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### EXPLORING THE POTENTIALS OF CROWD-FUNDING AS A NEW SOURCE OF FINANCE IN SAUDI ARABIA

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#### ABSTRACT

This work discusses the concept of the evolution of crowd funding and how suitable and feasible would crowd funding be in Saudi Arabia. Moreover, it analysis the strength, weakness, opportunities and threats of crowd funding comparing to other sources of finance for small and medium enterprise. This is done through a survey with 30 entrepreneurs who are in the process of startup as well as conducted interview with Professor in the Field of economics and management regarding this topic. The result of this research shows that there are Potentials of crowd funding to flourish in Saudi Arabia in the near future, but the lack of knowledge of the idea of crowd funding is limiting it from happening. However, still other sources of finance are demanded. Crowd funding is a complementary tool to other financial sources. This is mentioned in details under the section of findings.

#### INTRODUCTION:

Crowd Funding is a new concept that came into the business and it is a tool that can make entrepreneur who are in short of money to get funds from the society to startup their business [1]. This process is done through formal websites that links the initiators with the contributors. It is a new, fast; easy source of finance and that is because it only takes couple of minutes to write down the business idea, the capital needed and then post it online for people to see and contribute with any cent they can give if they liked the idea. When the target is reached, the amount is transferred to the initiator's account to collect and start up the business [2].

According to Rossi [3] there are 3 main sources of finance is commonly known, Bank instruments, stock market and angel investors. Recently, new phenomena of finance are emerging like crowd funding. The lack of cash flow can be a great barrier for many businesses to launch their projects. Since the funding is relied mainly on the crowd, the risk associated with the capital is diversified. There will be no losses if the business got bankrupt because the capital is not raised by one individual who bears the consequences like the traditional entrepreneurs but on the other hand is shared by the sum of the crowd who contributed, thus, the maximum loss for the each donator is the amount of fund he contributed. This adds value to the concept of crowd funding [4].

According to Drover [5], there are two main sources of financing, equity and debt. The main obstacle that can face entrepreneurs from growth is the lack of capital. Moreover, the major types of financial sources are, bank instruments for example bank loans, stock market, and private equity and angel investors. Lately, many entrepreneurs started to look for other types of raising capital through the Internet; this is not only support the use of technology but also it is an innovative way to communicate with customers (the contributors). Then, a new source of finance entered (Crowd funding) which can be done through pooling money from different people in order to support other peoples' investments [6].

Bradford [7] added that crowd funding could be the next revolution for small business to gain capital through small contributions because they can have access to everyone on earth. According to Howe [8], the power of the crowd is more efficient than a one single investor; he added that the wisdom of the crowd could help in building up the business and develop the idea before launching it. According to Crosetto, P et al. [9] crowd funding enhances the project in hand by refining it through different suggestions and point of views from the crowds before launching the project and customers would give evaluations of the project before investing, which limits business risks of any type and increases the change of success. Also, crowd funding serves as an advertising tool to the project. This is because it is a mean of informing customers (donators) that certain product/service does exist, which guarantees the existence of customers before launching the project. Moreover, since the willing of donation exists, this indicates a willing for purchasing the product/service. According to Agrawal [10] funding the project through relative or friends is considered one of the most easiest and safest sources of funds. According to Uddin [11], Islamic financing prohibit interest rate (Riba) because it is prohibited according to teaching of Islam. It also prohibits any financing/transaction of money to alcohol, tobacco, speculation and gambling. It also prohibits trading of debt, however, Islamic sources instead issue the Islamic bonds (Sukuk). There are many types of Islamic funding, Musharaka that is a joint venture arrangement, Mudaraba is profit sharing arrangement, Murabaha is a cost plus arrangement and Wadiah [11].

In a strong economy like Saudi Arabia, there is always a need for development of innovative sources of financing for youth and those who are willing to enter the business market. There are potentials for crowd funding that seems to be applicable. However, The problem is that in the gulf region and in Saudi Arabia specifically, the concept of Crowd Funding is new and many entrepreneur have little knowledge about this concept, they are not aware nor oriented that crowd funding might be a huge opportunity for them to start up their businesses. Thus in this work, the concept of the evolution of crowd funding and how suitable and feasible would crowd funding be in Saudi Arabia is presented. Moreover, it analysis the strength, weakness, opportunities and threats of crowd funding comparing to other sources of finance for small and medium enterprise.

## **METHODOLOGY**

### ***Research Hypothesis***

The research question will investigate the feasibility and suitability of crowd funding in Saudi Arabia through testing the following hypothesis. 1) Is crowd funding feasible and applicable in Saudi Arabia or not? 2) Why should Saudi entrepreneurs consider crowd funding as a new source of finance in Saudi Arabia. 3) Should crowd funding be considered as an innovative source of finance amongst other ways of funding projects in Saudi Arabia?. 4) Would crowd funding make a difference in the world of finance in Saudi Arabia?

### ***Method of Investigation***

The research combines primary and secondary sources of information. The researcher has followed a mixture of quantitative and qualitative methods to reach an understanding of crowd funding culture in Saudi Arabia. The primary sources of information is divided as Quantitative data and Qualitative data. In order to gain a valuable data to answer the research questions, a survey will be conducted to have a general view of sample's statistics, opinion and needs. This will help the researcher to gain a general knowledge of the market needs and to gain a base opinion of the entrepreneurs' needs. The secondary data stands as a supporting evidence for the research. Information was gathered from academic peer-reviewed journals and articles regarding the topic.

### ***Sample***

The sample for this work are Entrepreneurs who are in the process of starting up their business, SME startups. The target needed for the survey is 50 entrepreneurs who are in the process of starting up their own businesses.

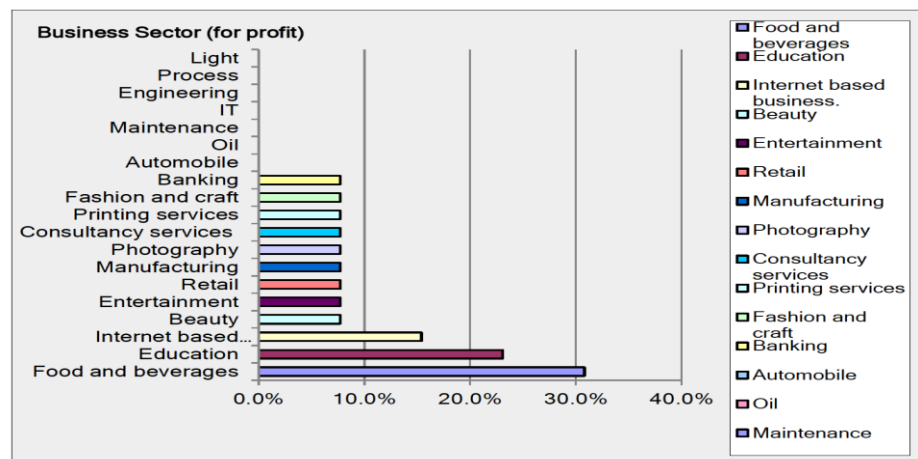
### ***Data Collection Tools***

The researcher used Survey Monkey advanced tools to collect the answers for the quantitative part of the research. Then the answers will be displayed in graphs that summarize the results to easily comprehend the answers.

**RESULT AND DISCUSSION**

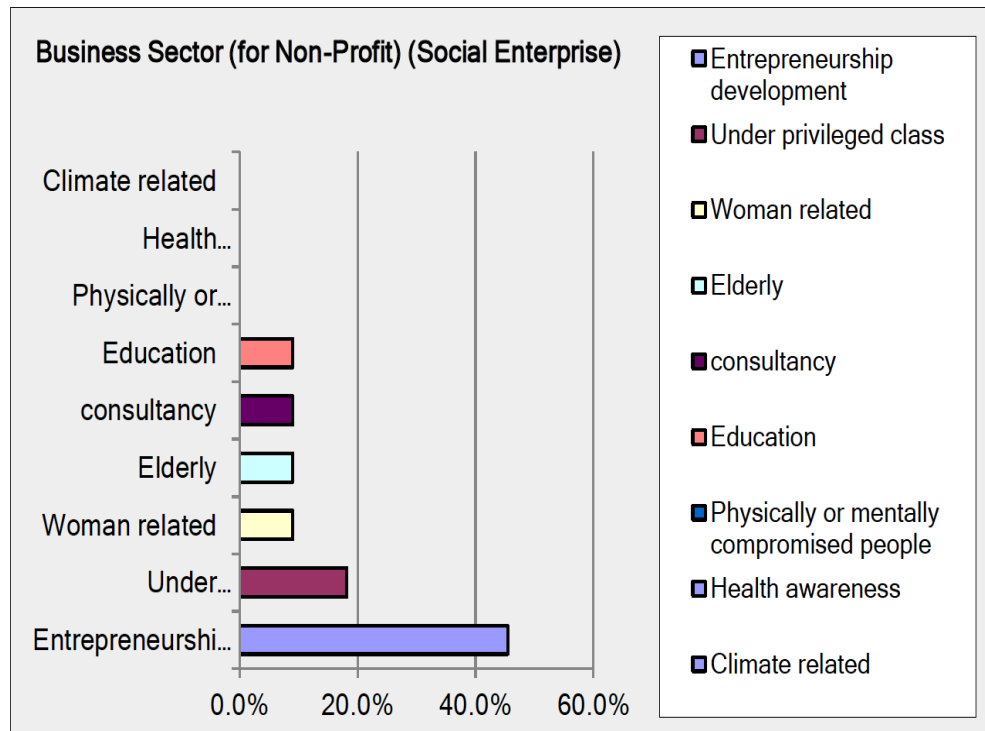
The survey has been conducted with entrepreneurs in the process of starting up through the vice general manager of Saudi Credit and saving bank in Saudi Arabia who put the researcher in contact with 30 entrepreneurs. One of the limits that faced the researcher is the target sample are Arabic native speakers so the researcher conducted the survey with 30 entrepreneurs whom are bi-lingual (Arabic and English speakers) because this research is done in the English language. Thus, this led the researcher to minimize the target sample to 30 entrepreneurs instead of 50.

Based on Figure 1, Business sector (For Profit), most of the entrepreneurs where launching their business in the industry of food and beverages. Education comes secondly. Then, Internet based businesses, then, the other sectors. However, none of the participants where investing in the Automobile, Oil, Maintenance, IT, Engineering, Light or process.



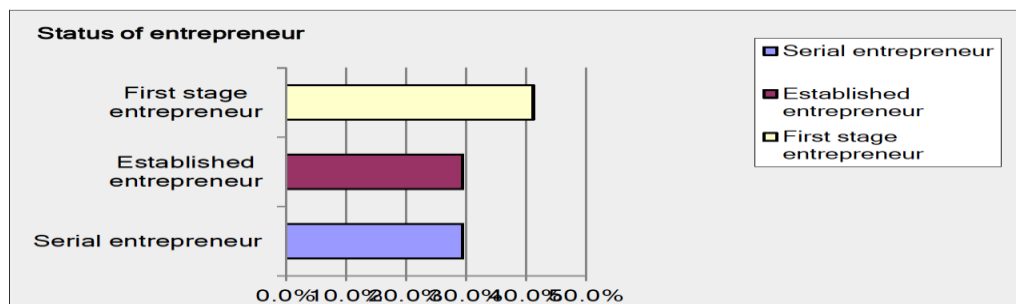
**Figure 1.** Business sector (For Profit)

Based on Figure 2, Business Sector (Non-Profit) (Social Enterprise, most of the entrepreneurs who made non-profit businesses invested in Entrepreneurship development sector. Then, the under privileged class, then women related, elderly, consultancy, education comes third. None of them were investing in the physically or mentally compromised people, nor health awareness nor climate related businesses



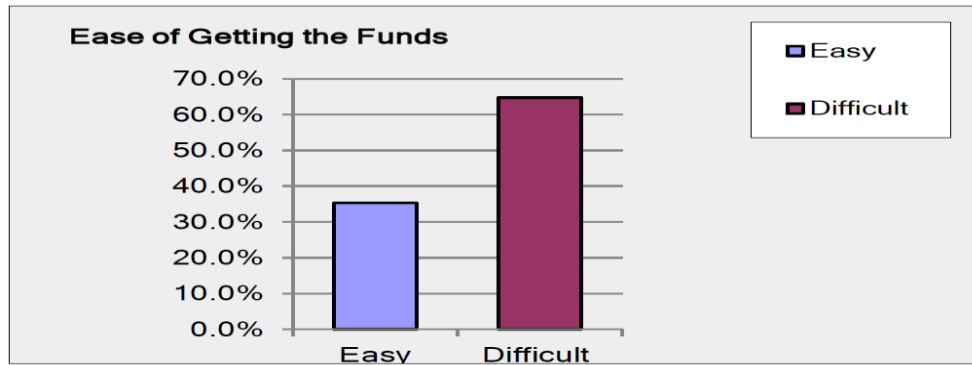
**Figure 2.** Business Sector (Non-Profit) (Social Enterprise)

Based on Figure 3, Status of entrepreneur: from the results above it is understood that most of the participants were launching their businesses for the first time. On the other hand, the other two figures represent established entrepreneurs and serial ones



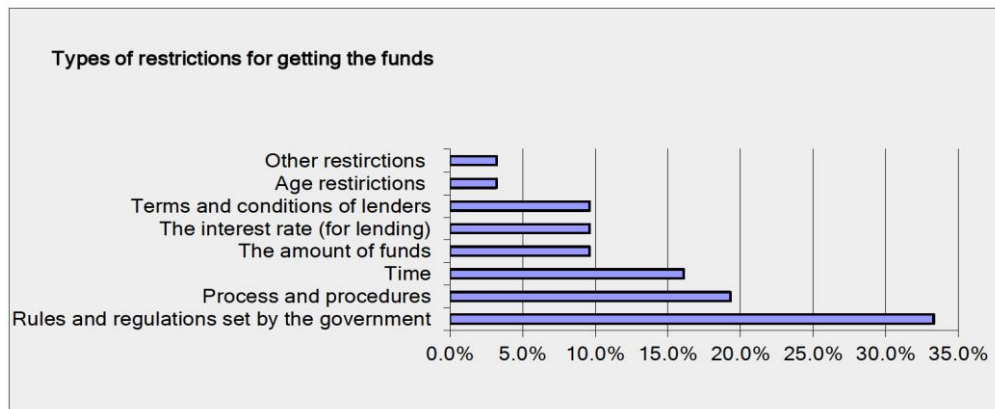
**Figure 3.** Status of entrepreneur

Based on Figure 4, Ease of getting the funds: most participants found that it is difficult to get funds with a present of 65%. However, still the other 35% found no difficulties



**Figure 4.** Status of entrepreneur

Based on figure 5, most of the participants found difficulties in getting the funds due to the rules and regulation that was set by the government. The second restrictions are from the process and procedures, and then participants faced difficulties of the long time that it takes to get the funds needed. The amount of funds, interest rate and terms and conditions were not a major problem. Finally, minority of the participants only faced restrictions for their age and other minor restrictions.



**Figure 5.** Types of restrictions for getting the funds

Based on Figure 6,; most of the entrepreneurs gained sufficient funds to establish their businesses as 53% reported so. In addition, based on Figure 7, the project cost varies from 1K to more than one million Riyals.

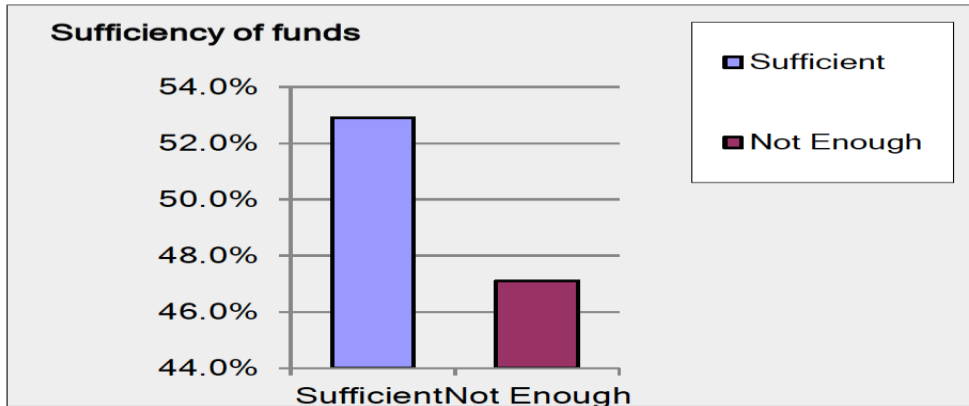


Figure 6. Sufficiency of funds

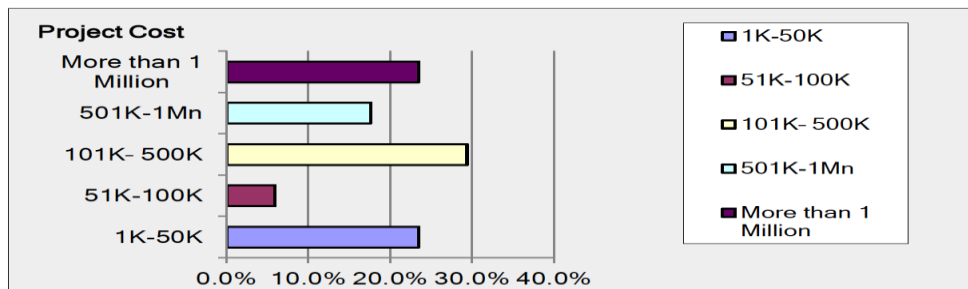
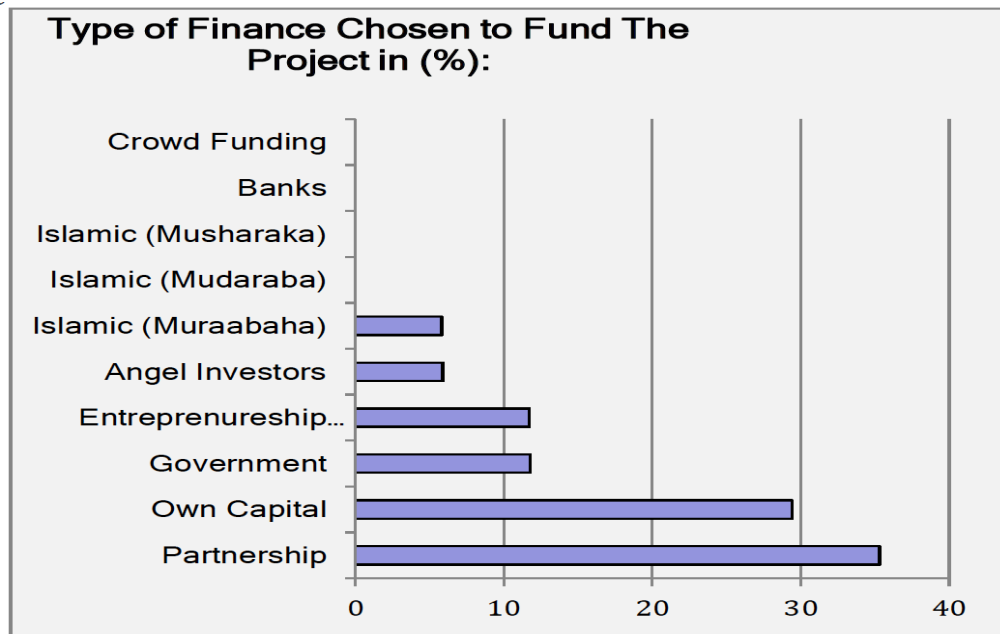


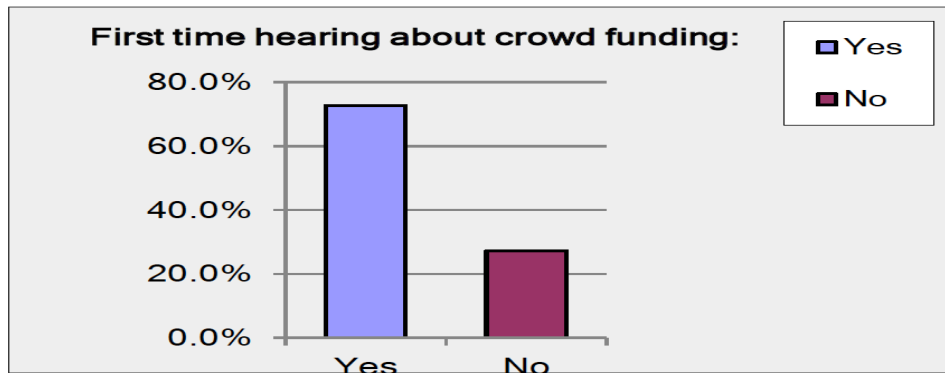
Figure 7. Project cost

Based on Figure 8, most of the participants joined a partnership to gain the capital needed, secondly, putting their own capital to the business. Third, they used the help of the government and entrepreneurship development agencies. Fourth, they used angel investors to support them with the capital needed and the Islamic Murabaha was chosen. None of the other participants chose Mudaraba, Musharaka, neither Banks nor Crowd funding. This indicates that crowd funding is not practiced in Saudi Arabia



**Figure 8.** Type of finance chosen to fund the project

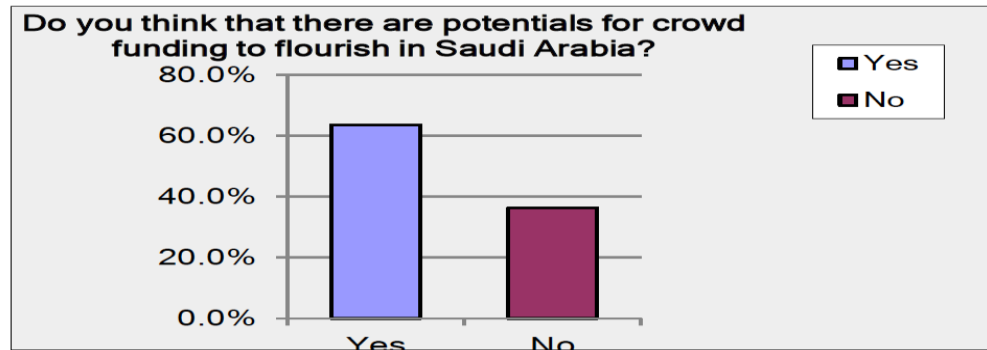
Based on Figure 9, most of the participants lack the knowledge of this source of funding by almost 75%. 25% have heard about the practice of crowd funding.



**Figure 9.** Awareness of Crowd Funding

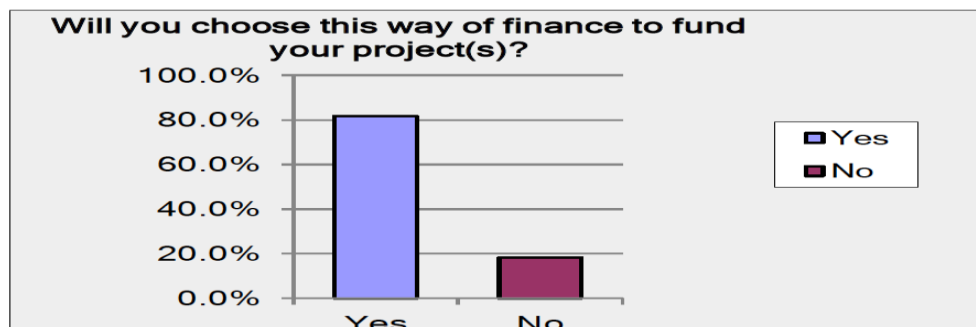
Based on Figure 10, majority of the entrepreneurs participated think that there are opportunity of crowd funding to grow in Saudi Arabia (65%). However, 35% of them think that crowd funding has no potential to grow because it is a new source to be implemented and it was not tested before and officially approved its success. It is a threat since it has not been implemented.





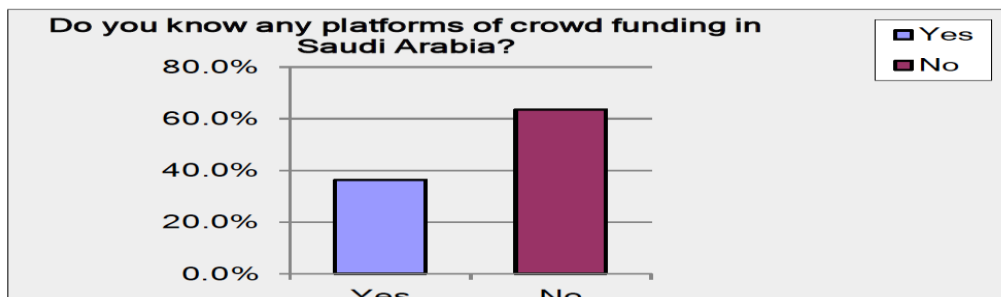
**Figure 10.** Potentials of Crowd funding to flourish in Saudi Arabia

Based on Figure 11, majority of the answers supports the idea of using crowd funding as a financial tool to establish businesses. This indicates the readiness of the crowd to use crowd funding



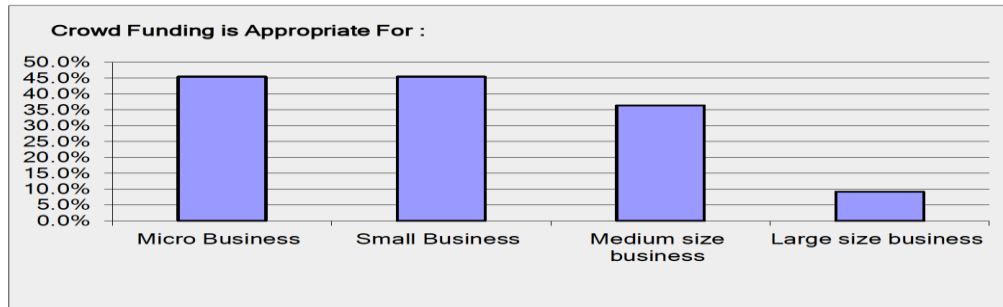
**Figure 11.** Using crowd funding as a financial tool.

Based on Figure 12, most of the participants have no idea of any crowd funding platforms available in Saudi Arabia by 60%. However, almost 40% know some crowd funding platforms but they either did not mention the name of the platforms or forgot the name.



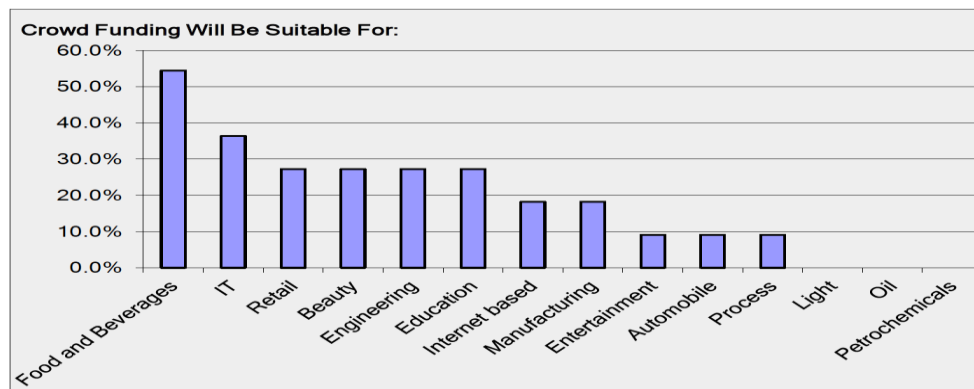
**Figure 12.** Knowledge of platforms of crowd funding in Saudi Arabia

Based on Figure 13, majority of the participants think that crowd funding is suitable for Micro and small and medium business.



**Figure 13.** Appropriateness of Crowd funding to Business Size

Based on Figure 14, majority of the answers think that food and beverages industry in Saudi Arabia is the most appropriate industry to be crowd funded. Then IT, then Retail, Beauty, Engineering, Education comes on the third ranks. Then, Internet based businesses and Manufacturing. Finally, Entertainment, Automobile and Process. Participants think that crowd funding is not suitable for the light, Oil and Petrochemicals.



**Figure 14.** Suitability of Crowd Funding to the types of industries

**CONCLUSION**

This research paper has discussed crowd funding evolution as an innovative way of funding in Saudi Arabia, highlighting its strength, weakness, opportunities and threats. The research started with an introduction to the concept of crowd funding in Saudi Arabia followed by deep analysis of the concept from different scholars point of views. Such claims were supported with quantitative and qualitative data to reach a holistic approach of the potentials of crowd funding and a general understanding of its practices in Saudi Arabia. It has been concluded from the results that crowd funding is a very important source of finance in any country to improve its economy. However, other sources of finance are essential and vital in the ecosystem of all the countries including Saudi Arabia. Moreover, the result of this research paper shows that there is a need of innovative sources of finance in Saudi Arabia and there is readiness to use such source of finance this refers to the entrepreneurs are willingness to use crowd funding in Saudi Arabia if available. However, a great deal of the lack of crowd funding availability and knowledge in Saudi Arabia is most probably caused by the lack in the role of media and the government to facilitate and introduce this source. This resulted

in the entrepreneurs' uncertainty of the success of crowd funding because the market of crowd funding was not tested before. This research paper proves that the lack of knowledge of this source of finance can be a great opportunity to test and apply crowd funding in a new market like Saudi Arabia. In Addition, From the literature, it can be seen that crowd funding found a great deal of success wherever it was applied, this can be a chance to crowd funding to take its place in Saudi Arabia and to make a difference for entrepreneurs and the economy of the Saudi Arabia.

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