

Challenges of the Startup Ecosystem in Pakistan

Prepared by

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“I am excited by the startup activity in Pakistan despite the inherent challenges”

It is apparent there is no dearth of ideas coming largely from the talented Pakistani youth. But we would be doing our country and the youth an injustice if we cannot change the status quo. A collaborative public private vision and execution plan is required to create the **Startup Pakistan** execution plan.

Planet N strongly believes in the power of collaboration and dissemination of information. We will be creating the public private forum and making all research that we do available to the general public.

It is my strong belief that entrepreneurship can become a game changer in Pakistan.

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1. Introduction

*“How do you make technology work for those who are not working?
Especially for those who are not working because of technology.” –*

Simon Johnson (Professor MIT)

Planet N in collaboration with Karandaz Pakistan and LUMS organized a workshop on 24th Jan 2017, on delivering roadmap for the start-up ecosystem in Pakistan by discussing the problems faced by entrepreneurs, investors, and other stakeholders in Pakistan.

Based on the event insights, this paper has been prepared by Planet N’s Research & Analytics Group for mapping the entrepreneurial landscape in Pakistan by assembling the possible solutions presented. The paper will identify the roadmap of entrepreneurial advancements for the development of start-up ecosystem in Pakistan.

Pakistan’s two third population of 180 million people are under 30 years old and has a young population who is hungry and determined for change. According to UNDP, 23 % of the youth wants to start their own business in Pakistan but the current landscape, procedures and requirement hinders materializing the execution of ideas.

1.1. Methodology

The objective of this study was to connect entrepreneurs with industry experts and to identify the challenges for reaching scales and create a strategy for mitigating those challenges through enabling environment for the start-up ecosystem in Pakistan.

Participants were divided into four groups of broad areas including awareness/curriculum, support of incubators/accelerators, company law and exit strategies. The participants of each group identified common challenges faced by the startups and proposed solutions and strategies to overcome it.

1.2. Aim

As regulatory bodies such as SECP, FBR, PSX along with public sector stakeholders were presented at the workshop, the ultimate aim of this workshop was to present the challenges to them for filling the gaps and challenges the prevails in creating an enabling environment for the start-ups.

1.3. Ecosystem Map

From the past few years entrepreneurial activities are on the rise in Pakistan with an increasing trend in new organizations, funds and initiatives supporting entrepreneurs. The fundamental problem for the enabling environment is lack of successful exits, local investors not ready to exit and foreign investors are also not willing to come in.

Regular communication and collaboration among the startup community, both national and international plays an important role for the growth of startups. Establishing an effective and efficient startup ecosystem cannot be done by the startups alone, it needs active participation and involvement of academia, investors, industry and other stakeholders.

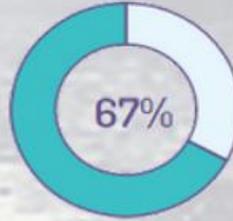
2. Trends of Startup Ecosystem in Pakistan

The overall trend shows a growing shift with more support players, more initiatives, and more investors resulting in increased startup activities in Pakistan for the past few years. However, serious dearth of angel investors, seed funds and venture capital remains which needs to be look at. There was a significant increase in number of startups in 2015, but due to lack of efforts and quality initiatives number of startups observed a declining trend in 2016. Hence, work needs to be done to improvise the existing initiatives along with efforts toward angel funds and private equity players needs to be strengthen too. Moreover, while the increase in angel investors is encouraging, it is also important to increase their knowledge and understanding of investment, particularly for those who are first-time investors.

Criteria: Startups with a Pakistani founder, operated from Pakistan and established after 2010

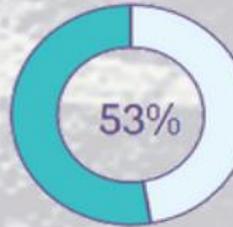


723
STARTUPS



Startups still active

68
RAISED FUNDING



Startups linked to at least one incubator/accelerator

6
RAISED > \$500k

THE BIG PICTURE

Startup Ecosystem of Pakistan

***Data collected from incubators, accelerators & individual startups*

Startups in Pakistan



***Data collected from incubators, accelerators & individual startups*



Incubators/
Accelerators



Co-Working
Spaces



Investor Groups



Research Funds

**ALL PAKISTAN
INCUBATORS/
ACCELERATORS/
CO-WORKING SPACES/
RESEARCH FUNDS/
INVESTOR GROUPS**

***Data collected from incubators, accelerators & individual startups*

Criteria: Startups with a Pakistani founder, operated from Pakistan and established after 2010



\$49 M

RAISED BY MID STAGE COMPANIES

\$20 M

RAISED BY STARTUPS*

Inov8 Limited \$5.4M

Zameen.com \$31.1M

Pak Wheels \$3.5M

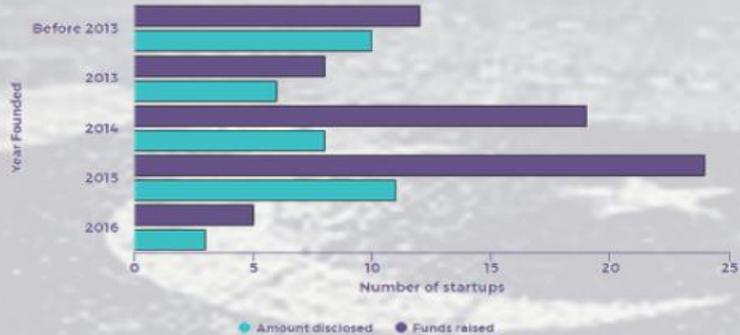
Roze.pk \$9.0M

*Startups who disclosed fundina value

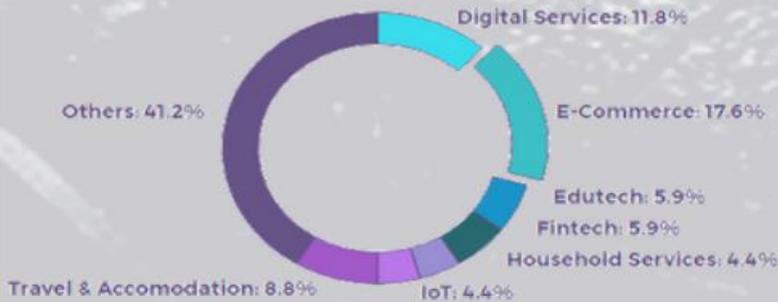
**Data collected from incubators, accelerators & individual startups

Criteria: Startups with a Pakistani founder, operated from Pakistan and established after 2010

Startups who raised funding



Funding raised by industry



Funding rounds by year

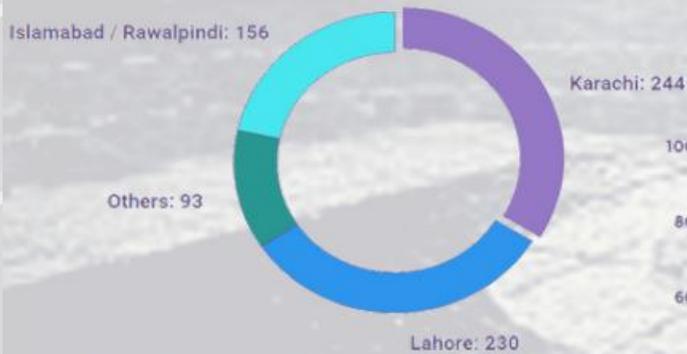


*Startups who disclosed funding value

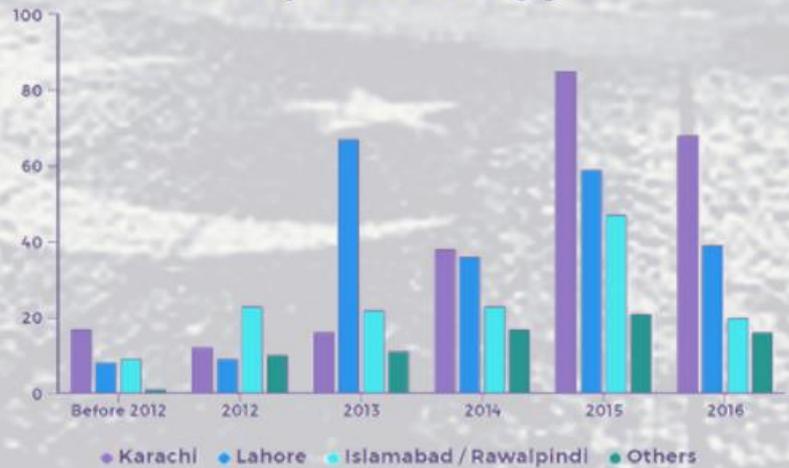
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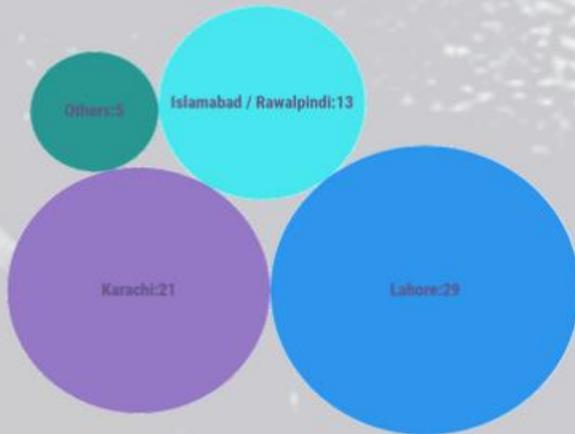
Startups by Location



Startups founded by year



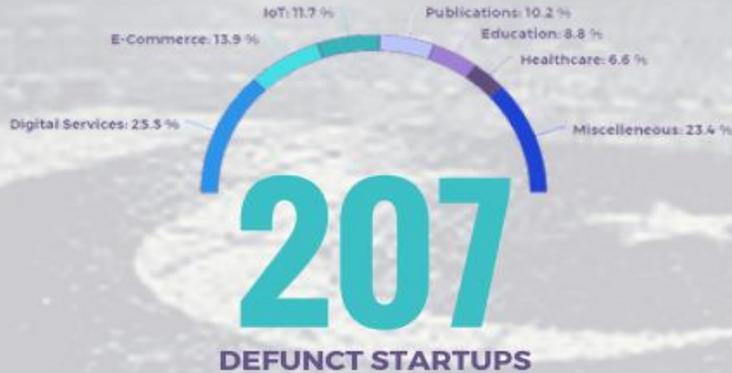
Startups who raised funding



***Data collected from incubators, accelerators & individual startups*

Criteria: Startups with a Pakistani founder, operated from Pakistan and established after 2010

Defunct startups by industry



Defunct startups by founding year



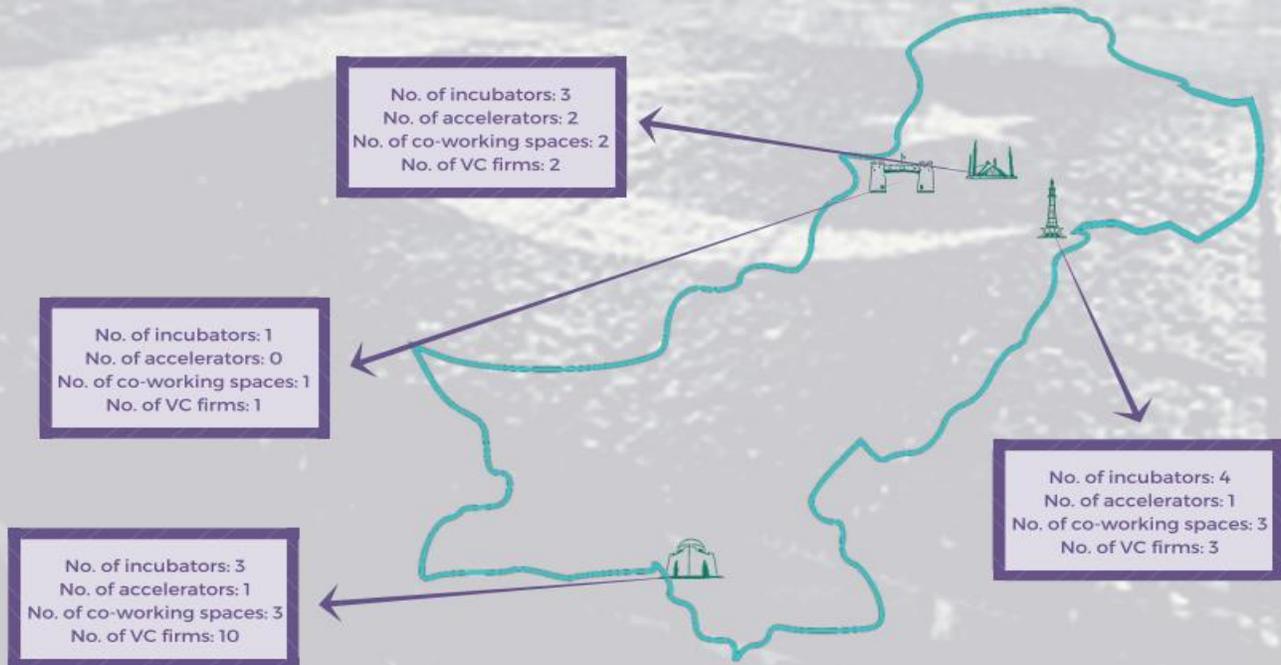
Defunct startups by location



****Data collected from incubators, accelerators & individual startups**

Criteria: Startups with a Pakistani founder, operated from Pakistan and established after 2010

Startup Ecosystem Support Network by Location



***Data collected from incubators, accelerators & individual startups*

Criteria: Startups with a Pakistani founder, operated from Pakistan and established after 2010

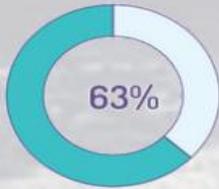
Startup Ecosystem Support Network by Number of Associated Startups



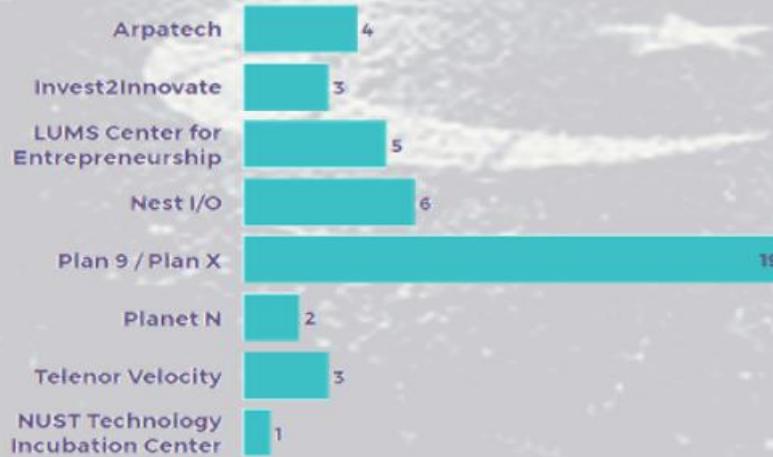
*Size of bubble corresponds to number of associated startups

**Data collected from incubators, accelerators & individual startups

Criteria: Startups with a Pakistani founder, operated from Pakistan and established after 2010



Startups linked to incubators/accelerators raised funding



Association of Startups who raised funding

***Data collected from incubators, accelerators & individual startups*

3. Action Plan: Objectives, Proposed Ideas/Solutions for Five Sub-Groups

3.1. Curriculum/Awareness

Objectives

- Create and nurture entrepreneurial mindsets - the socio-emotional skills to succeed as an entrepreneur, develop entrepreneurial attitudes, behaviors, competencies and enabling skills
- Strengthening entrepreneurial culture and socio-economic structure
- To create startups that facilitate additional employment

Ideas/ Solutions

The foundations of an entrepreneurship education are based on 3 essential features:

a. Availability across the entire educational spectrum starting at primary school

- *Primary school level:* standard the improvement of business enterprise mindfulness and entrepreneurial practices, for example, chance taking and cooperation exercises.
- *Secondary school level:* advance enterprise as a professional choice and as a subject that can be picked as a feature of a review course; show essential business aptitudes, for example, financial aspects,

advertising and simple nearby business law; mastermind additional curricular exercises including visits to organizations.

- *Higher education organizations and colleges:* offer enterprise courses and projects as electives or required subjects; promote entrepreneurship both inside and outside of the educational modules with the aim of providing a dedicated space for the incubation of business ideas with mentoring support available through the university's network of experts.

b. Create a curriculum to identify skills and competencies for each education level

- *Personal skills:* incorporating working in a group, figured hazard taking, critical thinking, and thinking as employers instead of as employees.
- *Core agent abilities:* including numeracy, bookkeeping, correspondence, ICT and simple knowledge of local commercial law and governance principles.
- *Business and administration abilities:* including competitive advantage analysis, market research, business plan development, marketing, financial management, sales and human resources.

c. Develop a trained and certified teaching faculty

- Training instructors and promoting a network of entrepreneurship educators is a fundamental piece of entrepreneurship training. Instructors of dedicated business courses ought to show key entrepreneurial abilities and traits and serve as an entrepreneurial role model and mentor for

students. They ought to engage with the private sector and support initiatives to bring entrepreneurs to educational establishments to serve as role models, mentors and coaches

- We need to armor children with tools and an action plan to garner confidence in them to have the capacity to execute a strong business plan and persist in the face of adversity. Entrepreneurship Education joins formal knowledge and aptitudes (cognitive) and creating individual qualities and dispositions (Non cognitive) to instill entrepreneurial attitude in kids from a young age.

The proposed educational modules would incorporate creative and critical thinking along with communication and presentation skills, collaboration and leadership while building confidence and a can-do attitude and negotiations, decision making, managing risks for adaptability towards change.

3.2. Incubator / Accelerator

Objective

- To clearly define the roles of incubators and accelerators for providing specialized support to startups.

Ideas/ Solutions

Even though it is encouraging to see Incubators and Accelerators paving the way for startups, some challenges and gaps remain. Some suggestions are made to counteract these challenges in an effort to further enhance the quality of I&A's and startups graduating from these institutions:

- As legal laws can be daunting for startups, it is suggested that I&A's partner with legal advisors to help startups with IP protection, Patents, Trademarks, Copyrights, Taxation Laws and Company incorporation.
- Many I&A's have mentors that don't have the background in the industry that the startups are trying to set foot in, so their advice becomes futile as they cannot provide guidance aligned with the scenarios startups face.

- Most of I&A's are run by people that do not have prior entrepreneurship experience. I&A's should bring in people with actual business expertise to guide startups from inception to scaling.
- Even if I&A's have great leaders, often times in-house support staff falls short of expectations. It is recommended to invest in human capital as they are responsible for critical coordination and should not be compromised.
- It is seen quite often that founders of technical companies do not have a technical background which results in founder mismatch, and valuable funds would have to be devoted to pay for software houses to develop software. Hence, in order not to lose valuation it is important for founders' expertise to match their company industry.
- Startups also frequently struggle with understanding laws. It is suggested that I&A's collaborate with lawyers to provide insights to make old, outdated laws more startup friendly.
- Guidance regarding taxation laws and education to minimize taxes and maximize tax cuts is also the need of the hour.

3.3. Company Law

Objectives:

- Create regulatory framework to support and sustain startup culture;
- Create a support network within the public and private sector to offer business solutions to budding entrepreneurs;
- Streamline regulatory processes to ease the process of starting a business.

Ideas/ Solutions

a. Regulatory framework to cumbersome:

The regulatory framework in Pakistan is too cumbersome and over cautionary. There are a labyrinth of laws that need to be decoded to make them startup friendly. Usually private law firms are needed to deduce solutions but law firms are too expensive and most startups do not have access to investment to hire a law firm. Therefore it is advised that the government simplifies procedures and runs awareness campaigns on laws and procedures to sustain and grow the startup culture in Pakistan.

There used to be a “one window solution” where companies could go for answers but this service has been discontinued. It is proposed to restore this service to address teething problems. It is

suggested to create a helpdesk liaison between government and private sector departments to have a one-stop shop for business solutions.

Key Government departments	Key Private Sector Departments
SECP	PASHA education institute
PRA	Incubators/Accelerators
PTC	PBC (Pakistan Business Council)
SBP	
FBR	
PTA	

Private sector is also encouraged to take part in developing creates a conceptual framework on policies, taxation, stock options, regulations etc. and get the government’s support.

b. Stock Option laws

Since startups companies are unable to pay high salaries to their employees, one way to retain talented employees is to use stock options. Stock Option Plans are an extremely popular method of

attracting, motivating, and retaining employees. However, no such laws for stock options exist in Pakistan at the moment, thus making startups lose out on talented individuals to work for them. It is advised to devise a stock option plan for companies to be able to retain high quality employees which would help them succeed.

c. Tax Breaks

Currently there is no special provisions made for startups in the taxation department. There are no tax holidays or exemptions for new startups and this acts as a deterrent for companies to register in Pakistan and would much rather take their business in countries with lower taxes. It is proposed to create a new tax bracket specifically for startups, and some exemptions or cuts for the first few years of the business.

d. Expensive Licenses

Licenses for startups especially for Fintech companies are too expensive, hence they can't start small, run pilots and work their way up. The government should give these new companies some wiggle room to be able to start small, experiment and learn from their mistakes.

e. IPO Laws

Intellectual Property laws are the corner stone of innovation, however in Pakistan IPO laws are very weak and take too long to process. By the time the process is over the technology goes obsolete. Hence most startups prefer registering their startups abroad and taking their technologies where

their ideas are protected. Government should strengthen IPO laws to protect innovative ideas and discourage brain drain.

f. Bankruptcy Laws

The fact that Startups are high risk ventures with a high failure rate coupled with the fact that there are no bankruptcy laws in Pakistan acts like a major deterrent for investors. The government needs to create an exit strategy with strong bankruptcy laws to create a cushion to recover in case they fail.

3.4. Exit Strategies

Objective

- To create a framework for investors and entrepreneurs of startups to seamlessly exit their investment at maturity.

Ideas/ Solutions

There are several regulatory suggestions made by industry specialists for successful exit strategies for investors:

➤ **SME Board on Pakistan Stock Exchange**

Pakistan has SME regulations in place but it is not a feasible option for startups as there needs to be a large capital investment setup. It is suggested that the PSX brings down paid up capital requirements for the facilitation of investors to sell out shares in SME's/startups through an IPO.

➤ **Private Market to match make investors and startups**

It can be a cumbersome process to create a listing on the Stock Exchange so PSX is working on a platform to serve as a matchmaker for investors and startups. The private firms will be able

independent and free to register, however SECP would need to develop the framework for due diligence for this option to be viable.

➤ **Crowd funding**

A crowd funding platform development is the need of the hour to tap into this investor base. It is usually easier to raise money through crowd funding rather than scouting for large investments from traditional investors.

➤ **Public Private funds**

Another suggestion was to develop a fund that is owned by the government and private investors together (e.g. 40% government owned and 60% privately owned).

This fund could be used to invest in startups and after 3-5 years the profits would be distributed in the fund which would be fiscally beneficial to both the government and private investors. Presently, there are separate Private Equity and Venture Capital regulations in place but this fund is proposed to be a combination of both for which a separate framework needs to be developed.

➤ **Angel Investors Platform**

As angel investors are a huge part of the eco-system and there needs to be a framework developed to give them fiscal incentives and tax breaks to encourage them to invest in startups

➤ **Revive private equity & VC fund**

There has not been a single PE and VC fund established in Pakistan since the update of the regulations in 2008. This indicates that the clauses need to be revised for better provisions of investments.

4. Conclusion & Recommendations

It has been quite encouraging to observe the amount of increased activity since 2014 even though the discussed gaps and challenges continue to persevere in the startup ecosystem of Pakistan. As the challenges persist in the country, the experts whose views are amalgamated in this report seemed to be very positive for the startup ecosystem of Pakistan.

Understanding the difference between the micro and macro environment of the ecosystem is very important in order to see the emergence of success stories in Pakistan. In the micro environment the number of players will continue to increase, but stakeholders should work together to coordinate efforts and strengthen the pipeline for young startups. The concept of entrepreneurship education aims to develop and sustain an entrepreneurial culture in Pakistan by using the structured approach of the formal education system. The curriculum needs to be designed to teach skills and competencies that are equally beneficial to starting one's own business as well as be applicable in most workplace situations.

While on the macro environment, there is a need for government to address the regulatory issues. As entrepreneurs are a special breed with special needs, hence laws should be tailored to their requirements to create an enabling environment for them to succeed. At the central part of this level, the government should have a long term and consistent vision for a proclaiming change. For the dilution of risk for investors, investing in startups and the reduction of barriers in access to

finance can be greatly done by federal agencies of the country. State Bank of Pakistan should also play an important role in this space and induce the change of legislation and provisions that holds the business back.

Startup ecosystem in Pakistan lacks having a harvest goal in mind and creating an exit strategy to achieve it. The main objective of professional entrepreneur is to create economic value. But unfortunately in our economy we don't pay much attention to the concept of exiting a business venture or harvesting the business. There is a famous saying by venture capitalists, "It is easy to get an investment but how to get out of it? Or what is the exit?" Usually no startups have an answer to this question which is the reason we don't have much investments. The law enforcing agencies in Pakistan should create an enabling and encouraging environment by providing funding's to startup founders and small business owners.

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