
- Germany
- Finland
- Taiwan
- France
- Spain
- Switzerland
- Austria
- Japan
- Netherlands
- Canada
- Australia
- Iceland
- Ireland
- Singapore
- China
- Pakistan
- Turkey
- Philippines
- Jordan
- Egypt
- Indonesia
- Sri Lanka
- India
- Vietnam
- Cambodia

Growth of Real GDP per Capita (PPP-adjusted), CAGR, 1998-2007

Source: EIU (2008), authors calculations
What is Competitiveness?

• Competitiveness depends on the **productivity** with which a nation uses its human, capital, and natural resources.
  
  – Productivity sets the **standard of living** (wages, returns on capital, returns on natural resources) that a country can sustain
  
  – It is not **what** industries a nation competes in that matters for prosperity, but **how productively** it competes in those industries
  
  – Productivity in a national economy depends on a **combination of domestic and foreign firms**
  
  – The productivity of **“local” or domestic industries** is fundamental to competitiveness, not just that of export industries

• Nations compete to offer the **most productive environment for business**

• The public and private sectors play **different but interrelated roles** in creating a productive economy
Comparative Labor Productivity
Selected Countries

GDP per employee (PPP adjusted US$), 2007

Note: In some cases 2006 data used where 2007 data unavailable.
Source: authors calculation, EIU (2009), Groningen Growth and Development Centre (2009)

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Labor Force Mobilization
Selected Countries

Employees as % of Total Population, 2007

Note: Use most recent year available, either 2007 or 2006

Source: The Conference Board and Groningen Growth and Development Centre, Total Economy Database, April 2008

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Foreign Direct Investment Flows
Saudi Arabia

FDI Flow (millions USD)

Inward FDI
Outward FDI

Saudi Arabia’s Export Share Trends
By Type of Product, 1991-2006

World Export Share (current USD)

- Processed Goods
- Semi-processed Goods
- Unprocessed Goods
- Services
- TOTAL (including unprocessed goods)

Source: UNComTrade, WTO (2008)
Average U.S. patents per 1 million population, 2003-2007

Innovative Capacity
Innovation Output, Selected Countries

Macroeconomic competitiveness creates the potential for high productivity, but is not sufficient. Productivity ultimately depends on improving the microeconomic capability of the economy and the sophistication of local competition.
Macroeconomic Competitiveness

Social Infrastructure and Political Institutions

- **Basic human capacity**
  - Basic education
  - Health system

- **Political institutions**
  - Political freedom
  - Voice and accountability
  - Political stability
  - Government effectiveness
  - Centralization of economic policymaking

- **Rule of law**
  - Judicial independence
  - Efficiency of legal framework
  - Business costs of corruption
  - Civil rights

Macroeconomic Policies

- **Fiscal policy**
  - Government surplus/deficit
  - Government debt

- **Monetary policy**
  - Inflation
  - Interest rate spread
Microeconomic Competitiveness: Quality of the Business Environment

- Local rules and incentives that encourage investment and productivity
  - e.g. performance based salaries, incentives for capital investments, intellectual property protection

- Vigorous local competition
  - Openness to foreign and local competition

- Sophistication of local customers and needs
  - Strict quality, safety, and environmental standards

- Many things matter for competitiveness
  - Successful economic development is a process of successive upgrading, in which the business environment improves to enable increasingly sophisticated ways of competing

- Access to high quality business inputs
  - Natural endowments
  - Human resources
  - Capital availability
  - Physical infrastructure
  - Administrative infrastructure (e.g. registration, permitting)
  - Scientific and technological infrastructure
  - Information and transparency infrastructure

- Demand Conditions

- Factor (Input) Conditions

- Related and Supporting Industries

- Context for Firm Strategy and Rivalry
Microeconomic Competitiveness: Cluster Development

Huston Oil and Gas Cluster

Upstream

Oil & Natural Gas Exploration & Development

Oil & Natural Gas Completion & Production

Downstream

Oil Transportation

Oil Trading

Oil Refining

Oil Distribution

Oil Wholesale Marketing

Oil Retail Marketing

Gas Gathering

Gas Processing

Gas Trading

Gas Transmission

Gas Distribution

Gas Marketing

Oilfield Services/Engineering & Contracting Firms

Equipment Suppliers
(e.g. Oil Field Chemicals, Drilling Rigs, Drill Tools)

Specialized Technology Services
(e.g. Drilling Consultants, Reservoir Services, Laboratory Analysis)

Subcontractors
(e.g. Surveying, Mud Logging, Maintenance Services)

Business Services
(e.g. MIS Services, Technology Licenses, Risk Management)

Specialized Institutions
(e.g. Academic Institutions, Training Centers, Industry Associations)
<table>
<thead>
<tr>
<th>Estimated Ranking:</th>
<th>2007</th>
<th>2008</th>
</tr>
</thead>
<tbody>
<tr>
<td>New Global Competitiveness Index</td>
<td>41</td>
<td>36</td>
</tr>
<tr>
<td>Macroeconomic Competitiveness</td>
<td>32</td>
<td>35</td>
</tr>
<tr>
<td>Microeconomic Competitiveness</td>
<td>53</td>
<td>36</td>
</tr>
<tr>
<td>GDP Per Capita Rank (ppp-adjusted)</td>
<td>36</td>
<td>36</td>
</tr>
</tbody>
</table>

Note: Rank versus 131 countries; overall, Saudi Arabia ranks 36th in 2008 PPP adjusted GDP per capita and 36th in Business Competitiveness.
Source: Institute for Strategy and Competitiveness, Harvard University (2009)
### Saudi Arabia’s Position

**Macroeconomic Competitiveness**

<table>
<thead>
<tr>
<th></th>
<th>2007</th>
<th>2008</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Estimated</strong> Macroeconomic Competitiveness Index</td>
<td>32</td>
<td>35</td>
</tr>
<tr>
<td>Social Infrastructure and Political Institutions</td>
<td>48</td>
<td>41</td>
</tr>
<tr>
<td>Macroeconomic Policy</td>
<td>20</td>
<td>27</td>
</tr>
</tbody>
</table>

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### Macroeconomic Competitiveness: Saudi Arabia

<table>
<thead>
<tr>
<th>Social Infrastructure and Political Institutions</th>
<th>Macroeconomic Policies</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Social policies have addressed poverty and basic <strong>social needs</strong>, but basic education and health remain weaknesses.</td>
<td>• Saudi Arabian macroeconomic polices are generally sound, but <strong>transparency</strong> remains limited.</td>
</tr>
<tr>
<td>• Political institutions are improving, but the <strong>predictability and transparency</strong> of reform is limited.</td>
<td>• The budget is exposed to swings in oil revenues, which leads to <strong>pro-cyclical fiscal policies</strong>.</td>
</tr>
<tr>
<td>• The Saudi legal system is improving, but <strong>fundamental reform</strong> is necessary.</td>
<td>• Inflation has risen, exposing weaknesses in <strong>monetary policy</strong>.</td>
</tr>
</tbody>
</table>
## Saudi Arabia’s Position
### Microeconomic Competitiveness

<table>
<thead>
<tr>
<th></th>
<th>2007</th>
<th>2008</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Estimated</strong> Microeconomic Competitiveness Index</td>
<td>53</td>
<td>36</td>
</tr>
<tr>
<td>National Business Environment</td>
<td>53</td>
<td>35</td>
</tr>
<tr>
<td>Company Operations and Strategy</td>
<td>54</td>
<td>38</td>
</tr>
</tbody>
</table>

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Source: Institute for Strategy and Competitiveness, Harvard University (2009)
# Saudi Arabia Competitiveness Strengths

<table>
<thead>
<tr>
<th>Macroeconomic competitiveness</th>
<th>2007</th>
<th>2008</th>
</tr>
</thead>
<tbody>
<tr>
<td>Government surplus/deficit</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td>(Low) Wastefulness of government spending</td>
<td>24</td>
<td>9</td>
</tr>
<tr>
<td>Public trust of politicians</td>
<td>22</td>
<td>17</td>
</tr>
<tr>
<td>Judicial independence</td>
<td>55</td>
<td>27</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Microeconomic competitiveness</th>
<th>2007</th>
<th>2008</th>
</tr>
</thead>
<tbody>
<tr>
<td>(Low) Brain drain</td>
<td>27</td>
<td>9</td>
</tr>
<tr>
<td>(Low) Impact of taxation on incentives to work and invest</td>
<td>8</td>
<td>12</td>
</tr>
<tr>
<td>Government procurement of advanced technology products</td>
<td>25</td>
<td>13</td>
</tr>
<tr>
<td>Flexibility of employment</td>
<td>7</td>
<td>15</td>
</tr>
<tr>
<td>Intellectual property protection</td>
<td>50</td>
<td>28</td>
</tr>
<tr>
<td>Production process sophistication</td>
<td>33</td>
<td>29</td>
</tr>
<tr>
<td>Cooperation in labor-employer relations</td>
<td>63</td>
<td>29</td>
</tr>
<tr>
<td>Quality of electricity supply</td>
<td>45</td>
<td>30</td>
</tr>
<tr>
<td>(Low) Time required to start a business</td>
<td>78</td>
<td>30</td>
</tr>
<tr>
<td>Quality of roads</td>
<td>38</td>
<td>31</td>
</tr>
<tr>
<td>Venture capital availability</td>
<td>39</td>
<td>32</td>
</tr>
<tr>
<td>Availability of scientists and engineers</td>
<td>57</td>
<td>35</td>
</tr>
</tbody>
</table>

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Ease of Doing Business
Saudi Arabia

Favorable

Unfavorable

Saudi Arabia per capita GDP rank: 32
Saudi Arabia Doing Business rank: 16
Saudi Arabia 2010 goal: 10

2007 Rank (Change) 24 (+8) 3 (+2) 6 (-1) 33 (+17) 49 (+25) 38 (+10) 44 (-1) 48 (-2) 82 (+25) 51 (-8) 136 (-1)

National Cluster Export Portfolio
Saudi Arabia, 1998-2006

Saudi Arabia’s Average World Export Share: 1.67%

Change in Saudi Arabia’s world export market share, 1998-2006

Exports of US$1.1 Billion = 1.5%
Saudi Arabia’s Average World Export Share: 1.67%

Note: Clusters with overlapping borders have at least 20% overlap (by number of industries) in both directions.
Saudi Arabian Business Environment

Progress in 2008

• Significant efforts underway to improve the **education system**, especially universities

• Recent reforms in the **financial sector**, but high volatility of the domestic market is a sign of immaturity

• Improvements in **business regulations**, but much remains to be done

• Improved availability of **ICT**

• Some progress on encouraging larger **presence of foreign companies** in the Saudi economy

• Some progress on **cluster development**, especially in areas related to oil and gas
### Saudi Arabian Competitiveness

#### Selected Weaknesses

<table>
<thead>
<tr>
<th>Category</th>
<th>2007</th>
<th>2008</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Human development</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Health expenditure</td>
<td>119</td>
<td>119</td>
</tr>
<tr>
<td>Quality of primary education</td>
<td>74</td>
<td>70</td>
</tr>
<tr>
<td><strong>Political institutions</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Voice and Accountability (WB)</td>
<td>127</td>
<td>126</td>
</tr>
<tr>
<td>Centralization of economic policymaking</td>
<td>72</td>
<td>54</td>
</tr>
<tr>
<td><strong>Role of Corporations</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(Low) Business costs of crime and violence</td>
<td>46</td>
<td>79</td>
</tr>
<tr>
<td>(Low) Business costs of corruption</td>
<td>83</td>
<td>50</td>
</tr>
<tr>
<td><strong>Macroeconomic policy</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Inflation</td>
<td>1</td>
<td>55</td>
</tr>
<tr>
<td><strong>IT infrastructure</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Internet access in schools</td>
<td>56</td>
<td>77</td>
</tr>
<tr>
<td>Fixed telephone lines</td>
<td>72</td>
<td>73</td>
</tr>
<tr>
<td>Internet users per 100 population</td>
<td>64</td>
<td>58</td>
</tr>
<tr>
<td><strong>Financial Markets</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Getting Credit Legal rights index</td>
<td>90</td>
<td>90</td>
</tr>
<tr>
<td>Regulation of securities exchanges</td>
<td>92</td>
<td>77</td>
</tr>
<tr>
<td><strong>Advanced Education</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Quality of math and science education</td>
<td>71</td>
<td>86</td>
</tr>
<tr>
<td>Quality of management schools</td>
<td>84</td>
<td>74</td>
</tr>
<tr>
<td>First year enrollment</td>
<td>73</td>
<td>73</td>
</tr>
<tr>
<td><strong>Regulation</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Regulatory quality</td>
<td>78</td>
<td>73</td>
</tr>
<tr>
<td><strong>Open Competition</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Prevalence of foreign ownership</td>
<td>116</td>
<td>98</td>
</tr>
<tr>
<td>Restrictions on capital flows</td>
<td>82</td>
<td>89</td>
</tr>
<tr>
<td>Business impact of rules on FDI</td>
<td>101</td>
<td>75</td>
</tr>
<tr>
<td>Market power of state-owned enterprises</td>
<td>79</td>
<td></td>
</tr>
<tr>
<td>Intensity of local competition</td>
<td>51</td>
<td>50</td>
</tr>
<tr>
<td><strong>Corporate Governance</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Efficacy of corporate boards</td>
<td>72</td>
<td>78</td>
</tr>
<tr>
<td>Strength of auditing and reporting standards</td>
<td>62</td>
<td>55</td>
</tr>
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Towards a Saudi Arabian Competitiveness Agenda

- Continue efforts on educational reform, including a stronger push on workforce development
- Make efficient capital provision to the private sector the central goal of financial market development
- Modernize corporate governance and reporting practices, especially in GLCs
- Shift the focus of business regulatory reform from discrete process improvements to improving the overall regulatory experience
- Use FDI attraction and the promotion of new business formation to challenge legacy market structures with little competitive pressure
- Create a comprehensive cluster development program to drive deeper competitiveness improvement and provide the structure for economic diversification
Clusters and Economic Diversification

- Upgrade the Quality and Efficiency of Existing Export Products and Services
- Upgrade Local Industries / Clusters
- Broaden Existing Clusters, (Including Resources Clusters)
- Build Clusters Around Strong MNCs
- Develop Related Clusters
- Invest in Enabling Conditions Where the Country Has Cluster Specific Advantages
- Build Positions in Clusters that are Strong in Neighboring Regions
Towards a Saudi Arabian Competitiveness Agenda

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- Unleash entrepreneurship and SME development
Emerging Companies and Competitiveness

Emerging companies:

• are a crucial driver of *competitiveness improvement*

• create *most of the new jobs* in advanced economies

• increase the *intensity of competition*

• are the *backbone of clusters*

Creating a *culture of entrepreneurship* in Saudi Arabia is a crucial priority
Entrepreneurship in Saudi Arabia
The Opportunity

• Large, youthful and growing population

• Growing markets with many undefended niches

• Stable economy with a prudent investment posture

• Modest income taxes

• Large and sustained government investments in the economy

• Increasing foreign interest in investing in the Middle East

• Emerging venture capital industry

• Opportunity to serve the entire region
Entrepreneurship in Saudi Arabia

Constraints

Culture
• Absence of an entrepreneurial culture

Skills
• Lack of a skilled Saudi workforce
• Absence of general and industry specific training programs for employees

Regulatory Processes
• Still cumbersome government regulation, red tape, and user experience

Infrastructure for Entrepreneurship
• Lack of program and supporting institutions for start-up and emerging companies
  – e.g, incubators, technical assistance, and entrepreneur networks
• Lack of public visibility and media coverage of emerging companies

Cluster Development
• Lack of supplier development programs at large companies
• Absence of cluster collaboration organizations providing support to SMEs
The State of Entrepreneurship in Saudi Arabia –
The Saudi Fast Growth 100

• In January 2008, at last year’s Global Competitiveness Forum, we committed to a process to identify entrepreneurial companies.

• SAGIA, AlWatan, and Next Economics set out to create the Saudi Fast Growth 25, which were the fastest growing, private companies in the Kingdom.

• Winners are ranked according to their revenue growth and each company goes through a rigorous qualification process.

• The list shines a spotlight on a new generation of companies that are creating jobs and spurring innovation and growth.

Instead of 25 fast growth companies, 95 companies qualified.
The Saudi Fast Growth 100

Fast Growth Companies  45
• 5 years and older
• Minimum of 4 million SAR (largest 3 billion SAR)
• 40% compound annual growth rate
• Created 15,000 jobs in the past 5 years

Fast Growth Start Up Companies  27
• Less than 5 years old
• 198% average growth from 2006 to 2007
• Minimum of 2 million SAR (largest 1.3 billion SAR)
• Winners are ranked according to their revenue growth and each company goes through a rigorous qualification process.

Fast Growth Companies to Watch  23
• Up and coming.
Saudi Fast Growth Companies
Facts & Figures

• Average entrepreneurial age at founding **32 years**

• There are **8 women founders**

• Winners are **100% college graduates**, half with master’s degrees

• More than half have founded **more than one company**

• About **25% plan to go public**

• **80% plan to launch another business in the next 2 years**

• Most common industries:  
  - High Tech & Telecom **23%**
  - Construction & Engineering **12%**
  - Health & Education **10%**
  - Management Consulting **10%**
Towards a Saudi Arabian Competitiveness Agenda

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- Move from 10 by 10 to a broader competitiveness strategy