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INVESTOR

ROUNDTABLE

2019

WHITEPAPER





This whitepaper summarizes and makes recommendations based on the discussions that took place at the Investor Roundtable, held at the NIC on the 11th of October 2019. The objective of the Roundtable was to discuss the investment landscape for startups in Pakistan. Participants shared insights and explored possibilities for collaboration at various levels. The agenda of the roundtable revolved around discussions on the current challenges in the investment landscape, sharing international best practices, and proposing solutions for structuring the investment process in the country.



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BACKGROUND

Pakistan has immense potential for entrepreneurship. Availability of talented software developers, young urban population, rising internet usage, improving regulatory climate, and a growing support network propose a progressive future for tech entrepreneurship in the country. However, the momentum of entrepreneurship has not picked pace the way experts predicted it would. The current landscape, procedures, and requirements hinder the materialization of ideas and hence act as barrier to entrepreneurship flourishing in the country. A major hurdle is the lack of venture capitalists and angel investors, which serves as a major showstopper for the Pakistani entrepreneurial ecosystem.

Regulatory constraints act as barrier to the registration of Venture Capitalist Firms within the country, leading to lack of local VC firms. There is a dire need to bridge the gap between start-ups and VCs, and to create an ecosystem that brings all stakeholders on board, to facilitate access of capital to start-ups, and provide greater visibility to VCs

interested in investing in entrepreneurial initiatives. NIC, in line with the above mentioned agenda, held an Investor Round Table Conference on the 11th of October 2019 in Islamabad, bringing all the stakeholders together to discuss challenges, opportunities and agree on a collective action plan.

Chaired by Zouhair Abdul Khaliq, moderated by Fasieh Mehta and Ahad Wazir, the RT witnessed diverse participation from Political leadership, Venture Capital Firms, Government Officials, Incubators & Accelerators, Angel Investors, Donors and International Non-Government Organizations. Multiple ideas for collaboration were put forward-the materialization of one of the ideas led to the establishment of Venture Capital Association of Pakistan (VCAP), later presented at a conference in Karachi.

This whitepaper summarizes the underlying issues pertaining to access to finance and the corresponding solutions proposed by the attendees of the IRT.



IRT PROCEEDINGS

The RT began with a brief presentation by the NIC on the impact created since 2017, followed by three startups, currently incubated in the facility, pitching their ideas to the participants. The participants rated the startups on their business model, and quality of pitching. The following startups presented their ideas to the participants:

- **Plate 101**
Empowering women home-chefs to generate income.
- **Zambeel**
Developing robotic equipment for architectural woodwork and composite work.
- **Augment Care**
An end-to-end health tech station, connecting patients to doctors.

Discussion

The discussions at the IRT revolved around five main points:

1. Government Regulations and Challenges for Investors in Pakistan.
2. The role of Incubators and Accelerators as catalysts.
3. The role of Angel Investors in entrepreneurial ecosystem of Pakistan.
4. Startups' Founders' Maturity.
5. Collaboration and Co-Investment Opportunities.



Government Regulations and Challenges

Officials from the Security and Exchange Commission of Pakistan (SECP) informed the participants on the ease of registering startups with SECP, the results of which are evident from the World Bank Report which scores Pakistan 108 out of 190 on Ease of Doing Business Index, in 2019. Venture Capitalists insisted upon the mandatory existence of vehicles (Venture Capital Fund or Private Equity) for risk capital to enter into the country. Current regulations for channelizing and mobilizing funds, poor past record on contract enforcement, huge time lapse in resolving commercial disputes were identified as the major issues leading to lack of trust amongst investors in the country.

In terms of financial characteristics, a prime concern for Pakistani VCs is the safety and liquidity of their investment. One of the main impediments for investors is the lack of well-articulated exit mechanisms, because of which their rights remain unprotected.

Various best practices adopted by international VC firms were discussed and ideas brought forward. Internationally, Venture Capital firms are setup with a General Partners (Fund Manager) and Limited Partners (investors in the fund) structure. Effectively, the fund then has an investment committee, comprising of general partners who have the decision-making authority over what investments to make. The biggest challenge in adoption of this model in Pakistan is the existence of a trust board on top of the entire



structure. There is a flawed system in place for the selection of trustees by the government, and these factors hinder the adoption of international model into the local ecosystem.

Owing to the current landscape, which provides no stock options plan for VCs, neither any investing schedules for governance of incentives, there is lack of interest from VCs to invest in the country. ***This creates a need to document international best practices so as to be used by SECP. Standardization in documentation to be used by investors and founders would create a smooth transition from registration of funds to their investment in a start-up.***

“There is disconnect between private and public sector. Do not assume that we in the Government know technical things especially about Venture Capital, so you need to educate us, too”

Faisal Khokar
Director Americas, Board of Investment, Prime Minister’s Office

The pivotal role to be played by the State Bank of Pakistan in creating an investment-friendly ecosystem in order to encourage foreign investment to enter into the country for local startups, was brought forward by Khurram Zafar. The stringent requirements put forward by SBP have created a barrier to entry for the Pakistani diaspora

and international investors to invest in startups in Pakistan. The individual procedures, regulations, and documentation requirements imposed by SECP, SBP, and FBR are not complementary to each other, adding to the overall administrative cost, and duplication of effort. This results in loss of investor interest and subsequent loss of FDI entering into the country, as investors choose to invest but headquarter the company in foreign land, leading to shift of value creation from Pakistan to other countries which provide ease of doing business.

Incubators and Accelerators as catalysts

The Incubators and accelerators are playing a pivotal role in boosting the entrepreneurial ecosystem in the country. The senior management of incubators present at the RT had a consensus that the purpose of the NICs is job creation in Pakistan and not creating unicorns. On the contrary, investors were of the view that growth by startups is more important than job creation, and growth to transform startups into unicorns can only be achieved through investments.

The investors further asserted the integral role to be played by NICs in providing in-depth knowledge to startups on legal and financial structuring of the company. This would reduce the investment cycles, and save investors from the hassle of restructuring the companies. There was a unanimous agreement by all participants of the IRT on the **creation of a nation-wide directory that categorically lists all start-ups and creates a user-friendly interface for easy access by public as well as investors.** This initiative would facilitate investors in their scouting process, providing greater visibility to startups, and ideas to aspiring entrepreneurs.

Angels can uplift the ecosystem

Angel Investors play a key role in providing

the initial capital for any startup to move from Problem-Solution Fit to pre-growth stage. A major concern raised by senior incubation management and investors was the lack of information available to angel investors, disabling them from making the right investment decisions. Disproportion in equity taken versus investment made results in loss of ownership for founders. The venture capitalists highlighted how this poses a challenge for them to invest in the startups, as eventually the founders would become minority shareholder and hence lose commitment towards the startup. It was also brought to the attention of the participants that there are small angel syndicates in Pakistan but they are not actively connected with incubators and accelerators. These angels are mostly connected via social groups on different informal channels such as WhatsApp, and spend only 5% of their time to scope out startups that are on the radar in the ecosystem, mostly picked up by media.

“We as investors have had some good and some not so good experiences but all those are reflective of the ecosystem evolving”

Rabeel Warraich
CEO, Sarmayacar

As such the gap can be filled by **creating an “Angel Syndicate” in Pakistan, to facilitate education about angel investment in startups which can result in co-investments by multiple angels to reduce the risk of investment.** This syndicate will also help with the due-diligence of the startups (for later rounds and for VCs) and filter out startups that have the potential to scale. The syndicate will facilitate incubators by providing access to finance for investment-ready startups at seed stage. Startups that raise funding through the syndicate at seed stage can attract funding from VCs at growth stage,

creating a collaborative ecosystem which provides investors the opportunity to capitalize on their investments, and correspondingly facilitate startups in generating more funds. **A formal Angel Education Program can be embedded into the syndicate to create awareness about angel investment and to open new avenues for start-ups seeking funding at seed stage.** A well-coordinated effort, with NICs playing an integral role, to bring such a syndicate together is needed.

Startup Founders' Maturity

All participants agreed on the dire need for startup founders to be more informed as to how they can value their business, and on the investor expectations from them. Lack of understanding from the start-up's side regarding the expectations of Angels vs VCs creates an ambiguous pitch designed for the wrong audience.

Investors urged incubation centers and accelerators to educate startup founders on the concept of 10x growth, and why a VC would expect a 10x growth from them before injecting funds into their startup. NIC management shared how it brings various VCs on board to educate its startups on developing investment pitches to different investors. All participants stressed on the importance of this to happen more frequently; **investors agreed to educate startups on their expectations from them, and to make them aware of the jargons and technical terms which most start-ups are unaware of.**

Co-Funding and Collaboration Opportunities

Despite many challenges existing in the Investment and Startup Ecosystem of Pakistan, all participants agreed on the potential for organizations to collaborate and improve the investment landscape. As a developing country, it is crucial for all key stakeholders to work together in bringing foreign invest-

ment into Pakistan.

Global models were discussed and brought to the knowledge of participants. **Suggestions were put forward to launch campaigns in order to raise awareness amongst the large corporates so as to co-invest with successful entrepreneurs to create a fund. Government and the Development Sector can also partner with investors in co-investing to minimize the risk for each player,** as the ability to take risk is critical. Intervention from the SBP and SECP can play a pivotal role in the same regard.

"Silicon Valley is not a place. It is a mindset. We are on that path, but not there yet, need to pick up pace & we need to inculcate this mindset across our academia, public & private sectors"

Naeem Zamindar
CEO, Zamindar Ventures

The riskiest form of investment is from the private sector. This risk can be offset by **program initiatives from government and international development organizations such as the World Bank and GSMA, to provide matching grant investments. It was brought to the attention of government representatives that schemes on tax credits, exemptions from income tax for predefined period, support for international patent protection, venture capital assistance schemes, credit guarantees, and small startup loan schemes are some of the ways in which the government can radically improve the investment landscape for startups in Pakistan.**



RECOMMENDATIONS

Based on the discussions held at the IRT, the recommendations put forward can be summarized as follows:

- i. A Venture Capital Association to be created in order to foster venture capital activity, bring more foreign investment and become the driving vehicle for creating co-investment vehicles within the country. This association will also put forward the global best practices for creating such vehicles, to facilitate the government in making more investor friendly regulations.
- ii. Creation of an Angel Syndicate Forum by the NIC, with an embedded Angel Education Program to create awareness about angel investment and to open new avenues for start-ups seeking funding at seed stage.
- iii. Incubators and Accelerators to launch program with universities nationwide to help instill entrepreneurial mindset within students and promote entrepreneurship as a viable career choice.
- iv. A comprehensive user-friendly online database to be created where all start-ups in the country (whether part of an incubation/acceleration program or not) can pitch for investments by sharing relevant business model details.
- v. Developing modules to educate start-ups on raising finance as an integral part of NIC curriculum, and collaborating with VCs and Angel Investors to align them in delivering relevant sessions to start-ups.
- vi. A database with a guide to be created for all startups founders, incubators, accelerator and investors. This would include documents like standard term sheets, educating all stakeholders on the entire investment process i.e. from registration of a fund to investment of the funds in a startup.
- vii. Quarterly roundtable to be held with all key stakeholders to address specific challenges faced by investors in the ecosystem, resulting in one collaborative initiative. The next IRT is proposed to be held in Feb 2020.



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