GOING PUBLIC IN SAUDI ARABIA: MOTIVATIONS AND BARRIERS

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Abstract

We set out to examine the motivations of going public and barriers to go public in Saudi Arabia. To accomplish this, we conducted a questionnaire survey. The questionnaire was sent to the largest 500 firms in the Kingdom. The results revealed that firms go public to use the money raised for more growth and expansion and to be more competitive. Moreover, decision makers in private firms are reluctant to go public because of the failure of many Joint Stock Companies, listed in the SSM, to generate profits.

1. Introduction

Recently, a lot of talks have been taken place in the Kingdom about increasing the number of Joint Stock Companies. Academics, business persons, and government officials are trying to find what could motivate the private firms to make Initial Public Offerings (IPOs) and also what could prevent them from doing so? These two issues are covered and studied in this paper by conducting a mail questionnaire.

It has been found that firms make this important decision for strategic and personal reasons. Respondents think firms go public to finance their current and future projects, to be able to compete more, and to merge or acquire with others. Furthermore, respondents believe firms make IPOs to give original owners the capacity to liquidate and diversify part of their investments more easily and solve the problem of lack of family succession and control.

The paper is organised as follows. Section 2 gives a selective review of recent work on the decision to list, section 3 discusses the results obtained from the questionnaire, and section 4 is the conclusion.

2. The Benefits and Costs of Going public

As any other decision, the decision of going public has its advantages and disadvantages. When a company listed in the stock market, it will have access to new finance sources, with concomitant improved prospects for growth and expansions (Ransley, 1984), (Jain and Kini, 1994), (McConaughy et al, 1995), (Rydqvist and Högholm, 1995), (Holthausen and Larcker, 1996), (Mikkelson et al, 1997), (Kutsuna et al, 2002), and (Kim et al, 2002). Access to security markets may reduce the cost of credit (Rajan, 1992) and (Pagano et al, 1998). When the shares of a company are publicly traded, the owners can easily liquidate and diversify their investment by trading in the stock market (Ransley, 1984), (Jenkinson and Espenlaub, 1991), (Pagano, 1993), (Rydqvist and Högholm, 1995), (Brennan and Franks, 1997), (Cai and Wei, 1997), (Mikkelson et al, 1997), and (Kutsuna el al, 2002). Moreover, going public gives IPOs an opportunity to offer vendors, suppliers, and employees stock or stock options, giving these individuals a stake in the company's success and a reason to act to advance that success (Ransley, 1984), and (Hare, 1994). Being open to public scrutiny, public companies tend to be better known and are likely to be accepted more easily as trustworthy and dependable. The reputation and visibility they gain as public companies can help them to win customers, secure financing, or expand from a regional company to a national one (Ransley, 1984), and (Rydqvist and Högholm, 1995). In addition, Companies can use the money raised from selling the stock to outsiders to pay their debt (Mikkelson et al, 1997), and (Pagano et al, 1998).

On the other hand, by going public, the founders might loss the control of the company and become no longer the decision players (Rydqvist and Högholm, 1995), (Zingales, 1995), (Cai and Wei, 1997) (Mikkelson et al, 1997), and (Pagano et al, 1998). By listing in the stock market, the companies have to disclose more information about their financial and managerial status (Choi, 1973), (Campbell, 1979), (Firth, 1979), (Leftwich et al, 1981), (Ransley, 1984), (Cooke, 1992), (Malone et al, 1993), (Wallace et al, 1994), (Yosha, 1995), and (Pagano et al, 1998). Finally, there are a great amount of direct costs (underwriting fees, accounting and consulting fees, register fees, etc.) associated with going public. Underwriters typically take at least 7% of gross proceeds (Lee, Lochhead, Ritter, and Zhao, 1996), and (Ritter, 1998).

3. Results from the Questionnaire

3.1 The Response Rate

151 firms responded from 500. Three companies mailed letters excusing themselves from answering the questionnaire. In addition, three questionnaires were excluded by the researcher because there were too many questions left unanswered. Therefore, there are now 145 usable questionnaires (29% response rate). 89 questionnaires were received before the follow up letters, some telephone calls, and some visits by the researcher and 56 responses were received after the follow up letters, some telephone calls and some visits by the researcher.

3.2 Testing Responses' Representativeness

All received questionnaires were checked and inspected for representativeness of the selected sample of 500 firms. The frequency and percentage presented in table 1 give a clear indication that the sample used in this study neither suffer from sector bias nor legal status bias. To ensure the sample does not exhibit significant bias, chi-square test ($\mathbf{X^2}$) was employed on the distribution of the original sample (500 Firms) and the set of usable responses (145 Firms) to test the hull hypothesis that there are no statistically significant differences. The chi-square results, in also table 1, show there are no significant differences between the original sample and the usable sample for both the Sector and legal status. The p-values for the sector and legal status are greater than 0.05 meaning that the hull hypothesis can not be rejected. Therefore, it can be concluded that participated sample is representative of the original and the results can be generalised.

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Table 1 Comparison between the Original Sample and the Sample Used in this Study and Chi-square Test Results of Differences between them According to Firms' Sector and Legal Status

Category		Original Sample		Participated		Test Results	
		No.	%	No.	%	X^2	P-Value
Firms' Sector	Agriculture	28	5.6%	7	4.8%	1.22	0.99
	Contracting	36	7.2%	8	6.2%		
	Trading	98	19.6%	22	18.6%		
	Financing	18	3.6%	6	4.1%		
	Services	72	14.4%	18	12.4%		
	Manufacturing	87	17.4%	33	18.6%		
	Diversified	161	32.2%	51	35.2%		
	Total	**500**	**100%**	**145**	**100%**		
Firms' Legal Status	Sole Proprietorship	146	29.2%	40	27.6%	0.90	1.00
	Partnership	25	5.0%	10	6.9%		
	Liability Partnership	21	4.2%	7	4.8%		
	Limited Liability	231	46.2%	64	44.1%		
	Joint Stock	77	15.4%	24	16.6%		
	Total	**500**	**100%**	**145**	**100%**		

X^2 is chi-square result

3.3 The Characteristics of the Respondents and their Firms

The results from part one in the questionnaire were summarised in table 2 and complete frequencies and percentage of participants and their firms are presented. 42.8% of the participants are from 41 to 50 years old, and 84.8% are Saudis.

65.5% are the presidents and 17.9% are the vice president of their firms. This mean that the great majority of the respondents is from the top management which is so desirable for this study since the going public decision is a strategic one and it is made by the top management. Moreover, most of participants are well-educated and specialised in business studies since 95% are holding undergraduate and postgraduate degrees, and 70.1% hold a degree in business studies.

Table 2 also shows that the highest number of respondents came from firms working in more than one sector (35.2%), then both the trading and the manufacturing sectors (18.6%), followed by the service sector (12.4%).

In addition, 44.1% are Limited Liability, 27.6% are Sole Proprietorship, 16.6% Joint Stock, 6.9% are Partnership, and 4.8% are Limited Liability Partnership. As seen, the private companies, which are in the position to go public, are the most (83.4%) while the rest are Joint Stock Companies which, however, have been included because they may made an IPO so they would have better knowledge about the issue.

Table 2 Summary Statistics of the Participants' Background and the Characteristics of their Firm

Category		No.	%
Participants' Age	Less than 30 years	10	6.9%
	From 30 to 40 years	43	29.7%
	From 4١ to 50 years	62	42.8%
	From 5١ to 60 years	20	13.8%
	More than 60 years	10	6.9%
	Total	**145**	**100%**
Participants' Nationality	Saudi	123	84.8%
	Other Nationalities	22	15.2%
	Total	**145**	**100%**
Participants' Position	President (Manager)	95	65.5%
	Vice President	26	17.9%
	Financial Manager	12	8.3%
	Other positions	12	8.3%
	Total	**145**	**100%**
Participants' Level of Education	Less than Bachelor Degree	7	4.8%
	Bachelor Degree	86	59.3%
	Postgraduate Degree	52	35.9%
	Total	**145**	**100%**
Participants' Field of Study	Business Studies	101	70.1%
	Other Studies	43	29.9%
	Total	**144**	**100%**
Firms' Sector	Agriculture	7	4.8%
	Contracting	9	6.2%
	Trading	27	18.6%
	Financing	6	4.1%
	Services	18	12.4%
	Manufacturing	27	18.6%
	Diversified	51	35.2%
	Total	**145**	**100%**
Firms' Legal Status	Sole Proprietorship	40	27.6%
	Partnership	10	6.9%
	Liability Partnership	7	4.8%
	Limited Liability	64	44.1%
	Joint Stock	24	16.6%
	Total	**145**	**100%**
Firms' Age	Less than 10 years	6	4.1
	From 10 to 20 years	28	19.3
	From 21 to 30 years	51	35.2
	From 31 to 40 years	32	22.1
	More than 40 years	28	19.3
	Total	**145**	**100%**
Number of Employees	Less than 500 employees	63	43.4%
	From 500 to 1000 employees	61	42.1%
	More than 1000 employees	21	14.5%
	Total	**145**	**100%**

Furthermore, table 2 illustrates that 35.2% of the firms are from 21 to 30 years old and 22.1% are from 31 to 40 years old. This is not surprising since it is correlated with the sharp increased of oil prices in the 1970s which had a strong positive effect on the Saudi economy. Lastly, 43.4% of participated firms employ less that 500 personnel, 42.1% have from 500 to 1000 employees, and 14.5% conduct their business with more that 1000 personnel.

3.4 The Motivations of Going Public in Saudi Arabia

In part two, question nine, in the questionnaire, asked participants about the possible motivations which would encourage the decision makers in the private firms to take their companies public. Twenty-eight possible motivations were listed and the participants expressed their opinions by using the 5-point Likert scale, 1= strongly disagree and 5= strongly agree.

Table 3 illustrates the rank, means, standard deviations, and coefficient of variations, of all possible motivations for going public in Saudi Arabia. The motivation "companies go public to use the money raised for more expansions and growth" has the highest level of agreement between respondents (4.255 mean, 0.632 S.D and 0.149 C.V), then "companies go public to be more competitive" is ranked the second motivation with 4.111 mean, 0.701 S.D, and 0.171 C.V. The third most agreeable motivation of going public is "original owners take their companies public to diversify part of their investment" with 4.103 mean, 0.779 S.D, and 0.190 C.V. The forth motivation is "original owners take their companies public to solve the problem of lack of family succession and control" with 3.979 mean, 1.017 S.D, and 0.256 C.V. "Original owners take their companies public to liquidate part of their investment" is ranked the fifth motivation of going public (3.828 mean, 0.960 S.D, and 0.251 C.V). The respondents rank "companies go public to acquire and merge with other companies" as the sixth motivation (3.641 mean, 0.984 S.D, and 0.270 C.V), and "companies go public to enhance the company image and publicity" as the seventh motivation (3.628 mean, 1.093 S.D, and 0.301 C.V).

However, on the other hand, table 3 shows that some motivations are not supported by the participants. For example, "companies go public to enhance the employee" status has only mean score of 2.678.

In addition, table 4 shows the percentage of responses regarding the motivations of going public in Saudi Arabia. 94% of the respondents agree and strongly agree and none of them strongly disagree with "companies go public to use the money raised for more expansions and growth", 89% of the respondents agree and strongly agree with "companies go public to be more competitive", 87% of the respondents agree and strongly agree with "original owners take their companies public to diversify part of their investment", 74% of the participants agree and strongly agree with "original owners take their companies public to solve the problem of lack of family succession and control", and 74% of the participants agree and strongly agree with "original owners take their companies public to diversify part of their investment".

It is obvious from table 3 and 4 that the decision to go public is driven by economical motivations "maximise the owners wealth".

Table 3 Rank, Means, Standard Deviations (S.D), and Coefficient of Variations (C.V) of the Motivations of Going Public in Saudi Arabia

Motivations	Rank	Mean	S.D	C.V
Companies go public to use the money raised for more expansions and growth	1	4.255	0.632	0.149
Companies go public to be more competitive	2	4.111	0.701	0.171
Original owners take their companies public to diversify part of their investment	3	4.103	0.779	0.190
Original owners take their companies public to solve the problem of lack of family succession and control	4	3.979	1.017	0.256
Original owners take their companies public to liquidate part of their investment	5	3.828	0.960	0.251
Companies go public to acquire and merge with other companies	6	3.641	0.984	0.270
Companies go public to enhance the company image and publicity	7	3.628	1.093	0.301
Companies go public when there is sharp stock price increase	8	3.586	1.045	0.291
Companies go public when they are overvalued by outside investors	9	3.497	1.094	0.313
Companies go public to attract well qualified personal	10	3.486	1.147	0.329
Companies go public because the competition in their market is severe	11	3.476	1.131	0.325
Companies go public to be recognised by investors	12	3.469	1.155	0.333
Companies go public to make firm's products better known	13	3.448	1.124	0.326
Companies go public to establish a value for the firm	14	3.421	1.229	0.359
Original owners take their companies public to overcome the conflicts accruing between the owners about the leadership	15	3.401	1.305	0.384
Firms go public because the government grants more subsidies to Joint Stock Companies	16	3.214	1.18	0.367
Companies go public because there are few resources of finance	17	3.182	1.052	0.331
Firms go public because the government allowed the G.C.C citizens to own stocks in the Saudi Stock Market (SSM)	18	3.152	1.114	0.353
Companies go public to use the money raised to pay their debt	19	3.131	1.056	0.337
Firms go public because the government allowed the foreign investors to participate in the SSM through special funds established by commercial banks	20	3.056	1.118	0.366
Companies go public to improve credit rating	21	3.000	1.088	0.363
Companies go public to motivate and create incentive to the management and employees	22	2.965	1.08	0.364
Companies go public to avoid bankruptcy	23	2.944	1.226	0.416
Original owners take their companies public when they know that the profitability is about to decline permanently (time their offerings with high performance to sale their share with higher price)	24	2.869	1.18	0.411
Firms go public because the government reduced the Tax Income rate	25	2.845	1.119	0.393
Companies go public to evaluate and monitor management and employees	26	2.841	1.097	0.386
Firms go public because the government eases the procedures for going public	27	2.778	1.087	0.391
Companies go public to enhance the employee status	28	2.678	1.085	0.405

"Companies go public to use the money raised for more expansions and growth' came as the most agreeable (highest mean, lowest S.D and lowest C.V) motivation of going public. This is not surprising result since this finding is consistent with other findings conducting in other countries (see literature review chapter). One possible explanation for this result is that Saudi Arabia is a growing country in many aspects. First, it is a large country and has one of the highest population growth rate in the world, increasing by an estimated 4.0% per year.

Second, most of the cities and towns are also growing so rapidly. Thus, businesses operating in the Kingdom try to be reachable and present in every possible part of the country.

Table 4 the Percentage of Responses Regarding the Motivations of Going Public in Saudi Arabia

Motivations	**1**	**2**	**3**	**4**	**5**
Companies go public to use the money raised for more expansions and growth	0%	2%	4%	60%	34%
Companies go public to be more competitive	0%	4%	7%	63%	26%
Original owners take their companies public to diversify part of their investment	1%	4%	9%	57%	30%
Original owners take their companies public to solve the problem of lack of family succession and control	1%	12%	13%	39%	36%
Original owners take their companies public to liquidate part of their investment	0%	15%	10%	51%	23%
Companies go public to acquire and merge with other companies	4%	11%	15%	57%	13%
Companies go public to enhance the company image and publicity	1%	21%	10%	49%	19%
Companies go public when there is sharp stock price increase	1%	22%	10%	45%	21%
Companies go public when they are overvalued by outside investors	3%	17%	15%	48%	17%
Companies go public to attract well qualified personal	6%	15%	19%	46%	15%
Companies go public because the competition in their market is severe	3%	25%	13%	40%	19%
Companies go public to be recognised by investors	1%	27%	15%	37%	20%
Companies go public to make firm's products better known	4%	22%	13%	45%	16%
Companies go public to establish a value for the firm	9%	15%	21%	34%	21%
Original owners take their companies public to overcome the conflicts accruing between the owners about the leadership	11%	17%	18%	30%	24%
Firms go public because the government grants more subsidies to Joint Stock Companies	10%	23%	11%	48%	8%
Companies go public because there are few resources of finance	3%	30%	22%	36%	9%
Firms go public because the government allowed the G.C.C citizens to own stocks in the Saudi Stock Market (SSM)	10%	22%	16%	48%	4%
Companies go public to use the money raised to pay their debt	3%	30%	27%	30%	10%
Firms go public because the government allowed the foreign investors to participate in the SSM through special funds established by commercial banks	11%	23%	22%	40%	5%
Companies go public to improve credit rating	9%	24%	35%	24%	8%
Companies go public to motivate and create incentive to the management and employees	5%	38%	19%	30%	8%
Companies go public to avoid bankruptcy	11%	32%	20%	25%	12%
Original owners take their companies public when they know that the profitability is about to decline permanently (time their offerings with high performance to sale their share with higher price)	8%	40%	17%	30%	6%
Firms go public because the government reduced the Tax Income rate	11%	36%	18%	28%	8%
Companies go public to evaluate and monitor management and employees	13%	28%	26%	28%	5%
Firms go public because the government eases the procedures for going public	13%	31%	24%	31%	2%
Companies go public to enhance the employee status	13%	41%	15%	31%	1%

1 = strongly disagree, 2 = disagree, 3 = neither agree nor disagree, 4 = agree, and 5 = strongly agree

3.5 The Barriers to Go Public in Saudi Arabia

The participants were asked in part two, question ten, in the questionnaire about the possible barriers which would reduce the rate of going public in the Kingdom. Twenty-two possible barriers were listed and the participants stated their views by using the 5-point Likert Scale, 1= strongly disagree and 5= strongly agree.

Table 5 shows the rank, means, standard deviations, and coefficient of variations, of all possible barriers to go public in Saudi Arabia. "The failure of many Joint Stock Companies, listed in the SSM, to generate profits" is ranked the first agreeable barrier in the Kingdom (4.028 mean, 0.971 S.D and 0.241 C.V), then "owners avoid going public because of the possible loss of control" is ranked the second highest barrier with 3.821 mean, 1.065 S.D, and 0.279 C.V. The third most agreeable constrain reducing the rate of IPOs is "fear of more restrictions on the private transactions" scored mean of 3.655, S.D of 1.057, and C.V of 0.289. "Stock market is not open completely for international investors" is ranked the fourth highest barrier in the Kingdom (3.594 mean, 1.115 S.D and 0.310 C.V), then "unwelcome attention regarding a possible takeover" is ranked the highest fifth barrier with 3.559 mean, 1.079 S.D, and 0.303 C.V.

Furthermore, participants rank the barrier "there is no complete financial system" as the sixth highest constrain with 3.462 mean, 1.213 S.D, and 0.350 C.V, and "restrictive regulations from Ministry of Commerce for companies willing to convert into a Joint Stock Company" as the seventh highest constrain with 3.400 mean, 1.151 S.D, and 0.339 C.V.

Moreover, table 6 shows the percentage of responses regarding the barrier to go public in Saudi Arabia. 78% of respondents agree and strongly agree and none of them strongly disagree with that firms do not go public because of "the failure of many Joint Stock Companies, listed in the SSM, to generate profits".

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Table 5 Rank, Mean, Standard Deviation (S.D), and Coefficient of Variation (C.V) of the Barriers to Go Public in Saudi Arabia

Barriers	Rank	Mean	S.D	C.V
The failure of many Joint Stock Companies, listed in the SSM, to generate profits	1	4.028	0.971	0.241
Owners avoid going public because of the possible loss of control	2	3.821	1.065	0.279
Fear of more restrictions on the private transactions	3	3.655	1.057	0.289
Stock market is not open completely for international investors	4	3.594	1.115	0.310
Unwelcome attention regarding a possible takeover	5	3.559	1.079	0.303
There is no complete financial system	6	3.462	1.213	0.350
Restrictive regulations from Ministry of Commerce for companies willing to convert into a Joint Stock Company	7	3.400	1.151	0.339
The lack of experience about the legal and financial points related to the IPO	8	3.345	1.139	0.341
More disclosure requirements	9	3.338	1.075	0.322
The difficulty of determining the real value of the firm	10	3.264	1.177	0.361
The ambiguity in regulations that cover fundamental IPO issues	11	3.241	1.101	0.340
External investor scrutiny	12	3.146	1.223	0.389
Fear that the offer price might be less than market price in the first day	13	3.145	1.099	0.349
Liquidity in the Saudi Market is limited	14	3.139	1.210	0.385
Dividend pressure	15	3.138	1.116	0.356
Restricted regulations from the Department of Zakat and Income Tax	16	3.090	1.073	0.347
Expenses and Fees associated with the procedures of going public are high	17	2.958	0.981	0.332
Fear of the increase of agency costs	18	2.862	1.058	0.370
Owners avoid going public because of the possible negative impacts on their relationships with managers and employees	19	2.848	1.198	0.421
There are few underwriters in the country	20	2.834	1.137	0.401
The lack of well experienced personnel who can manage companies after transition	21	2.690	1.071	0.398
Tax Income rate is high	22	2.607	0.967	0.371

72% of the respondents agree and strongly agree with "owners avoid going public because of the possible loss of control", 68% of the respondents agree and strongly agree with that firms do not go public because of "fear of more restrictions on the private transactions", 66% of the participants agree and strongly agree with that firms do not go public because "stock market is not open completely for international investors", 72% of the participants agree and strongly agree with that firms do not go public because of "unwelcome attention regarding a possible takeover", 56% of the participants agree and strongly agree with that firms do not go public because "there is no complete financial system", and 52% of the participants agree and strongly agree with that firms do not go public because of "restrictive regulations from Ministry of Commerce for companies willing to convert into a Joint Stock Company".

Table 6 the Percentage of Responses Regarding the Barriers to Go Public in Saudi Arabia

Barriers	1	2	3	4	5
The failure of many Joint Stock Companies, listed in the SSM, to generate profits	0%	12%	10%	41%	37%
Owners avoid going public because of the possible loss of control	4%	9%	15%	44%	28%
Fear of more restrictions on the private transactions	3%	17%	12%	49%	19%
Stock market is not open completely for international investors	6%	14%	15%	47%	19%
Unwelcome attention regarding a possible takeover	5%	18%	6%	59%	13%
There is no complete financial system	3%	27%	13%	33%	23%
Restrictive regulations from Ministry of Commerce for companies willing to convert into a Joint Stock Company	6%	17%	25%	34%	18%
The lack of experience about the legal and financial points related to the IPO	6%	21%	17%	42%	13%
More disclosure requirements	3%	26%	13%	48%	10%
The difficulty of determining the real value of the firm	4%	30%	18%	31%	17%
The ambiguity in regulations that cover fundamental IPO issues	3%	29%	23%	31%	14%
External investor scrutiny	10%	27%	10%	43%	10%
Fear that the offer price might be less than market price in the first day	3%	32%	21%	32%	11%
Liquidity in the Saudi Market is limited	6%	35%	11%	35%	13%
Dividend pressure	8%	27%	16%	43%	6%
Restricted regulations from the Department of Zakat and Income Tax	6%	27%	30%	28%	10%
Expenses and Fees associated with the procedures of going public are high	4%	32%	38%	19%	8%
Fear of the increase of agency costs	7%	39%	18%	32%	3%
Owners avoid going public because of the possible negative impacts on their relationships with managers and employees	11%	38%	15%	27%	9%
There are few underwriters in the country	7%	44%	17%	23%	9%
The lack of well experienced personnel who can manage companies after transition	11%	41%	18%	27%	3%
Tax Income rate is high	10%	37%	39%	8%	6%

1 = strongly disagree, 2 = disagree, 3 = neither agree nor disagree, 4 = agree, and 5 = strongly agree

4. Conclusion

The key objective of this study was to investigate two axes of going public issues. This study revealed the motivations of going public, and the barriers to go public. The findings and results of this study can be summarised as follows. First, companies are motivated to go public to use the money raised for more expansion and growth and to be more competitive. Second, private firms in the Kingdom are reluctant to go public because of the failure of many joint stock companies listed in the Saudi Stock Market to generate profit and also because of the possible loss of control.

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