

# THE PRIVATE SECTOR IN MEDITERRANEAN COUNTRIES

MAIN MALFUNCTIONS AND

OPPORTUNITIES OF SOCIAL ENTREPRENEURSHIP

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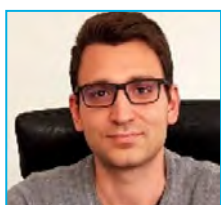
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# The private sector in Mediterranean countries: Principal dysfunctions and opportunities for social entrepreneurship

## Introduction

By Patricia AUGIER

*This report reviews the situation of the private sector in Mediterranean countries, with the aim to improve our understanding of the main bottlenecks and to analyse the potential of social entrepreneurship in meeting the need for more inclusive growth. The Mediterranean region forms the scope and the report focuses on 8 of the 10 partner countries of the European Union: Algeria, Egypt, Israel, Jordan, Lebanon, Morocco, Palestine and Tunisia (the 2 countries that we have not included, due to lack of available data and information, are Libya and Syria) to which we have added Turkey whose accession process has, to date, been put on hold.*

### **Why focus on the private sector in this report?**

*Firstly, there is a more than ever urgent need to create jobs in all countries of the region and, considering the degradation of public finances and overstaffing of the public sector, future job creation must be driven by the private sector. The latter must prove sufficiently dynamic to absorb a supply of labour that is under-employed or employed in the informal sector with very low wages and no social protection. To avoid the recruitment of young educated Mediterraneans by extremist groups, we must provide the youth of the Arab world with job opportunities and a future that will ensure their social integration. So far, and despite all the initiatives and reforms undertaken in certain countries,*

*the needs of the private sector have always been considered as secondary, as compared to political conflict, the interests serving a financial and economic elite in collusion with the political regime and the lack of willingness for cooperation between the different countries of the region. Mediterranean entrepreneurs truly suffer from this situation as they have no access to incentives for development, or to a market that is sufficiently substantial to drive competitiveness and to build regional value chains. But those who bear the brunt of this state of affairs are the millions of people who, excluded from the formal economic system, are deprived of improved living standards. For these reasons, the private sector must, henceforth, be the focus of development in the different countries of the region.*

*Secondly, Mediterranean countries must shift their growth regime towards greater competitiveness and achieve an upgrade in quality. Production systems must create more added value, which in turn will provide for better paid jobs. To achieve this, growth must come mostly from gains in productivity rather than from increased production capacity alone. These changes rely upon the capacity of firms to adapt their production systems and organisation, and above all, the capacity of public authorities to create the necessary conditions and the right incentives to encourage companies to lead this change.*

*Thirdly, despite all of the literature on this question, so far no summary document has set down all of the potential explanatory*

factors, including at once the contributions of academic literature, the different reports produced by international organisations, information stemming from all available data on the private sector in Mediterranean countries, as well as the multiple points of view and testimonies gained from our missions or those of our partners from academic and operational spheres.

**Why include the chapter on social entrepreneurship?** Among the paradoxes of Mediterranean countries is that despite a low level of poverty compared to developing and emerging countries, certain parts of their population are isolated and/or excluded from the economic world. This is the case for the youth, women and rural areas that are far from large urban centres. To the afore, we may add those working in the informal sector. The economic system therefore excludes at least two thirds of the population, thus, the foundations for sustainable development are lacking. In the Arab world, the gap in probability of gaining access to formal economic sphere, between a man in his forties living in a large urban area or a young woman living in a rural area, is most likely the greatest among all developing and emerging regions. In view of this situation, in addition to the well-known and more general macro factors (investment, innovation policy, exchange rate policy, regulations, etc.) that can contribute to the growth of these economies, it is essential to develop other initiatives that respond more specifically to these problems of exclusion. To enable the region to converge towards a more inclusive development model, Mediterranean countries need both appropriate economic policies and social innovation that can come from civil society and which

the public authorities have every interest to encourage by creating a favourable and incentive-based legislative, fiscal and administrative environment. Although social entrepreneurship cannot provide a global solution for a country's development, it can be considered as an opportunity to meet the need for a broader integration of populations previously excluded from the economic sphere.

The report does not intend to draw up an exhaustive list of the obstacles facing the sector. This would not make sense at the scale of a the entire region as, despite certain similarities, each country has its own specificities whose roles are essential in addressing these obstacles. Therefore, in-depth analyses are required to understand the specific difficulties of companies, not only by country, but also by type of firm (the problems of large companies are not the same as those of micro, small and medium-sized enterprises, or those of start-ups.) These analyses should also target specific issues, such as access to land, financing, informality, corruption, taxation, etc.) [1]. The report does, however, strive to provide some answers to the following questions: How have Mediterranean countries evolved since the launch of the Barcelona Process? Why has growth fallen short of expectations? What role can Central Banks play in making the private sector more dynamic? How can governments contribute to the development of social entrepreneurship?

The report is structured in 4 chapters. The first presents the dynamics observed in Mediterranean countries over the past 20 years. The second attempts to analyse the main reasons for the lack of growth. The third chapter focuses on the role of Central Banks in improving the business environment and the attractiveness of foreign investment. The fourth and final chapter focuses on social entrepreneurship.

## *Executive summary*

**Chapter 1** introduces the report by taking stock of the economic dynamics of Mediterranean countries since the beginning of the Barcelona Process. Over the last 20 years (1995-2017), the region's growth rate has averaged 4.1% per year compared to 5.1% for all comparable income countries and 7.9% for East Asian countries. Among Med countries, growth has ranged from 5.1% for Jordan to 3.5% for Algeria. The region's growth rates, considered by some economists as high, are far from sufficient in the eyes of Femise. In this chapter, we show that: - GDP per capita increased by an annual average of only 1.9% between 1995 and 2017, while over the same period, GDP per capita in developing and emerging countries increased by 4%. As a result, the convergence process between Med countries and the EU has stagnated and absolute differences in living standards between the two shores have even increased.

- With an average rate of 12.4% in 2017, unemployment remains very high within the region. It also continues to affect young people and graduates more strongly (with unemployment rates of 27% and 29% respectively). Worse still, female participation rates are extremely low (29% against 50% for all countries with comparable incomes).
- Although poverty rates in Med countries are lower than in all developing and emerging countries, the incidence of poverty among the populations, measured against national thresholds, has increased in Egypt and Jordan. In addition, compared to all countries of comparable income, it is in Med countries that the population's vulnerability to poverty has increased the most.
- In Med countries, the distribution of wealth remains the most egalitarian of all Southern countries. But here again, there is growing discontent among the population with regard to health and education, a sign that

the situation is deteriorating and that there is a trend towards growing horizontal factors of inequality.

- In terms of integration within the global economy, despite greater diversification and improvement in the technological content of products, the export growth rate of Med countries has remained below that of comparable income countries.
- Finally, the region's trade deficit has continued to deteriorate in an increasingly worrying way. This deterioration is much stronger as compared to the Rest of the World than with regard to the EU.

**Chapter 2** makes a general analysis as to the possible reasons behind this situation. Mediterranean countries are caught in the "middle-income country trap", with wage levels that are too high to compete with lower-income countries and inadequate competitiveness, due to gains in productivity that are insufficient to compete with more advanced countries. This chapter highlights a number of observations:

- In the period when investments in Asian countries took off the rates were between 30% and 40%, whereas, in the Med region, rates have remained relatively stable over the past 20 years, at levels varying between 23% and 25%. Over the recent period, the countries that have risen above this regional average are Algeria (33.5%), Morocco (30.6%) and Turkey (28.5%) while, to the contrary, Tunisia (21.3%), Israel (20%) and Egypt (14%) have fallen behind. But the most surprising factor is that since the beginning of the Barcelona Process until recent years, the ability of this investment to create growth has declined.
- The contribution, to GDP, of foreign direct investment (FDI) entering the region has decreased from 6.7% in the early 2000s to 3.8% today. One important point, underlined in the academic literature, is that the positive effects of FDI on growth depend on the absorption capacity of host countries (namely the qualities of their human capital,



infrastructure, financial system, institutions and public services, customs procedures, the managerial capacities of business leaders, etc.) and the characteristics of the FDI (sector of destination, type of agreements and relations with the host country and local companies, etc.).

- Mediterranean countries have shown the worst progression of overall productivity out of all developing and emerging countries: the average annual growth rates of total factor productivity between 1995 and 2016 were just below 0% in the region. Other indicators confirm that, compared to other comparable income countries, a significant innovation gap has developed.
- Beyond the fairly positive general image offered, by global indicators (Doing Business, Competitive Global Index, Economic Freedom Index,) of the region's business environment, we demonstrate that multiple problems remain. We also show that there can be a gap between the results of these global indicators (which are useful in that they allow for international comparison and can also highlight the progress made in some countries), and actual conditions in the country. In addition, the time limits and conditions for the application of laws and reforms create a lag between the vote of the law or reform and its actual implementation. It is therefore essential to constantly evaluate results in relation to expected outcomes.
- Finally, cronyism within business and politics continues to exist in most countries of the region and we demonstrate not only its very negative effect on growth but, above all, that it has more insidious and damaging consequences regarding society itself (development of feelings of injustice and exclusion, changes in representation and value systems, etc.). This system of collusion is at the root of a large number of problems

(unfair competition in certain sectors, discouraging of private initiatives and entrepreneurship, low private sector investment, corruption, poor governance, administrative barriers, etc.) and is a key obstacle to the development of the private sector. It is urgent to break this deadlock, which is undermining growth and job creation in the countries of the region.

**Chapter 3** analyses the major contribution that can be made by central banks in Mediterranean countries towards private sector reforms, to improve the business climate and international attractiveness for foreign investment. By focusing on recent reform actions carried out by the Central Bank of Tunis (BCT), while analysing comparative experiences and scenarios of central banks in other Mediterranean countries (Egypt, Jordan, Morocco), the chapter outlines the type of responses brought in six areas of intervention:

- (i) the first area is inherent to the modulations of operational frameworks for monetary policy management to improve the banking sector's support for private sector investments, whether this be through the implementation of non-conventional monetary policy measures, or the modernisation of monetary policy instruments with a view to improving the banking sector's support of the economy.
- (ii) the second area is the pursuit of financial stability to ensure that the private sector benefits from an environment conducive to doing business,
- (iii) the third area concerns the monetary authorities' real commitment to the financial inclusion of SMEs in order to remove obstacles to private sector access to sources of funding,
- (iv) the fourth area also concerns the international commitment of central banks to the implementation of structural reforms, in particular in the context of specific programmes

with the IMF, focusing mainly on the re-evaluation of private sector business practices,

- (v) the fifth area concerns exchange rate flexibility for greater private sector competitiveness and resilience to external shocks. For the central banks analysed, the mixed effects of this area of intervention are mainly due to the varying achievements of certain prerequisites, namely, the robustness of financial systems, the sustainability of macroeconomic fundamentals, the viability of foreign exchange reserves and, above all, the international support provided by the main donors. These are all preconditions for the implementation of floating exchange rates,
- (vi) Finally, the sixth area concerns the relaxation of exchange rate regulations to optimise the attraction of foreign companies and international capital. On the latter point, converging findings emerge from the strategies of central banks. Aware of the risks inherent to a disorderly liberalisation of capital movements, the latter have quite rightly adopted a sequential approach with the progressive liberalisation of capital and financial transactions, which prove effective in mobilising the external resources required to finance the necessary reforms. But the expected benefits of this external financial liberalisation will not be automatic. They will be conditioned by the level of financial development, the stability and resilience of the macroeconomic framework and the quality of institutions. This requires a pragmatic and gradual approach to relaxing exchange rate regulations.

**Chapter 4** analyses the potential of social entrepreneurship (SE) as a driving force for private sector development and support for growth and employment in Mediterranean countries (MC). It looks at the current situation of SE, firstly by investigating any remaining potential obstacles to its development in MC. In the second part, there is a focus on the range of available tools,

in particular financial instruments, to support the further development of SE in the Mediterranean. In the third and final part, we present possible routes of investigation that could feed into future actions and programmes to promote SE within the framework of the EuroMed partnership. This chapter highlights a number of findings:

- Social entrepreneurship could play an important role in MC. If supported by appropriate public policy, it can help to improve the economic security of vulnerable populations. Social enterprises are economically efficient while strengthening equity, diversity, equality, territorial development and respect for the environment.
- Nevertheless, the emergence and development of SE in MC remains far beneath its potential. Social innovation comes up against persistent obstacles, among which access to finance is one of the greatest. Access remains limited due to the lack of an adequate legal framework. Yet there is a plethora of financial tools adapted to SE (micro-finance, social impact bonds, crowdfunding platforms, etc.). Current needs call for a more open multi-stakeholder approach, which would unleash the innovative potential of social entrepreneurship. These dynamics must be pursued at the national level, calling on all public, private and institutional actors to contribute to a sustainable economic model. A dialogue could be launched in each country to define social impact performance indicators that could be adapted within a national framework. This framework would enable public and private actors to better evaluate investment projects and contribute to the implementation of socially responsible and inclusive projects.
- Public authorities could also play a facilitating role by providing a legal framework for the sector and by introducing tax incentives. By developing their legal and regulatory framework in the financial sector, governments in the South could open up the possibility of attracting so-called social finance actors.

- *To complement national initiatives, cooperation with Europe and between countries of the South could be strengthened. We believe that the development of a EuroMed system that would match socially impactful investments with the needs of social entrepreneurship would be appropriate. Such a mechanism could take the form of an online EuroMed platform dedicated to social entrepreneurship. It would provide social entrepreneurs with a link to financial structures focusing on social impact. It would also provide a means for financial structures to better identify and evaluate the social projects that require support.*
- *Moreover, the creation of a social entrepreneurship ERASMUS would cultivate entrepreneurial skills with a social impact in the Mediterranean. In addition to the transfer of innovative knowledge for entrepreneurs on both shores, this initiative would lead to the discovery of new markets and new partners and, above all, would open up the prospect of creating a socially innovative entrepreneurship ecosystem in the Mediterranean.*

## Notes

1. *This point of view, which we defend when it comes to identifying the difficulties of the private sector, has led us to produce the next Femise EuroMed report, focusing on one country (Morocco), one specific theme (integration into global value chains) and one type of enterprise (small and medium-sized enterprises).*

# CHAPITRE 1

## Dynamics observed in Mediterranean countries

by Patricia AUGIER and Jocelyn VENTURA

*The purpose of this chapter is to take stock of the economic dynamics of Mediterranean countries over the past 20 years, i.e. since the launch of the Barcelona Process. A well-functioning private sector must result in growth rates and international integration equivalent to those of countries with comparable levels of development. In the following, we will therefore evaluate the main outputs of the private sector in Mediterranean countries. In the first section, we question whether growth rates have been sufficient (in comparison with other developing and emerging countries, by evaluating the convergence process with the European Union (EU), in relation to the main unemployment figures and changes in poverty and inequality indicators) and, in the second section, we analyse the evolution of the region's exports*

### **I. Have the growth rates of Mediterranean countries been sufficient over the past 20 years?**

#### **I.1. A comparison with the growth rates of other emerging and developing countries**

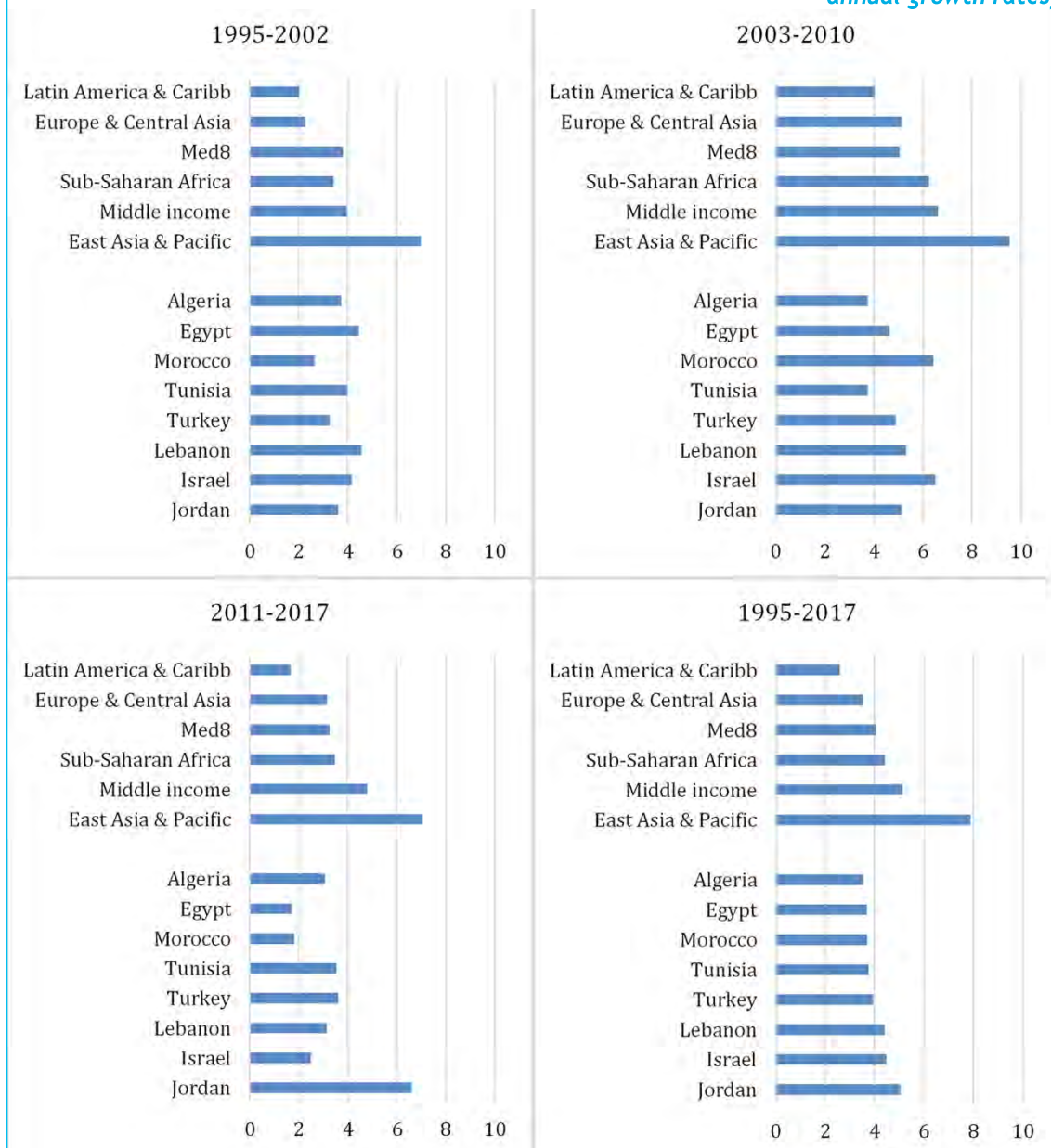
The first three quadrants in Figure 1.1 break down the average annual growth rates into three periods (1995-2002, 2003-2010, then 2011-2017). The last quadrant shows the average yearly growth rates

over these twenty years (1995-2017). Figure 1.1 shows the average growth rates for the eight Mediterranean countries studied, the overall average of these eight countries (MED8), that of comparable income countries (countries belonging to the "middle income" category defined by the World Bank) and those of developing and emerging countries in the other main regions of the world.

Between 1995 and 2002, i.e. during the first eight years following the implementation of the Barcelona Process, Mediterranean countries showed an average annual growth rate of **3.8%**, which is well below the growth rate of East Asian and Pacific countries (7%), but in line with the average for middle-income countries. Mediterranean countries do better on average than the countries of Europe and Central Asia (2.3%) and Latin America and the Caribbean (2%). Among Mediterranean countries, Egypt (4.6%), Tunisia (4.5%), Israel (4%) and Jordan (4.2%) are above the average of the 8 Mediterranean countries (MED8).

Over the period 2003-2010, their average annual growth rate was higher (5.1%), but remained below the average growth rate of all middle-income countries (6.6%). Only Latin

**Figure 1.1**  
**Average growth rate of Mediterranean countries in comparison with reference countries (average annual growth rates)**



Source : WDI 2018, World Bank.

Note : For the 4 regional groups, high-income countries were excluded. The groups of countries are defined in the Apeendices.

American countries showed lower growth, with an average rate of 4%. The Mediterranean countries with the highest average annual growth rates over this period were Jordan (6.5%), Lebanon (6.4%), Egypt (5.3%), Turkey (5.1%) and Morocco (4.9%).

The economic crisis has slowed growth in all developing and emerging countries.

Mediterranean countries have suffered the additional impact of the political events referred to as the Arab Springs. The average annual growth rate over the recent period (2011-2017) has fallen to 3.3%, compared to 4.8% for all middle-income countries, 7% for East Asia and the Pacific, 3.5% for Sub-Saharan Africa, 3.2% for Europe and Central Asia and 1.7%



or Latin American and Caribbean countries.

Overall, over the last twenty years (1995-2017), the growth rate of Mediterranean countries has increased by an average of 4.1%, in contrast to 5.1% for comparable income countries. It can be noted that there are few differences between the Mediterranean countries. The average of these rates varies between 5.1% for Jordan and 3.5% for Algeria. East Asia and the Pacific (7.9%) and Sub-Saharan Africa (4.4%) recorded stronger growth, while the other two regions, Europe and Central Asia, as well as Latin America and the Caribbean, did less well (3.5% and 2.6% respectively).

Comparison of the growth rates of Mediterranean countries with those of other developing and emerging countries suggests that this growth has been adequate. However, the analysis of other indicators does not confirm this point of view.

## 1.2. The region is not converging towards the EU standard of living

Due to a growing population, these growth rates only allowed an increase in **GDP per capita (expressed in terms of purchasing power) of 2%, on an annual average for all Med countries between 1995 and 2017, while over the same period, per capita income increased by 4% for middle-income countries and by 6.8% for East Asia and the Pacific countries** (see Table 1.1). Without Israel and Turkey, the GDP per capita of the group of 7 Med countries increased slightly between 1995 and 2010 and then stagnated (Figure 1.2). Since 2013, the purchasing power per capita of all 7 Med countries has fallen below that of middle-income countries.

**Table 1.1 Average annual growth rate of GDP per capita in parity of purchasing power between 1995 and 2017**

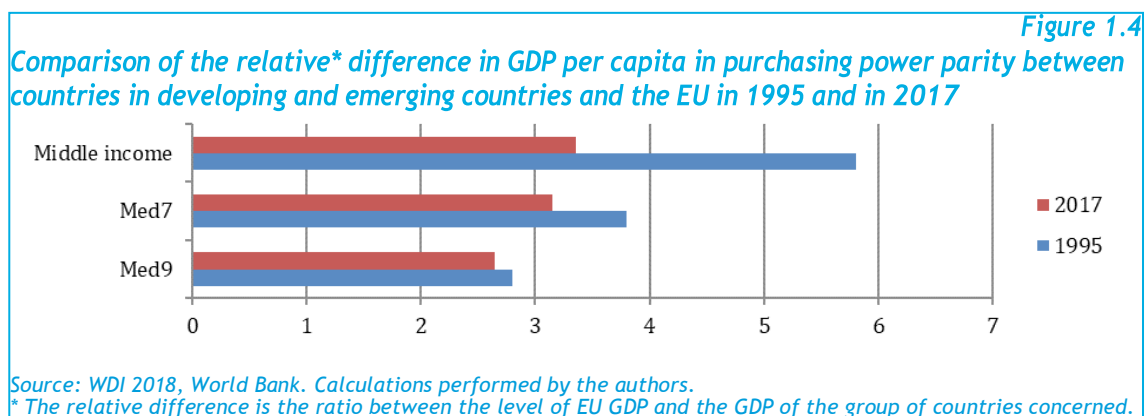
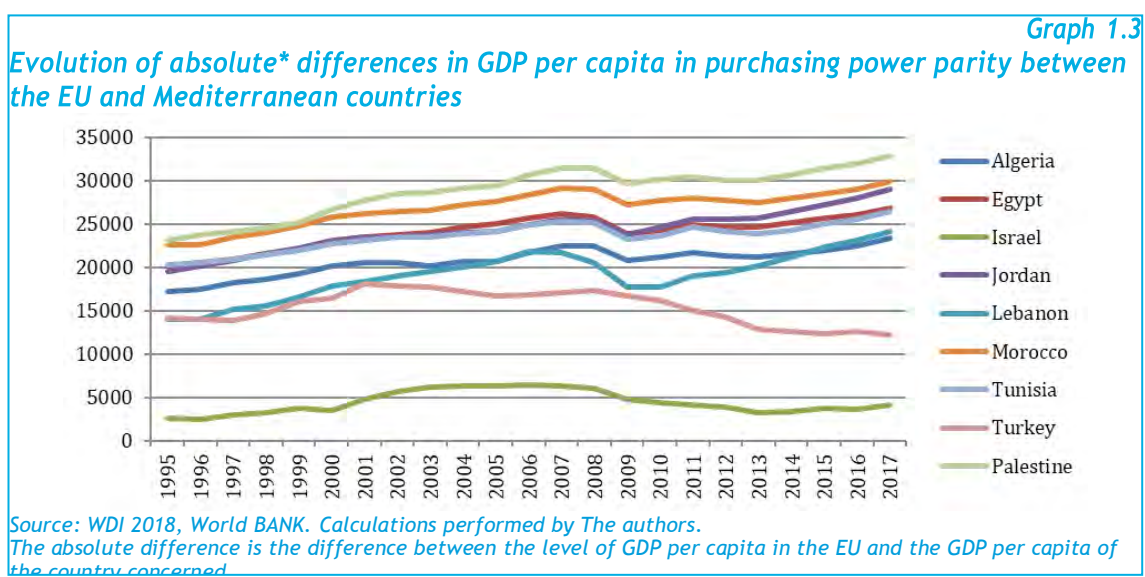
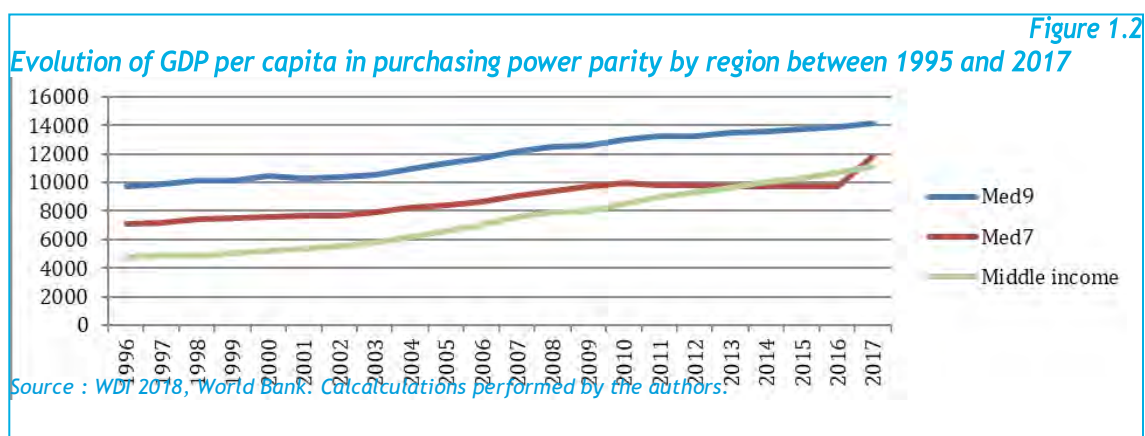
By Country		By Region	
Algeria	1,86	Med9	1,99
Egypt	2,41	Med7	1,83
Israel	1,63	East Asia & Pacific	6,78
Jordan	1,02	Europe & Central Asia	3,20
Lebanon	0,58	Latin America & Caribbean	1,33
Morocco	2,59	Sub-Saharan Africa	1,89
Tunisia	2,63	Upper middle income	4,42
Turkey	3,41	Lower middle income	3,75
Palestine	1,66	Middle income	4,04

Source: WDI 2018, World Bank. Calculations done by authors.

Med9: Algeria, Egypt, Israel, Jordan, Lebanon, Morocco, Tunisia, Turkey, Palestine

Med 7: Med9 except Israel and Turkey

Consequently, instead of declining, absolute differences [1] in living standards between the EU and Mediterranean countries have increased, except for Turkey, which is among those countries with a standard of living close to that of the EU (see Figures 1.3). When considering the relative differences [2] in standards of living, we can see that the convergence process between Mediterranean countries and the EU has been practically stagnant: in 1995, GDP per capita in purchasing power parity for Europeans was 3.8 times higher than the GDP per capita of the 7 Mediterranean partners. In 2017, this ratio was 3.1 (see Figure 1.4). The comparison with all comparable income countries is edifying. In 1995, the European standard of living was 5.8 times higher than that of middle-income countries. In 2017, this ratio fell to 3.4 (lower than the MED7 ratio).



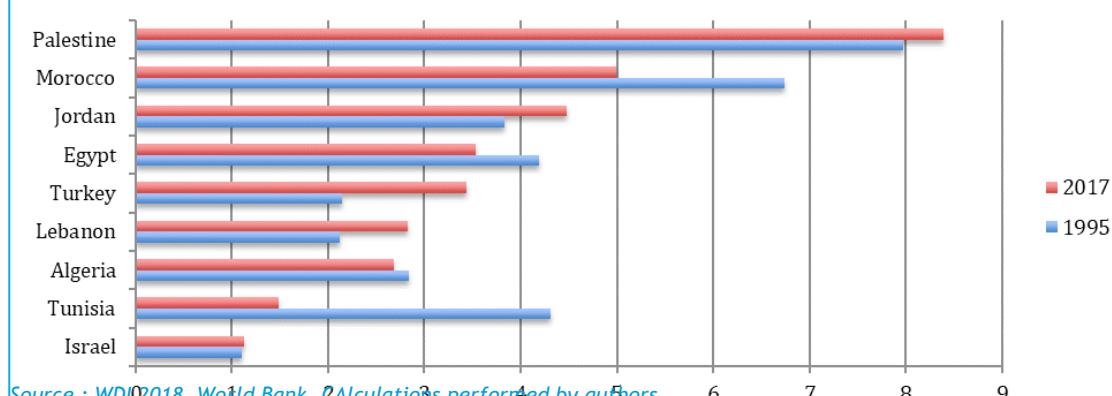
The distance between Palestinian Territories, Lebanon and Jordan from the European standard of living has become even greater (Figure 1.5). The countries that have converged towards the EU's GDP per capita in purchasing power parity are Turkey, Tunisia, Morocco, Egypt and Algeria.

### 1.3. Unemployment rates remain very high

With the exception of Israel and Lebanon, unemployment rates in the Mediterranean partner countries are very high. On average, **this rate was 12.4% in 2017**, whereas it was much lower in other developing regions: 4.1% in East Asia and Pacific countries, 8.3%

Figure 1.5.

Comparison of the relative\* difference in GDP in purchasing power parity per capita between Mediterranean countries and the EU in 1995 and 2017



Source : WDI 2018, World Bank. Calculations performed by authors.

\* The relative gap is the ratio between the level of EU GDP and the GDP of the relevant country.

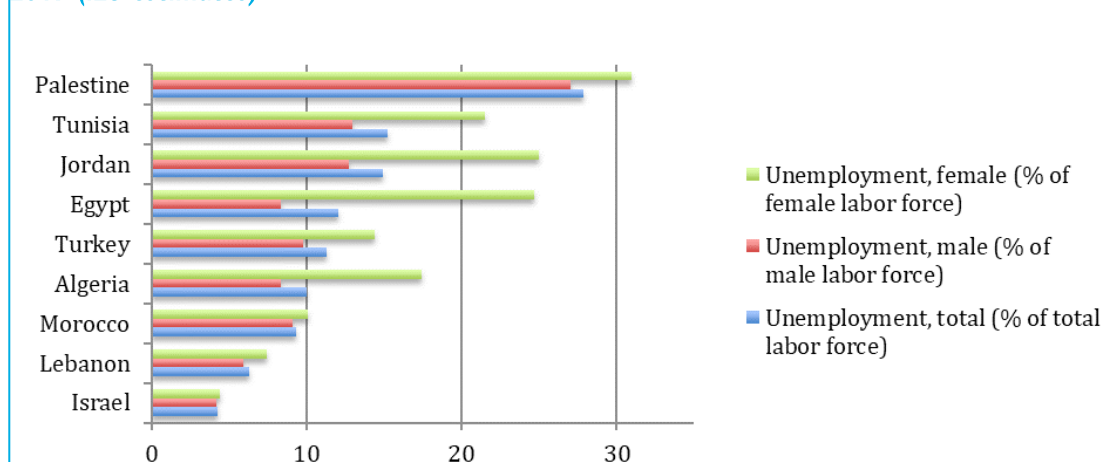
in Latin America and the Caribbean, 7.4% in the EU and Central Asia, 7.3% in Sub-Saharan Africa, and only 5.5% for all middle-income countries (Charts 1.6 and 1.7)

Moreover, **Mediterranean countries are characterised by particularly high unemployment rates among women** (17.3% on average for the MED9, 24.7% for Egypt, 31% for the Palestinian Territories and 25% for Jordan). In all Mediterranean countries, the female unemployment rate exceeds the unemployment rate for the entire active population.

To obtain a more accurate picture of the labour market, unemployment rates should be considered alongside participation rates [3], which show the proportion of people who are employed or unemployed, out of the total working-age population. These participation rates by Mediterranean partner country (Figure 1.8) and by region (Figure 1.9) are presented for the whole population and by gender.

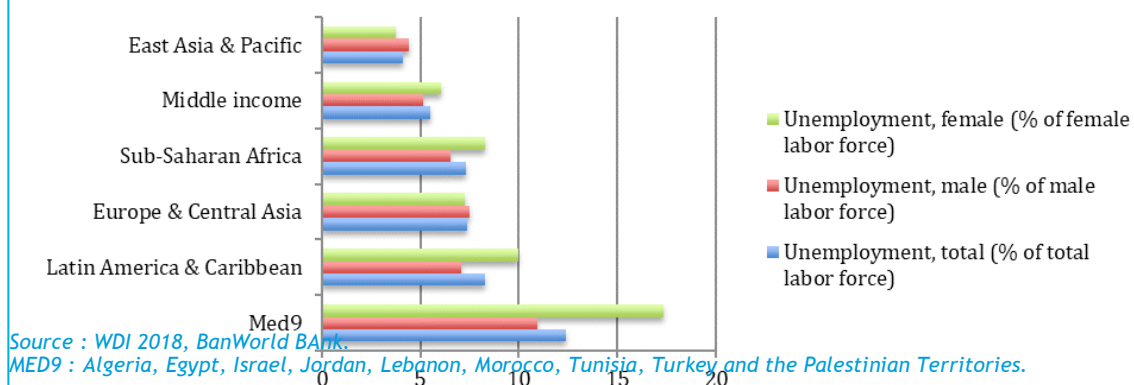
It is striking to note that, with the exception of Israel, **the participation rates of Mediterranean countries are particularly low.**

Figure 1.6. Total and gender participation rates in the Mediterranean partner countries in 2017 (ILO estimates)

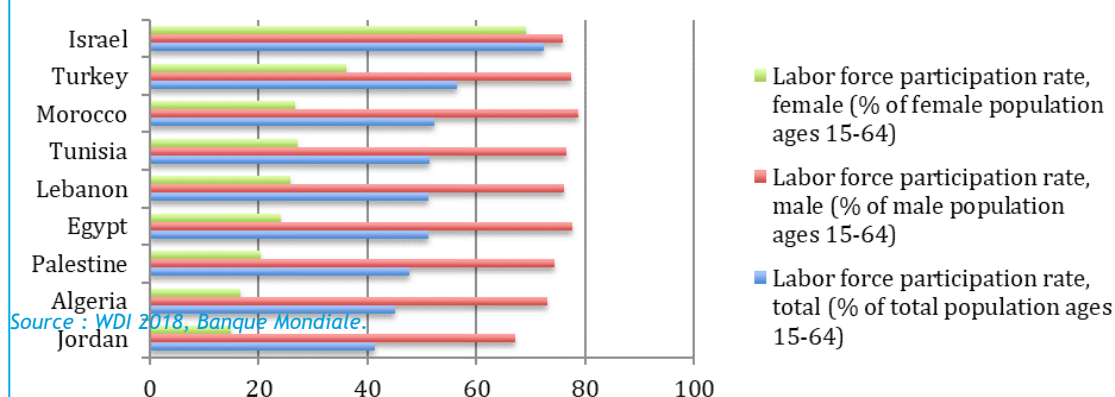


Source: WDI 2018, World Bank.

**Figure 1.7 Comparison of total and gender unemployment rates between developing regions in 2017 (ILO estimates)**



**Graph 1.8. Total and gender participation rates, in Mediterranean partner countries in 2017 (ILO estimates)**

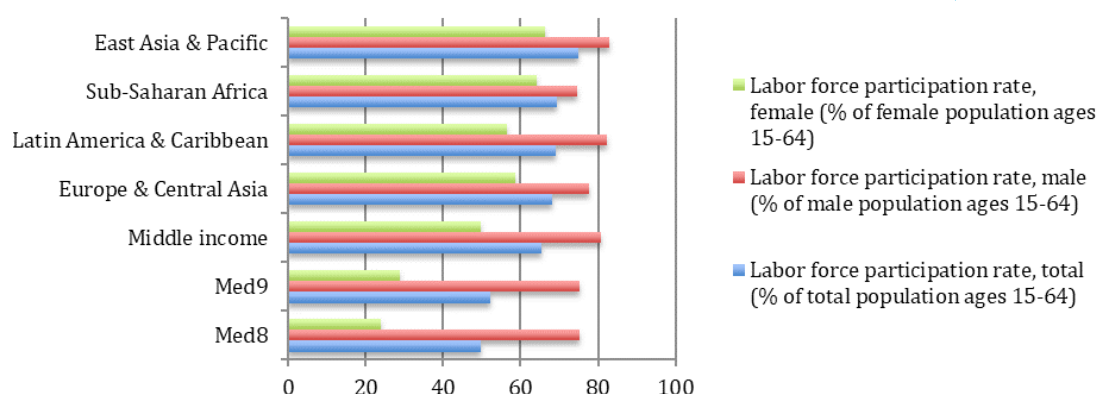


For the MED9, the average rate was 52.2% against 65.4% for all middle-income countries, 74.7% for East Asia and the Pacific, 69.4% for Sub-Saharan Africa, 69.2% for Latin America and 68% for Europe and Central Asia. Participation rates are fairly homogeneous among Mediterranean countries, ranging from 56.5% for Turkey to 41.4% for Jordan.

Male participation rates are slightly lower, on average, for Mediterranean countries than for other developing regions (75.3% for MED9 against 80.7% for all middle-income countries), but Mediterranean countries are mainly characterised by extremely low female

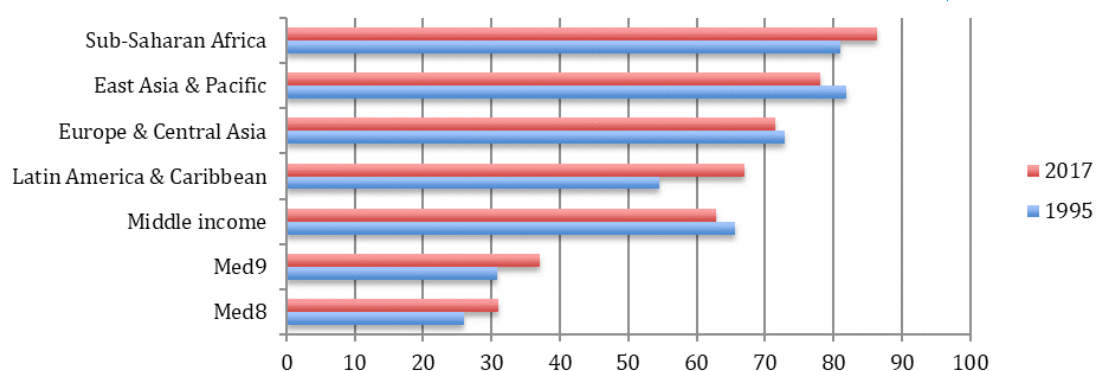
participation. The latter is 29% for MED9 and, even 24% without Israel, while for all middle-income countries as a whole, the participation rate for women is 49.7% (66.2% for East Asia and the Pacific, 64.3% for Sub-Saharan Africa, 58.8% for Europe and Central Asia and 56.5% for Latin America). We therefore note that, **there is a considerable gap in female participation rates, between Mediterranean countries and other developing regions.** This gap is also obvious if we calculate the ratio of the active female population to that of the active male population [4]. Figure 1.10 show that there is a big gap between Mediterranean partners

**Figure 1.9.**  
*Comparison of participation rates, total and by gender, between developing regions in 2017 (ILO estimates)*



Source: WDI 2018, World Bank

**Figure 1.10.**  
*Ratio of female to male labour force in 1995 and 2017 (ILO estimates)*



Source: WDI 2018, World Bank.

Med8 without Israel: Algeria, Egypt, Jordan, Lebanon, Morocco, Tunisia, Turkey and the Palestinian Territories.

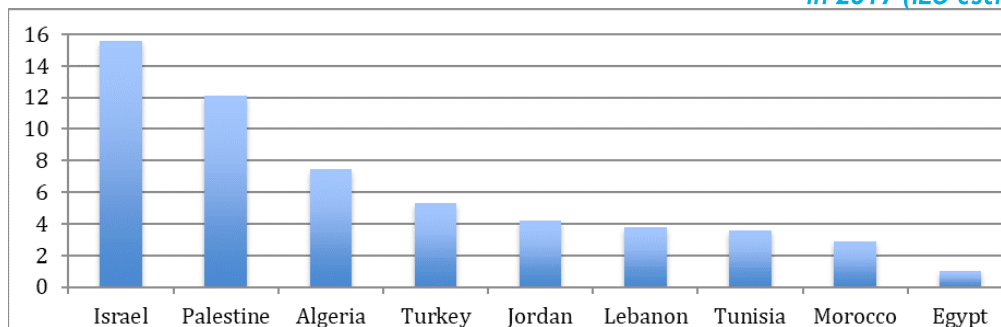
and other developing regions, as the former has a very low average ratio (31% [5] -without Israel-, as compared to 62.8% for all middle-income countries, 86.3% for Sub-Saharan Africa, 78.1% for East Asia and the Pacific, 71.5% for Europe and Central Asia and 66.9% for Latin America and the Caribbean). The ratios for Algeria (22.6%), the Palestinian Territories (27.2%), Jordan (21.9%) and Egypt (30.1%) are lower than the average for Mediterranean countries, Lebanon (32.6%), Morocco (33.7%) and Tunisia (34.4%) are barely above this average, followed by Turkey (45%) and Israel, whose ratio is almost 4 times higher than that of Algeria (Figure 1.).

Two other characteristics of Mediterranean countries' labour markets are the high levels of unemployment among the youth and among graduates.

**Concerning the youth unemployment rate**, the most heavily affected countries are the Palestinian Territories (44%), Jordan (40%), Tunisia (36%) and Egypt (34%) (Figure 1.12). **The average of Mediterranean countries, which stands at 27%, is well above that of the other developing regions** (from 11% for East Asia and the Pacific to 18.5% for Latin America and the Caribbean) (Figure 1.13). Although between 1995 and 2017, on average, the youth unemployment rate hardly

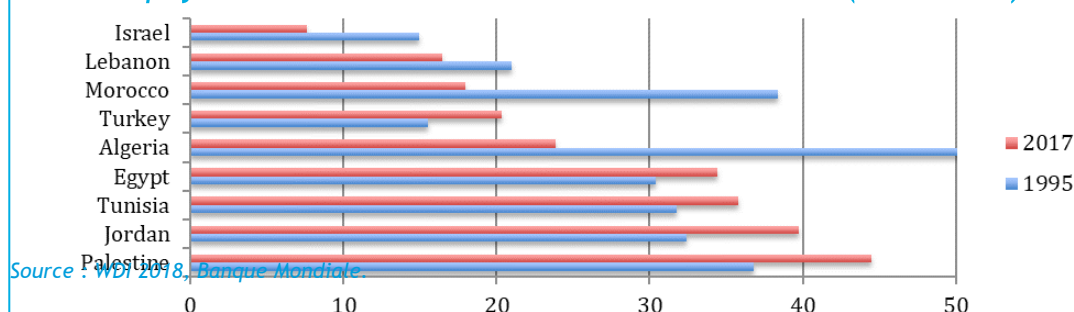


Figure 1.11.  
Ratio of female to male labour force by Mediterranean partner country  
in 2017 (ILO estimates)



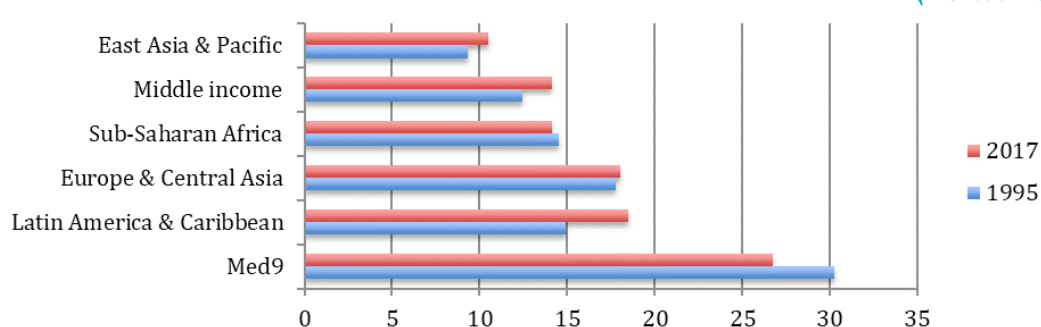
Source : WDI 2018, Banque Mondiale.

Figure 1.12.  
Youth unemployment rates in Mediterranean countries in 1995 and 2017 (ILO estimates)



Source : WDI 2018, Banque Mondiale.

Figure 1.13.  
Comparison of youth unemployment rates between developing regions in 1995 and 2017  
(ILO estimates)



Source: WDI 2018, Word Bank.

MED9: Algeria, Egypt, Israel, Jordan, Lebanon, Morocco, Tunisia, Turkey and the Palestinian Territories.

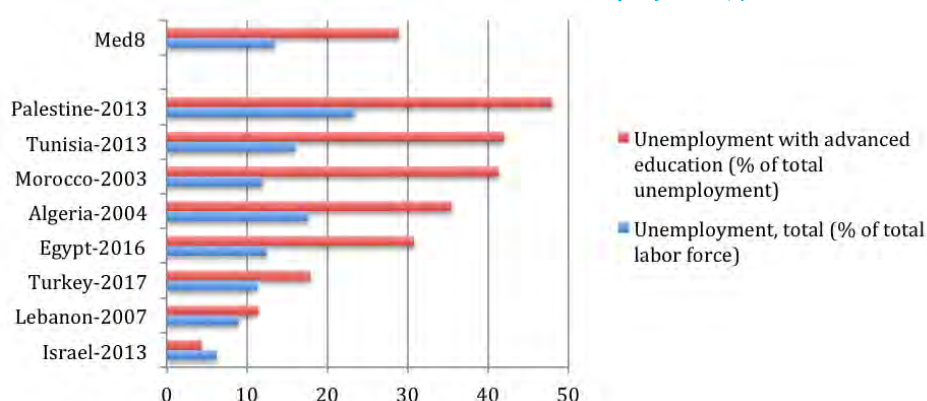
changed (it declined by only 4 percentage points over 20 years), the evolutions were highly heterogeneous between Mediterranean countries. The youth unemployment rate declined significantly in Algeria (-27 percentage points) and Morocco (-20 percentage points), it increased in the Palestinian Territories (+8 percentage points), Jordan (+7 points),

in Turkey (+5 points), Tunisia and Egypt (+4 points for these two countries).

**The unemployment rate for graduates** is not as well-documented, firstly because the average of the other developing regions is not available, and secondly because for Mediterranean countries, the data available is

Figure 1.14.

*Unemployment rate of graduates in Mediterranean countries, compared to the rate of total unemployment, for the most recent year \**



Source: WDI 2018, World Bank.

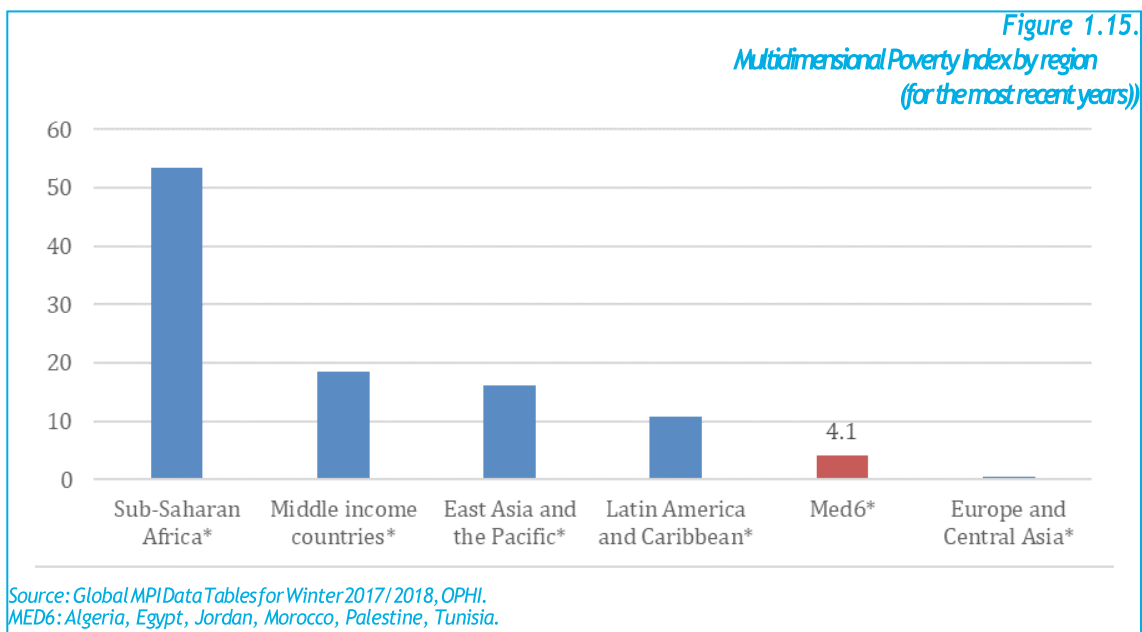
MED8: Algeria, Egypt, Israel, Lebanon, Morocco, Tunisia, Turkey and Palestinian Territories (Data for Jordan is not available). Note: The "Advanced education" level corresponds to university studies and all other training after high school

not always very recent. In Figure 1.14, the unemployment rate for graduates (i.e. those with a higher education) for the most recent available year (country-specific and specified in the Figure) is compared to the overall unemployment rate for the same year. With a regional average of 29%, we may note that **the unemployment rate for graduates is more than double that of the population as a whole**. The graduate unemployment rate reaches **48% in Palestine, 42% in Tunisia, 41.2% in Morocco, 35.4% in Algeria, 30.8% in Egypt, 18% in Turkey and 11.4% in Lebanon**. Israel is the only country in which this rate is proportionally lower than the overall unemployment rate: in 2013 (latest year available) the unemployment rate for graduates was 4.4%, while the overall unemployment rate was 6%.

#### **1.4. Poverty levels lower than in comparable countries but have not declined everywhere**

As shown by the Multidimensional Poverty Index [6], estimated at 4.1 for the region compared to 18.6 for all comparable income countries (see Figure 1.15), Mediterranean countries have lower poverty rates than all other developing and emerging countries.

Considerable progress has been made in this area over the past 20 years. This is the result of the development model implemented in all these countries in the 1970s, which has been described as a "social contract" or "authoritarian arrangement" (Yousef, 2004) and which consisted in leading civil society to accept the lack of individual freedom and expression as a counterpart to a kind of economic and social protection of the population by (i) creating a large number of public jobs (the State has become the main employer in the formal sector), (ii) providing free access to health care and education, (iii) investing in infrastructure, (iv) subsidising basic foodstuffs and fuel. Millions of people in the Arab world have thus emerged from extreme poverty. **The percentage of the population suffering from extreme poverty has fallen to 0.9%, while that of middle-income countries as a whole remains at 7.7%** (see Figure 1.16). However, it can be seen that **the incidence of poverty as a percentage of the entire population, measured on the basis of country-specific national poverty lines, has increased in recent years in two Mediterranean countries: in Egypt, the increase has been particularly strong as the**

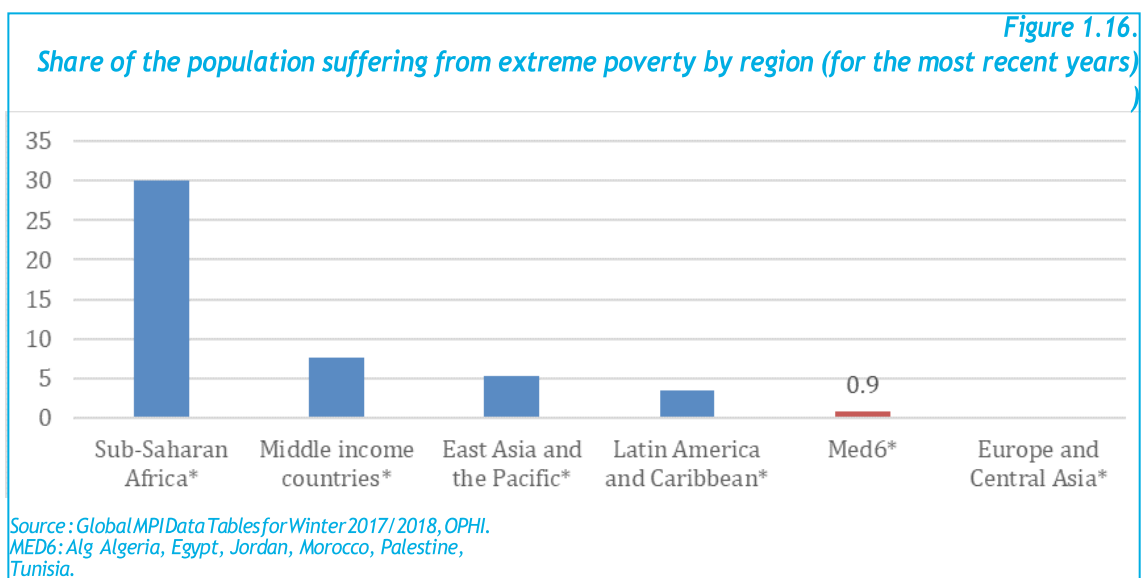


poverty rate rose from 16.7% in 1999 to 27.8% in 2015, and less pronounced in the case of Jordan, where the poverty rate rose from 13.3% in 2008 to 14.4% in 2010. In other Mediterranean countries for which data exists, the incidence of poverty, as share of the total population, has declined (Figure 1.17).

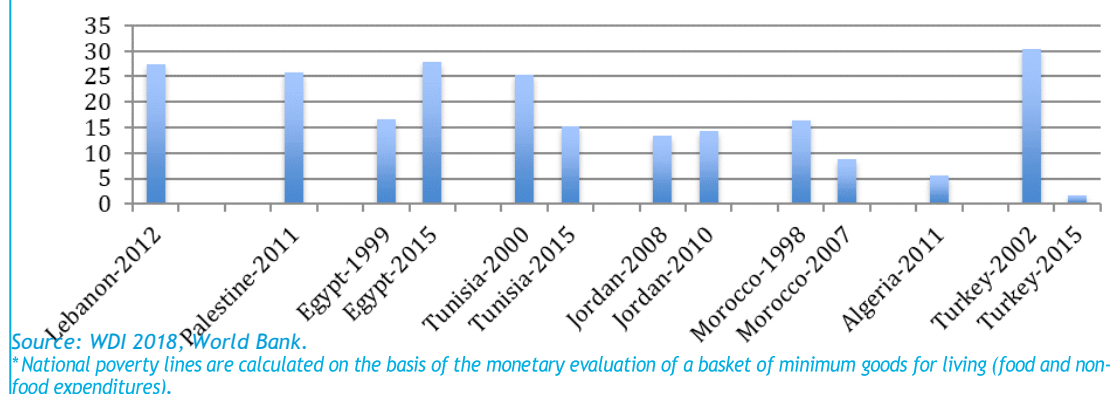
In addition, the poverty levels of the countries in the region and their urban-rural distribution are very heterogeneous. **On the basis of national poverty lines, once again, three countries have a poverty incidence among the population that exceeds 25% (Lebanon, Palestine and Egypt), two are around 15%**

(Tunisia and Jordan), Morocco and Algeria have shares of 9% and 5.5% respectively, while this share has fallen to 1.6% in Turkey.

For most countries, poverty rates in rural areas are higher than in urban areas. The largest differences are recorded in Egypt (32.3% in rural areas, 15.3% in urban areas), Morocco (14.4% against 4.8%) and Turkey (5.1% against 0.6%). In Jordan, the gap is only 3 percentage points (16.8% as compared to 13.9%). In Palestine, however, the poverty rate is higher in urban areas

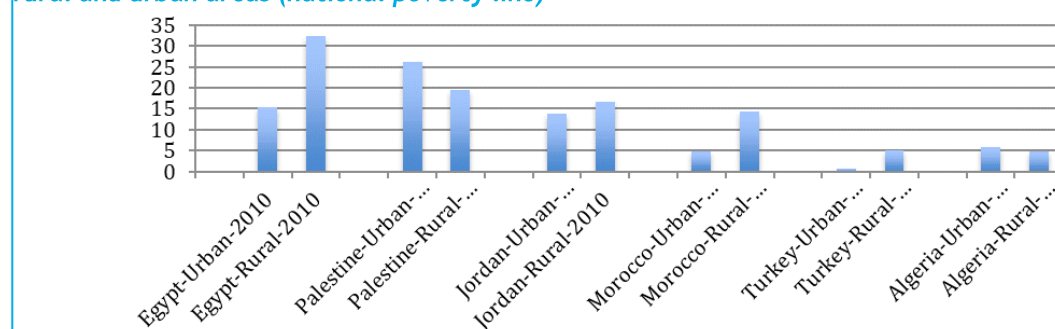


*Incidence of poverty as a percentage of the total population for the first and last year available (national poverty line\*)*



**Graph 1.18.**

*Incidence of poverty as a percentage of the total population for the latest year available, in rural and urban areas (national poverty line)*



(19.4% in rural areas compared to 26.1% in urban areas, see Figure 1.18).

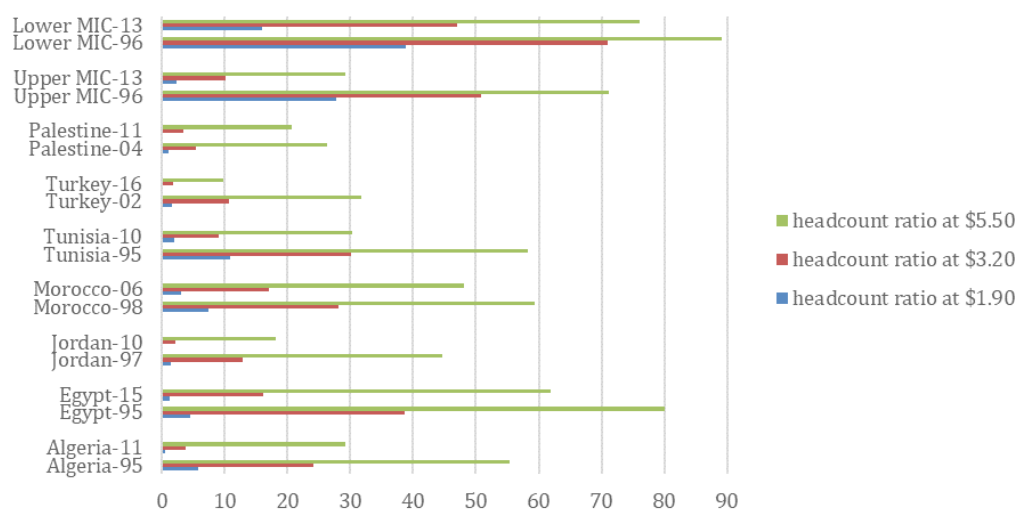
The use of international poverty thresholds (Figure 1.19) yields very different poverty proportions compared to those obtained from national thresholds [7]. This figure highlights two findings. Firstly, regardless of the international threshold, the incidence of poverty has decreased for each of the Mediterranean countries. The reduction of poverty has been particularly significant in Tunisia, Morocco and Algeria: with a threshold of \$3.20 per day, it dropped respectively from 30.1% in 1995 to 9.1% in 2010, from 28.2% in 1998 to 17% in 2006, and from 24.1% in 1995 to 3.9% in 2011. Secondly, the proportion of the population in Mediterranean countries that are considered to

be poor (either at the \$1.9 threshold or at the \$3.2 threshold) is lower than that observed in comparable developing or emerging countries.

An important dimension to consider when addressing poverty is the vulnerability of populations. This corresponds to the proportion of individuals living close to the poverty threshold, not otherwise considered poor, but who could become poor at the slightest shock, whether exogenous (political, environmental, economic, climate, etc.) or specific to the individual (illness, lack of work, etc.). To assess the countries' levels of vulnerability, we extracted the share of the population

Figure 1.19.

*Incidence of poverty as a percentage of the total population for the first and last year available (international poverty lines at \$1.90, \$3.20 and \$5.50 per day)*



Source: WDI 2018, World Bank.

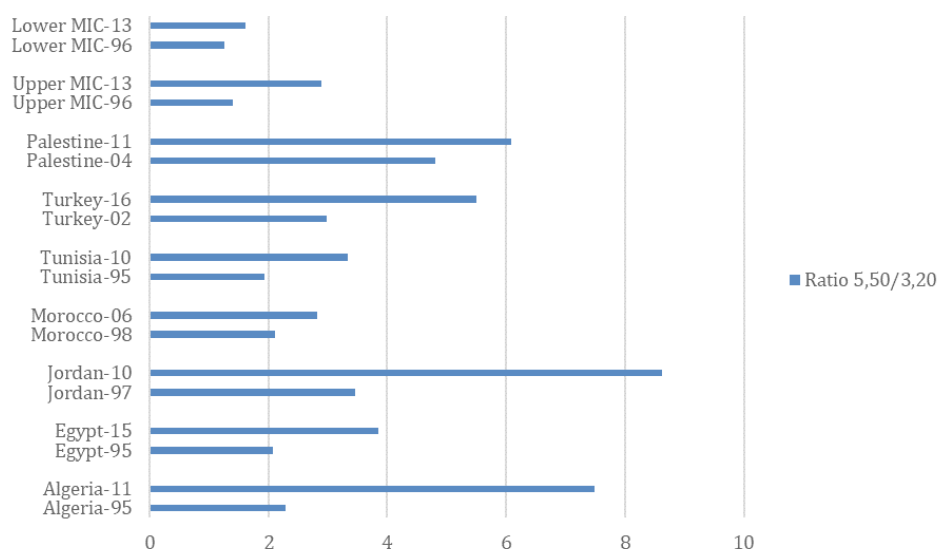
who lives on less than \$5.5 per day, then we calculated the ratio of this share to that of the population living below the \$3.20 threshold (graph 1.20).

Although the share of the population living below the \$5.5 per day threshold is high (about 30% for Tunisia and Algeria, 48% in Morocco and up to 62% in Egypt), this share has declined

everywhere. The important point here, however, is that the decline in this share was much smaller than that of the share of the population living below the \$3.20 threshold. Consequently, our vulnerability indicator (i.e. the ratio: population share below \$5.5 over population share below \$3.2) has increased for all countries or groups of countries compared to all developing or emerging countries

Figure 1.20.

*Vulnerability to poverty indicator\* for the first and latest year available*



Source: WDI 2018, World Bank.

\*Our vulnerability to poverty indicator corresponds to the ratio of population share below the \$5.5 threshold to population share below the \$3.2 threshold.



**the Med countries show the greatest increase in vulnerability to poverty.**

### **I.5. Relatively low levels of inequality but increasing inequities**

Mediterranean countries have generally lower levels of inequalities than other developing and emerging countries, although, once again, there are marked differences between them, since, as can be seen in Figure 1.21, the Gini coefficient [8] ranges between 27.6 for Algeria and 41.9 for Turkey. It has decreased in only 3 countries (Algeria, Jordan and Tunisia), has remained more or less stable for Morocco, Turkey and Palestine and has slightly increased in Israel and Egypt. The ratio between the incomes of the richest 20% and the poorest 20%, confirms **a more egalitarian distribution of the wealth created in the Med region than in other comparable income countries.** The Mediterranean countries with the highest levels of inequality are Israel (the richest 20% earn almost 10 times more than the poorest 20%), Turkey (with a ratio of 8.5), followed by Morocco (ratio of 7.4) and Tunisia (ratio of 6.4).

Beyond differences in wealth or income (or expenditure), which are so-called vertical inequalities, the populations' sense of inequality or inequity

may be fuelled by other factors whose effects may be even more damaging to the stability and equilibrium of societies. In Mediterranean countries, the emergence of these factors of inequity is linked to the erosion of the old social contract, which is no longer sustainable at all: public services have deteriorated considerably, food and fuel subsidies have been reduced and, above all, as the State is no longer in a position to recruit, employment opportunities, especially for young people are increasingly reduced.

One of the main manifestations of the degradation of public services is the sharp decline in the quality of health and education. In the region, more than 49% of the population report that they are dissatisfied or very dissatisfied with the education system. This proportion rises to 56% for health services (Figure 1.23). The Egyptian population voices the greatest dissatisfaction (with about 72% dissatisfied with both education and health), followed by Algeria (about 62% dissatisfied in both areas), Morocco (56% regarding education and 71% regarding health), Tunisia (58% regarding education and 60% regarding health), Palestine (51% regarding education and 49% regarding health) and Lebanon where the population is essentially dissatisfied with the health system (60% of the population is dissatisfied). The results from the latest set of surveys carried out by the



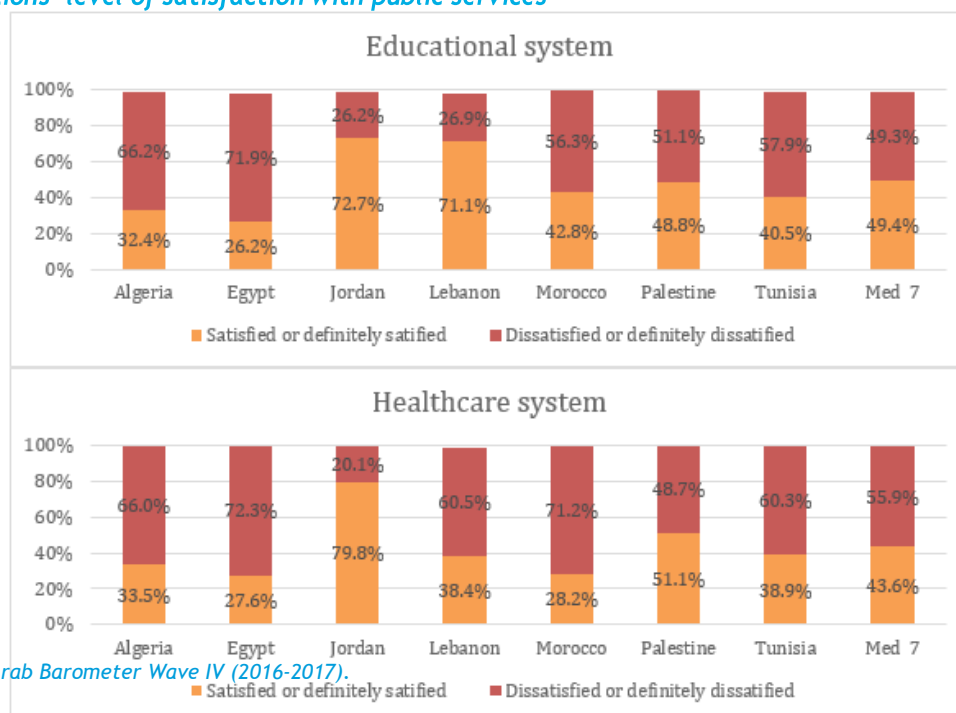
Arab Barometer are consistent with the testimonies and findings reported in the literature. According to a 2013 World Bank report, one woman in Egypt said "you can go to the private health centre and lose your money or go to the public health centre and lose your life". Where data exists, as in the case of Egypt and Morocco, absenteeism rates among doctors in health centres range from 20 to 30% (Brixi et al., 2015). Schools lack basic supplies, medicines are very often out of stock and clinics are often closed as the doctors are absent from work.

at the bottom of the rankings. These difficulties, both in health and education, affect poor rural areas even more extensively. In a nutshell, students are poorly educated and people receive poor medical attention. Faced with this situation, people have no choice but to turn to the private sector, which can be costly. In Egypt, 70% of students have private tuition (Dang and Rogers, 2008).

In the field of education, teacher absenteeism is also high. Scores obtained by Mediterranean countries in international assessments on the acquisition of students' knowledge and skills (such as PISA an OECD initiative) generally place them

Figure 1.23.

#### Populations' level of satisfaction with public services



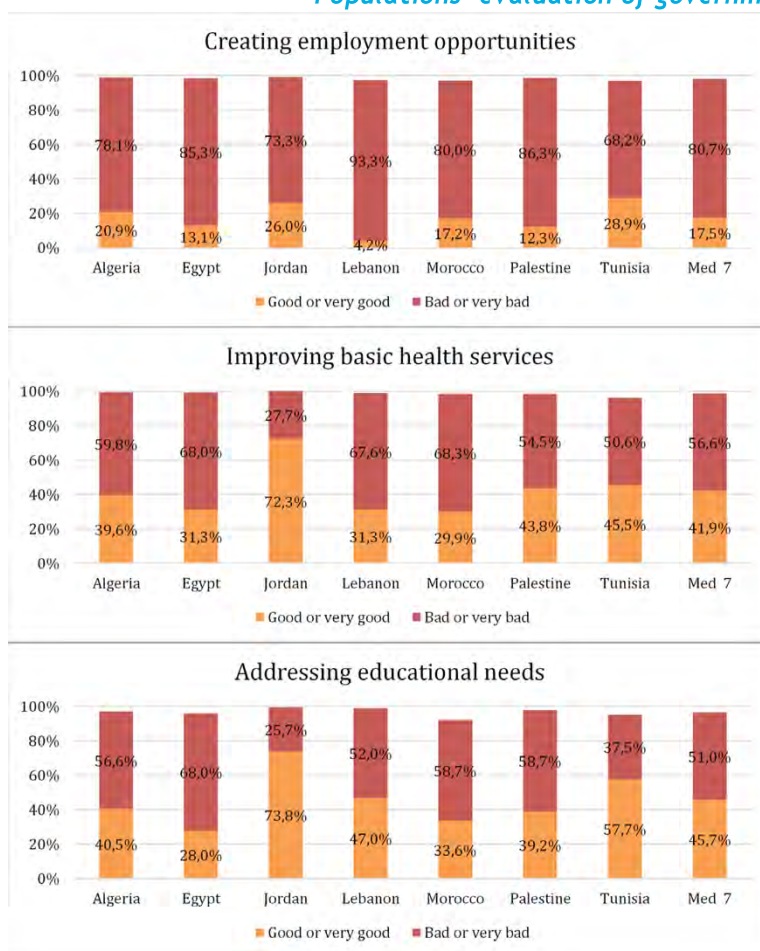
Source: Arab Barometer Wave IV (2016-2017).

Where their income allows it, families prefer to place their children in private schools. This creates an even greater disadvantage for poor populations. The gap is widened even further by the fact that those who can afford to, seek health care within the private sector.

Sen (1999), demonstrated that development must above all aim to broaden the "possibilities" or "potentialities" offered to people so that they may live the life they choose to lead. Economic development must therefore reduce the sources of "potential deprivation" that prevent people from benefiting from their intrinsic qualities and the efforts they wish to make (investment in education, work, etc.) to achieve their goals or simply to escape poverty. The lack of access to

quality education and lack of access to health care are the two main sources of "deprivation of potential" since they remove all opportunities for an individual to choose the life they lead. Conditions of access to education and health are therefore the pillars of a fair society. It is clear that the lack of access to formal employment also reduces the opportunities that an economy must provide for people. In addition, a country that does not eliminate, or at least reduce, the sources of deprivation of potential or opportunities, is a country that cannot achieve sustainable development as it under-utilizes the human capital of a large proportion of its population. In a society that defends the foundations of equity between people, wealth inequalities

**Figure 1.24.**  
**Populations' evaluation of government effectiveness**



Source: Arab Barometer Wave IV (2016-2017)

can be accepted. However, inequalities that constrain people's lives, preventing them from doing what they want and from using their own capacities and intrinsic qualities, are unacceptable as they undermine societies. Also, allowing this type of inequality to take root in a region marked by conflict, political turmoil and potentially rising religious extremism would be the worst turn of events for Mediterranean countries. In this respect, the results of the latest surveys conducted by the Arab Barometer are alarming, since 81% of the region's population consider that the governments' effectiveness in creating employment opportunities is "bad" or "very bad" (figure 1.24). Survey respondents are a little harsh regarding the effectiveness of governments in meeting educational needs and improving health services since 51% (for education) and 57% (for health) consider it to be "bad" or "very bad". Clearly, the increased sense of inequity and loss of trust in public services affects (i) political institutions, making them weaker and (ii) decision-makers, who suffer a loss in credibility.

## II. The evolution of Mediterranean exports

### II.1. An imbalanced composition of exports by country

Turkey and Israel largely dominate regional exports. In 2017, they alone accounted for about two thirds of Mediterranean exports (their share was 62.5% in 1995). Turkey's weight has increased considerably, from 33.2% in 1995 to 47% in 2017 (Figure 1.25). If we exclude these two countries (Figure 1.26), most of the trade is carried out by Algeria, Morocco, Tunisia and Egypt. The shares of Algeria and Tunisia decreased (from 38.3% to 30% and from 22.4% to 12% between 1995 and 2017). Those of Morocco and Egypt increased (from 19% to 22% for Morocco and from 14% to almost 22% for Egypt). Jordan's share of the region's exports (excluding Turkey and Israel) has remained more or less stable (from 6% to 5%). While Lebanon and Palestine represent 8% and 1% of Mediterranean exports respectively (excluding Turkey and Israel).

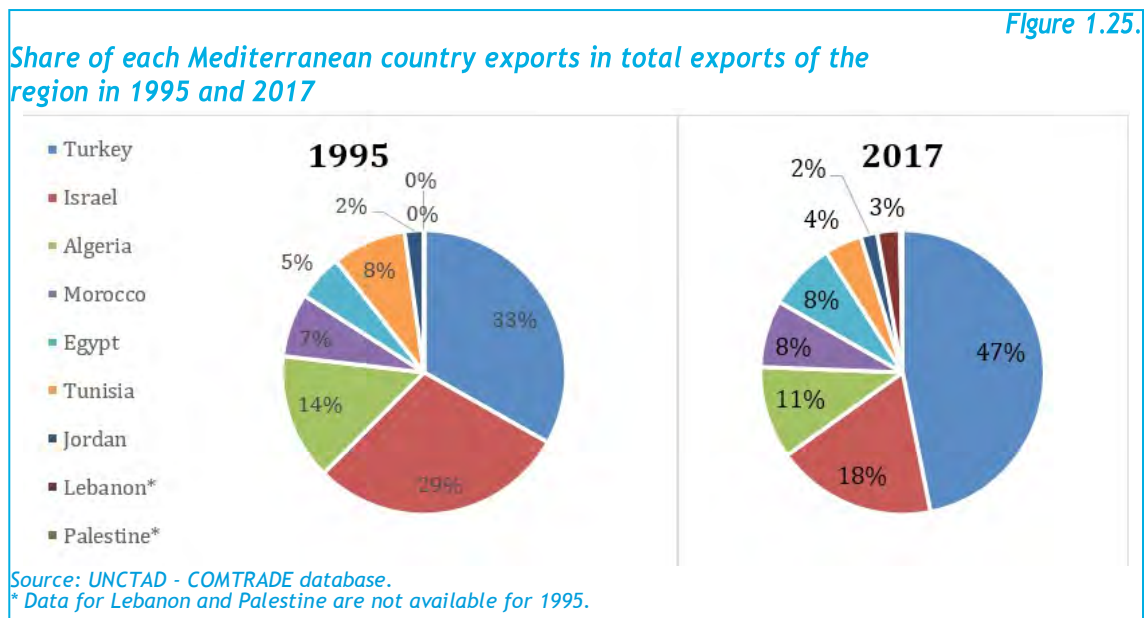
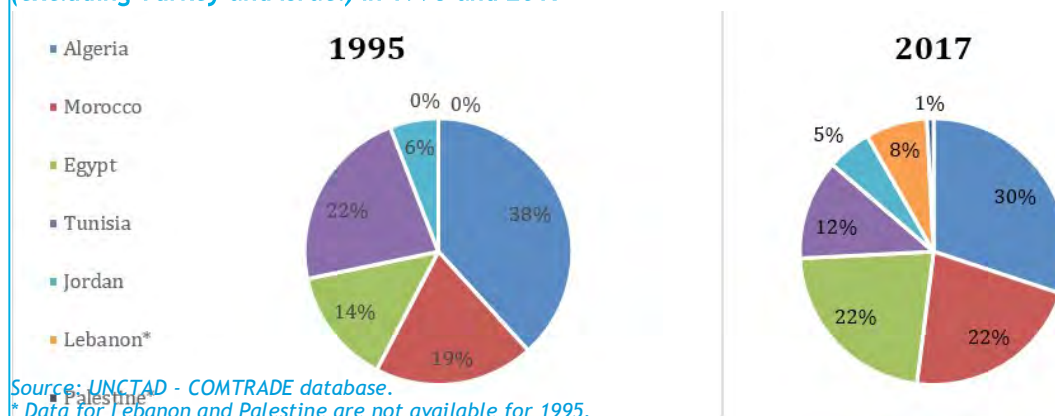


Figure 1.26.

Share of each Mediterranean country exports in the region's total exports (excluding Turkey and Israel) in 1995 and 2017



## II.2. Relatively low export growth rates

Exports from all Mediterranean countries increased by about 413% between 1995 and 2017 (Figure 1.27), which is well below all comparable income countries (+672%), and below all regions of South Asia (+659%), East Asia and the Pacific (+765%) and Europe (+1,884%). The only regions with a lower performance were Latin America (+278%) and Sub-Saharan Africa (+432%).

Among the Mediterranean countries, four countries have driven up the region's export rate (Figure 1.28); these are Jordan (600%), Egypt (+550%), Turkey (+525%) and Lebanon (+492%). The 400% growth rate of Moroccan exports between 95 and 2017 is close to the regional average. The other four countries did less well than this average (200% for Israel, 190% for Algeria, 150% for Tunisia and 46% between 2000 and 2017 for the Palestinian Territories, data for this country relative to previous periods is not available).

Figure 1.27.

Comparison of the evolution of Mediterranean country exports with groups of comparable countries

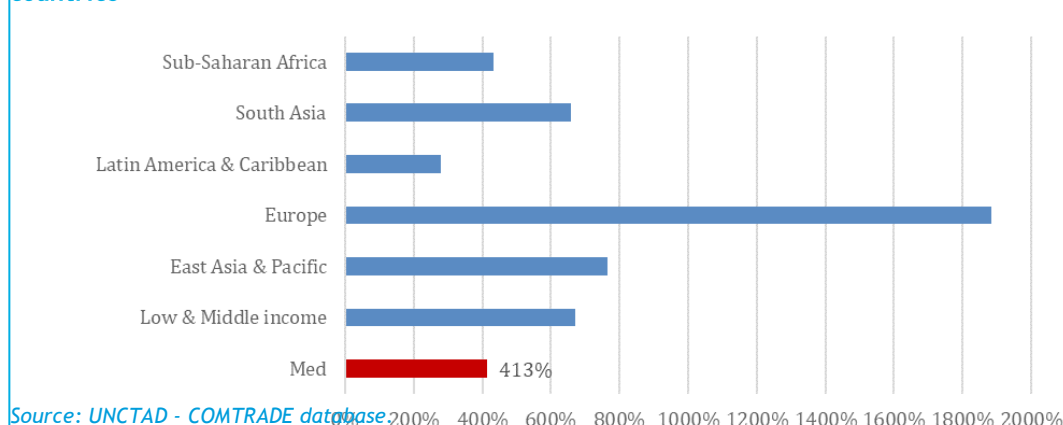
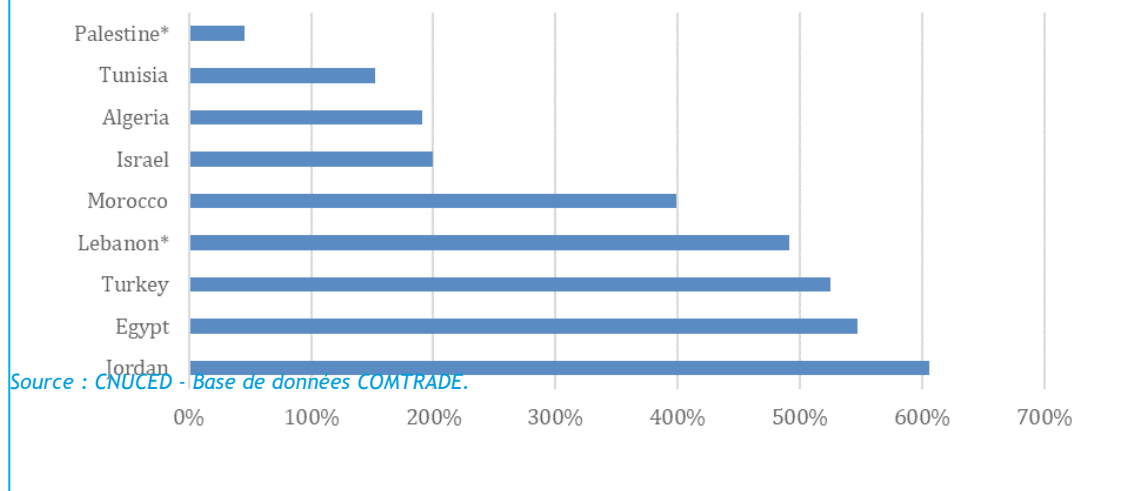




Figure 1.28.

### Growth rates of Mediterranean country exports between 1995 and 2017



### II.3. Evolving destinations, but regional integration remains very weak

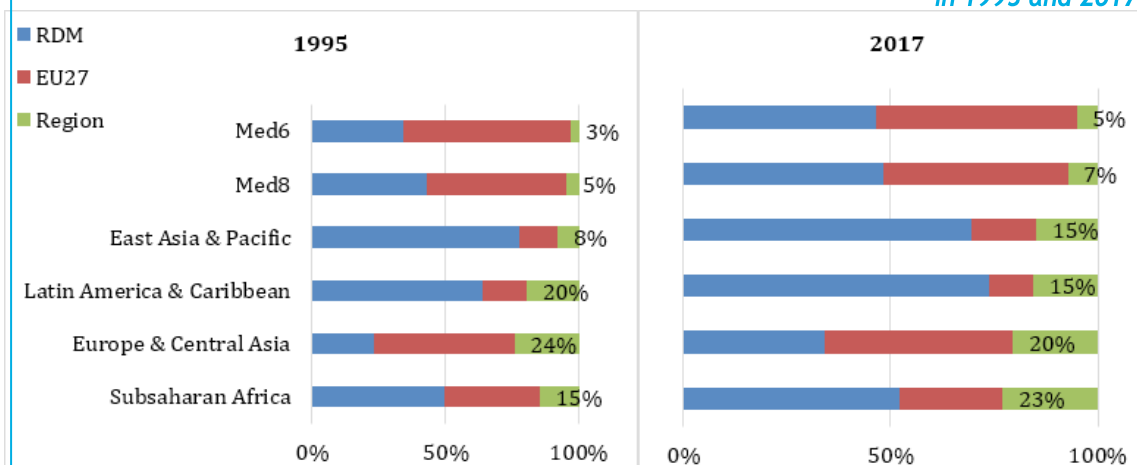
The distribution of exports between three major destinations (the EU, the countries of the Region and the Rest of the World, Figure 1.29) reveals two striking facts.

- The first is that **the share of Mediterranean exports to the EU declined between 1995 and 2017**, by 8 percentage points for all Med countries (from 53% to 45%) and by 14 percentage points for Med countries excluding Turkey and Israel (from 63% in 1995 to 48% in 2017). To a greater or lesser extent, this trend concerns all Med countries except for Morocco, whose share of exports to the European market has remained almost stable (from 63% in 1995 to 66.5% in 2017, Figure 1.30). The most significant decline was in Lebanon (22 percentage points) and Egypt (19 percentage points). Two countries (Algeria and Turkey) saw their share of exports to the European market decline by about 8 and 10 percentage points while for Jordan, Tunisia and Israel the decline was around 4 to 5 points. In 2017, the export shares of Mediterranean countries to the EU were even more heterogeneous than they were in 1995. These shares were

by 74% for Tunisia, 66.5% for Morocco, 58% for Algeria, 48% for Turkey, 48% for Israel, 30% for Israel, 29% for Egypt, 3.7% for Lebanon and 2.8% for Jordan.

- The second is that **this relative decline in exports to the EU has not really benefited regional integration. The share of Med countries' exports within the region increased by only 2.7 percentage points between 1995 and 2017**. In contrast, the share for the Rest of the World increased by 6 percentage points for all Med countries and by 12.6 percentage points for med countries excluding Israel and Turkey. In all, **in 2017, regional trade accounted for only 7% of their exports and only 5% if Israel and Turkey are excluded**. In other developing regions, the proportion of regional trade out of total exports is much higher: 23% for Sub-Saharan Africa, 20% for European developing countries, 15.5% for Latin American countries and 15% for East Asia. Moreover, individually, no Med country has significantly redirected its exports to the regional market, since the increase in this regional share in each of their exports ranges from 1.2 percentage points for Israel to 5.5 percentage points for Egypt.

Figure 1.29.  
Main export destinations of all Med countries and other developing regions in 1995 and 2017.



Source: UNCTAD - COMTRADE database.

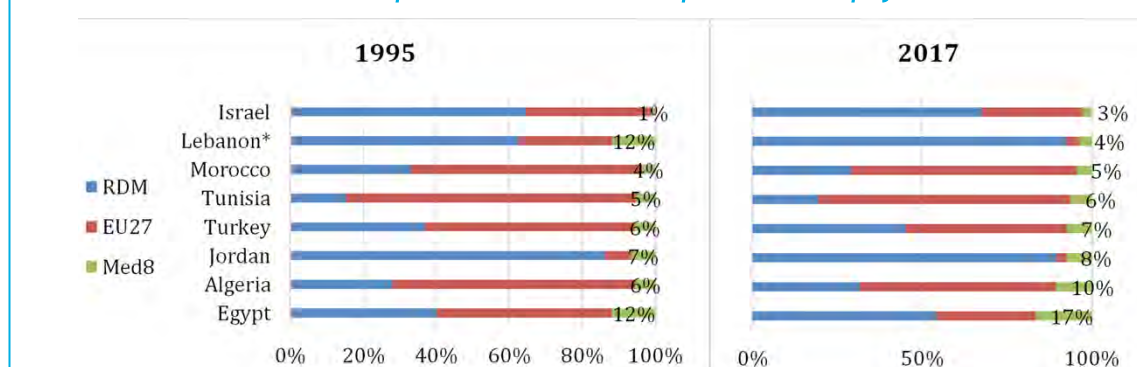
It should be noted that we have not included Palestine (which represents less than 1% of the region's exports as seen previously), since more than 80% of Palestinian exports go to Israel.

The Med countries' main export partner countries changed very little between 1995 and 2017 (Figure 1.31). The four largest markets remained the United States, France, the United Kingdom and Italy. Among the top 10 main destinations in 2017, 7 countries already figured among the top 10 in 1995. These were solely European countries: to the three European countries mentioned previously,

we may add Spain, the Netherlands and Germany. Between 1995 and 2017, three countries declined (Belgium, Japan and Russia) and were replaced by Iraq, the United Arab Emirates and China. The destination structure was, however, more balanced in 2017 than in 1995: on the one hand, the shares of each of the top 10 partner country destinations were more homogeneous and, on the other hand, the top 10 in 1995 represented 66% of total exports compared to 52% in 2017.

If we focus on the Rest of the World (Figure 1.32), even though among the top 10 destination countries in 2017, six were already among the top 10 in

Graphique 1.30.  
Principales destinations des exportations des pays med en 1995 et 2017



Source : CNUCED - Base de données COMTRADE.

\* Données 1997 pour le Liban.

Figure 1.31.

**Top 10\* of the main destination countries for exports from all Mediterranean countries 1995\*\* and 2017\*\***

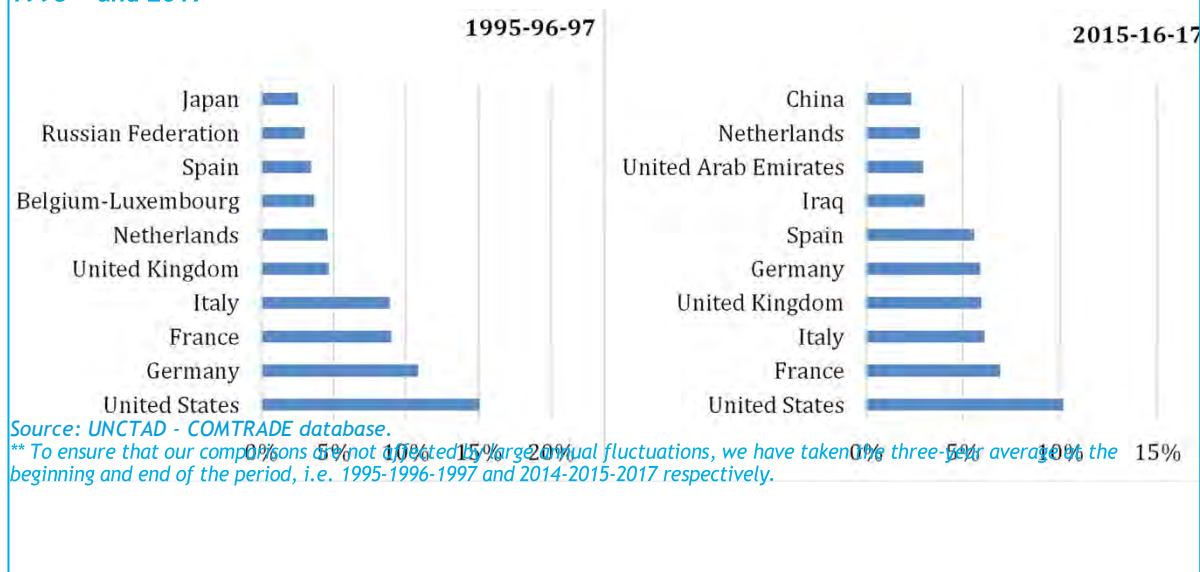
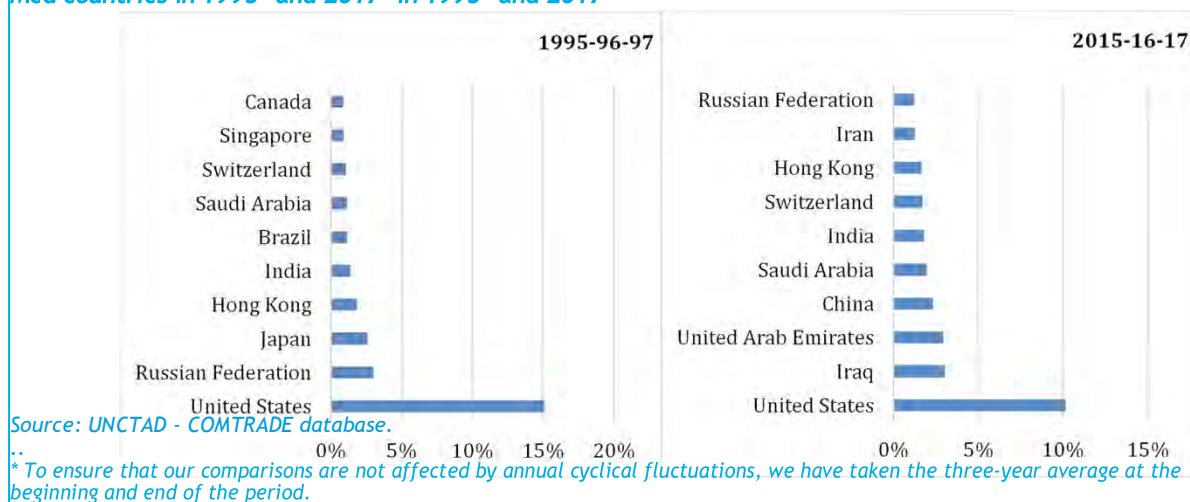


Figure 1.32.

**Top 10 main destination countries (excluding EU and Med countries) for exports of all Med countries in 1995\* and 2017\* in 1995\* and 2017\***



1995 (namely, the United States, Russia, Saudi Arabia, Hong Kong, Switzerland and India) and that four new countries (Iran, Iraq, the United Arab Emirates and China) replaced the four outgoing countries (Japan, Canada, Singapore and Brazil), the composition of countries from the Rest of the World receiving Mediterranean exports changed more significantly: whereas in 1995, the four most important markets were the United States and Russia,

Japan and Hong Kong, in 2017, these became the United States, Iraq, the United Arab Emirates and China.

#### II.4. A trend towards the export diversification for certain Med countries

**Med countries export a greater number of products, on average, than all other countries with comparable incomes.**

Figure 1.33.  
Number of products exported by Med countries in comparison with other developing countries and emerging markets in 1995\* and 2017\*

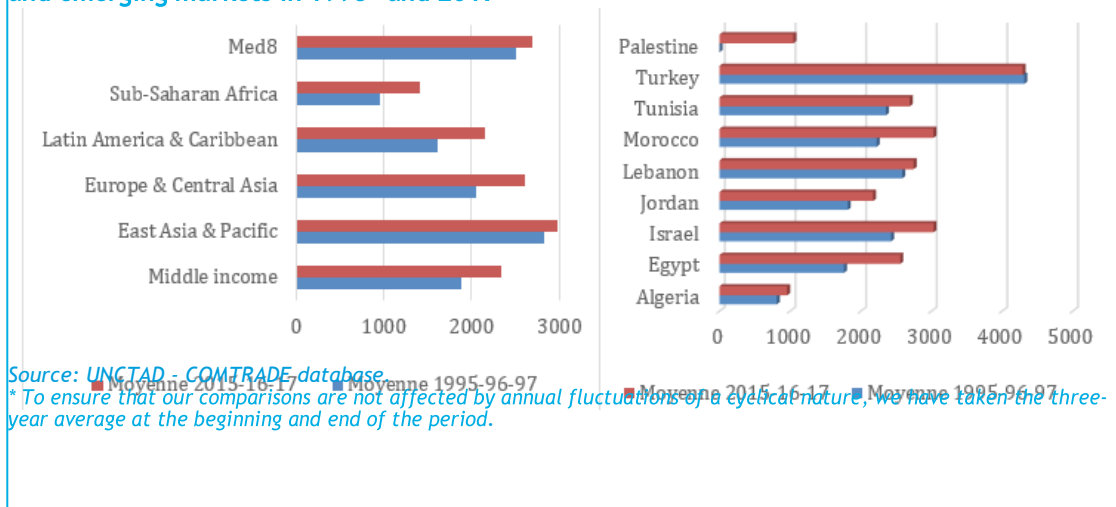
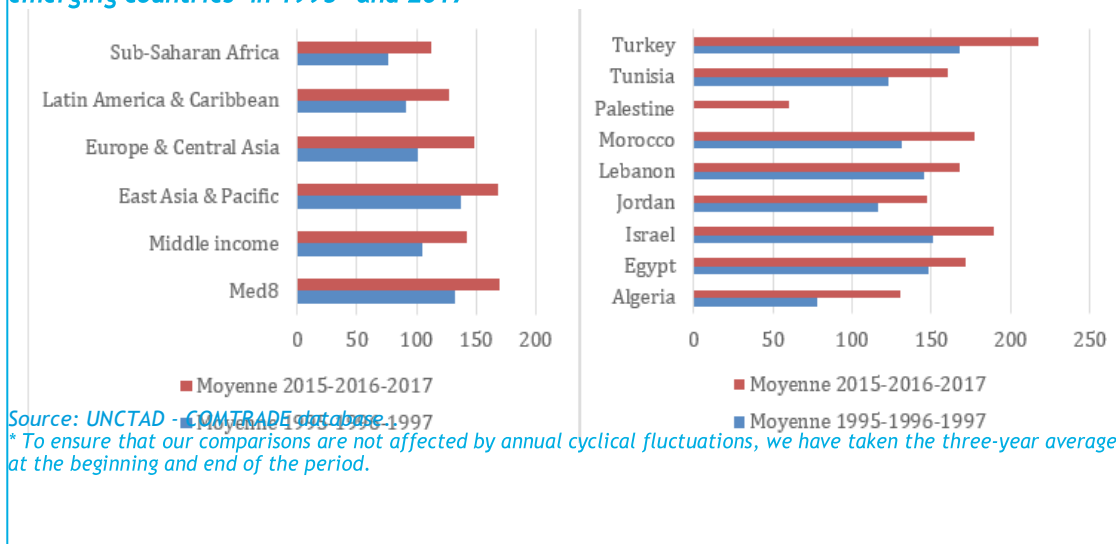


Figure 1.34.  
Number of products of Med country export partners in comparison with other developing and emerging countries in 1995\* and 2017\*



Only East Asian countries outperform them. However, the number of products exported has only slightly increased in 20 years, from 2,500 in the mid-1990s to 2,700 today (Figure 1.33, left-hand chart). The diversification of exports in number of products is highly heterogeneous between the countries of the region. Algeria exports less than 960 products, while Turkey exports almost 4,300 products. Since the beginning of the Barcelona Process, all have increased the number of exported products. We may note that after Turkey,

Morocco and Israel are the countries that have exported the greatest number of products (about 3,000), followed by Lebanon (2,750), Tunisia (2,700), Egypt (2,560), Jordan (2,200), Palestine (1,050) and, as already mentioned, Algeria (960) (right-hand chart in Figure 1.33).

**In terms of number of partners, Med countries exceed all comparable income countries with levels that are on a par with East Asian countries.** They have increased from an average of 132 partners in the mid - 1990s

to

170 in the recent years. Although all have increased their number of export partners, the situation between the Med countries remains very different between countries: Turkey has 217, Israel 189, Morocco 177, Egypt 172, Lebanon 168, Tunisia 160, Jordan 147, Algeria 130 and Palestine 60 (see Figure 1.34).

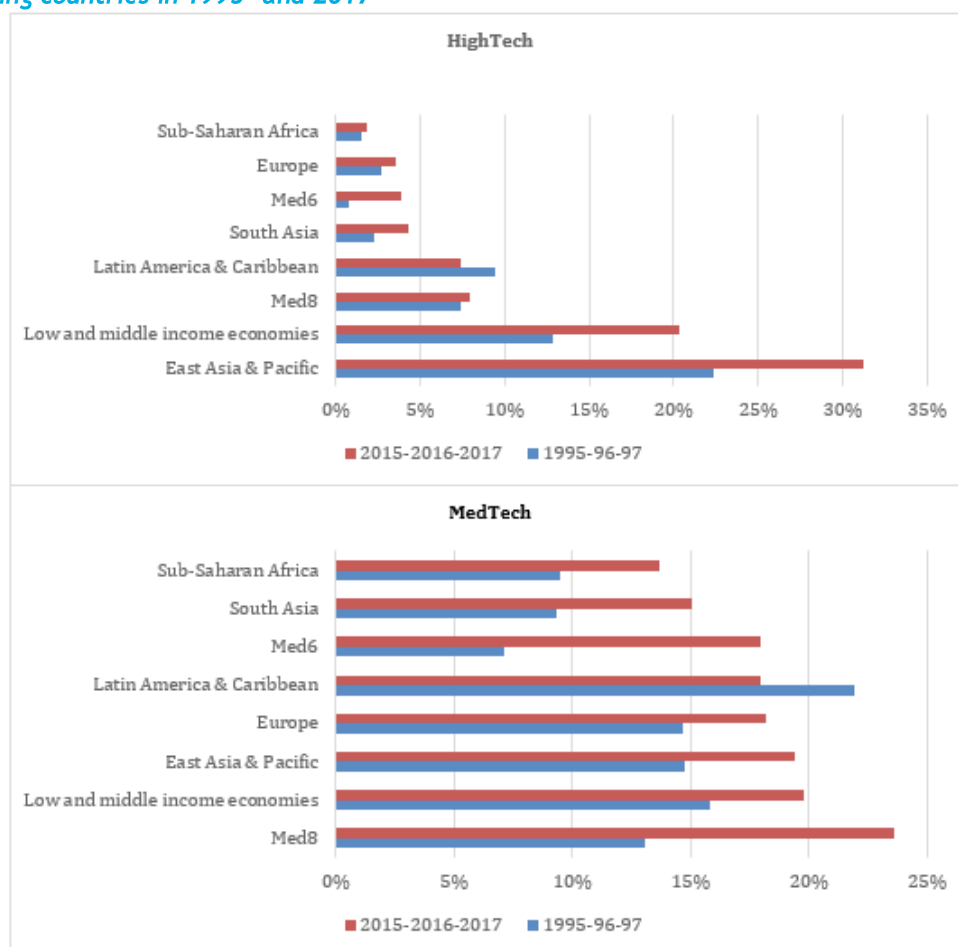
## II.5. The technological content of exports

The share of high-tech products [9] has increased very little on average in the region and that this share remains well below that of all comparable income countries (8% against 20%), however, exports of medium-

technology products have increased from 13% in the mid-1990s to almost 24% in more recent years. This share now far exceeds that of all developing and emerging countries as a whole (Figure 1.35). If Israel and Turkey are not considered, the share of high-tech products falls to less than 4% and that of medium technology to 18%

These advances are highly heterogeneous among Med countries. For high-tech products, Tunisia made the most progress (from 3% in 95 to 13% in 2017) followed by Lebanon (from 4% to just under 7%), Morocco (almost 0% to 5%), Turkey (3% to 4%) and

**Figure 1.35.**  
*Technological content of Med countries' exports in comparison with other development and emerging countries in 1995\* and 2017\**

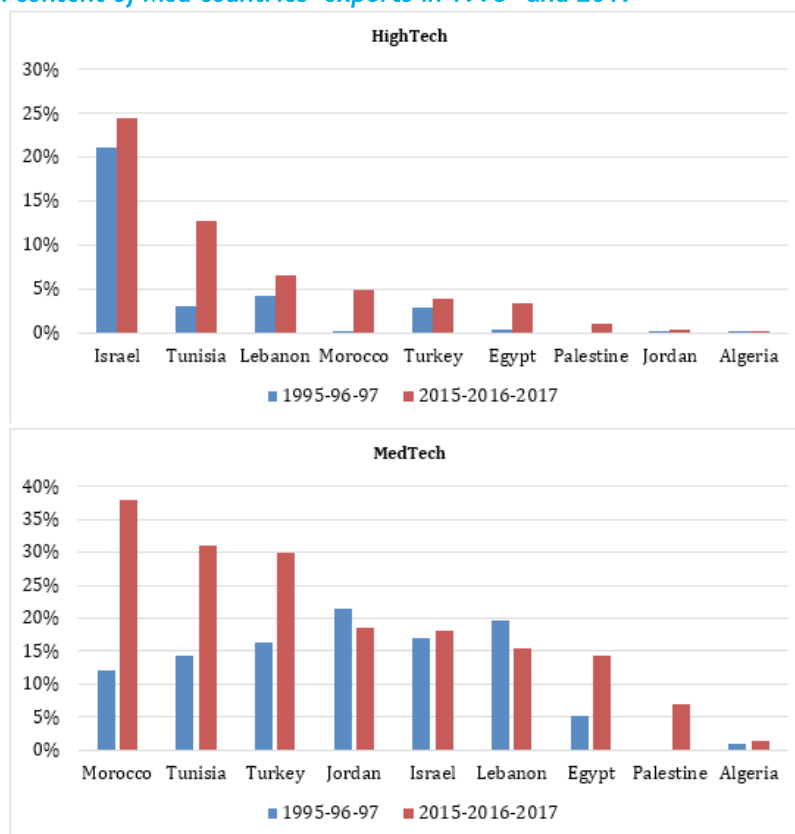


Source: UNCTAD - COMTRADE database.

\* To ensure that our comparisons are not affected by annual cyclical fluctuations, we have taken the three-year average at the beginning and end of the period.



Figure 1.36.

*Technological content of Med countries' exports in 1995\* and 2017\**

Source: UNCTAD - COMTRADE data base.

*Technological content of Med countries' exports in 1995\* and 2017\**

Egypt (from almost 0% to 3,5%). Palestine's share is 1% and Jordan's and Algeria's shares are below 1%. For medium-technology products, the most significant progress has been made by Morocco and Tunisia (whose shares have increased from 12% to 38% and 14% to 31% respectively), followed by Turkey (from 16% to 30%), Egypt (5% to 14%) and Palestine (0% to 7%). The content of medium-technology products remained stable for Israel (around 18%) and Algeria (1%) and decreased for Lebanon (20% to 15% and, to a lesser extent, for Jordan (21% to 19%) (Figure 1.36).

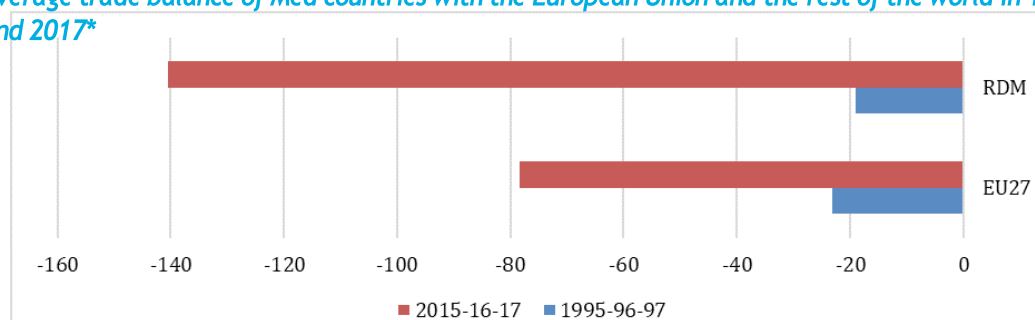
It should be noted that these positive developments for the Med countries, achieved in particular in Tunisia and Morocco, may not reflect a progression in the technological content of the value

added created by the countries, insofar as exports may contain imported inputs that are the source of such progress. Only a thorough analysis, by country, would determine if these advances stem from an upscaling of national production systems.

## II.6. A considerable deterioration in trade balances

**The trade balance of the Med countries has deteriorated considerably since the beginning of the Barcelona Process.** An interesting point is that in the mid-1990s, the largest deficit was with the EU, whereas **in recent years, the highest trade deficit is with the Rest of the World** (Figure 1.37). We already demonstrated in the 2013 Femise Report

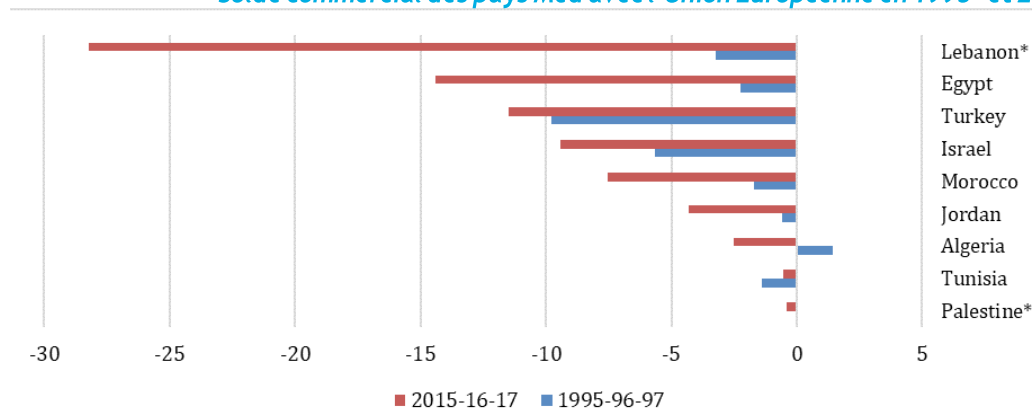
**Figure 1.37.**  
Average trade balance of Med countries with the European Union and the rest of the world in 1995\* and 2017\*



Source: UNCTAD - COMTRADE database.

\*To ensure that our comparisons are not affected by annual cyclical fluctuations, we have taken the three-year average at the beginning and end of the period. \* Palestine is excluded from the average of the Med countries (no data before 2007). The 1995-1997-1997 average of the Med countries includes the years 1997-1998-1999 for Lebanon (no data before 1997 for this country)

**Figure 1.38.**  
Solde commercial des pays Med avec l'Union Européenne en 1995\* et 2017\*

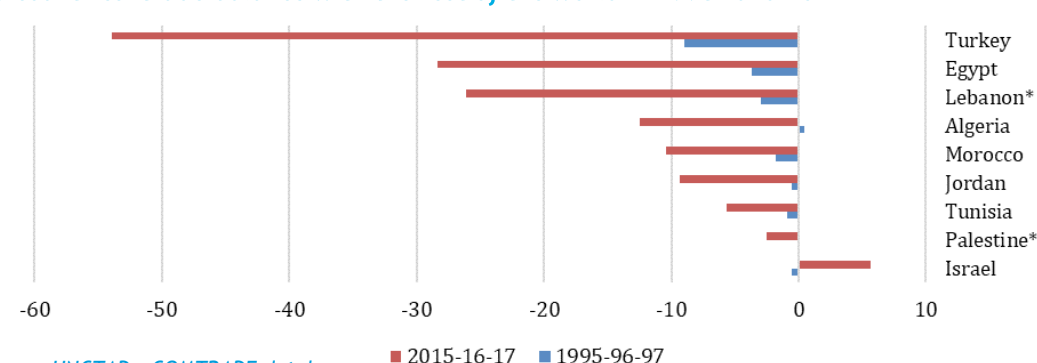


Source: UNCTAD - COMTRADE database.

\*To ensure that our comparisons are not affected by annual fluctuations of a cyclical nature, we have taken the three-year average at the beginning and end of the period.

\*\* Data are only available from 1997 for Lebanon and 2007 for Palestine.

**Figure 1.39.**  
Med countries' trade balance with the rest of the world in 1995\* and 2017\*



\*Source: UNCTAD - COMTRADE database.

To ensure that our comparisons are not affected by annual fluctuations of a cyclical nature, we have taken the three-year average at the beginning and end of the period.

\* Data are only available from 1997 for Lebanon and 2007 for Palestine.

that (i) the trade balances of the Med countries vis-à-vis the whole world only seriously deteriorated from 2002/2003 (for non-oil trade, for example, the trade deficit increased from \$40 billion in 2001 to \$180 billion in 2011) and that (ii) this deterioration in trade balances is much stronger with the Rest of the World than with the EU. The overall deficit of all Med countries increased by a factor of 5.2 between 1995 and 2017, from \$42 billion to \$218 billion [10]. With regard to the EU, the deficit rose from 23 billion dollars in 1995 to 78 billion in 2017. With regard to the Rest of the World, the deficit increased sevenfold, from 19 billion in 1995 to 140 billion in 2017. These figures show that not only has there been an increase in imports from the EU but, above all, there has been a significant influx in Mediterranean domestic markets of low-priced imported products that regional companies have had difficulty competing with. The trade deficit with the Rest of the World has increased for all Med countries, (mainly for Turkey, Egypt and Lebanon), except for Israel, which has recorded a surplus in recent years. With regard to the EU, all have seen their deficits increase (in particular for Lebanon, Egypt and Morocco), with the exception of Tunisia (whose deficit has been reduced).

This is partly due to the largely asymmetrical nature of the reduction in customs duties implemented in Mediterranean countries. As a reminder, the average tariff on imports applied by the region increased from 28% in 1992 to 7% in 2009, almost the lowest average of all developing and emerging countries.

The overvaluation of exchange rates in some countries also partly explains the lack of dynamic exports. But, generally speaking, this observation is also due to a broader set of factors that will be discussed in the next chapter. It is quite obvious that if no effort is made to move upmarket and become more

competitive on international markets and if competing with low-priced product inputs remains impossible, trade deficits will continue to deteriorate.

## Notes

1. The absolute difference corresponds to the simple difference between the GDP per capita of the EU and the GDP per capita of the Mediterranean countries (or a Mediterranean country).

2. The relative gap is the ratio between the EU's GDP per capita and the GDP per capita of Mediterranean countries (or a Mediterranean country). It should be noted that an increase in the absolute gap and a decrease in the relative gap can occur simultaneously if the growth rate of GDP per capita in the EU (in the numerator) is lower than the growth rate of GDP per capita in the Mediterranean country or countries (in the denominator).

3. The participation rate is the ratio of the labour force to the working-age population. The active population as defined by the ILO includes both employed and unemployed people. It should also be recalled that the unemployment rate within the meaning of the ILO is the number of people looking for work in the labour force

4. The labour force includes people who are employed and those who are unemployed.

5. A ratio of 31% means that on average, in Mediterranean countries (excluding Israel), the total number of working women represents less than one third of working men.

6. The Multidimensional Poverty Index (MPI) estimated by the Oxford Poverty and Human Development Initiative (OPHI) includes nine indicators

associated with the three dimensions of poverty (education, health and living standards).

7. The incidence of poverty calculated using the national thresholds is, except for Morocco, Turkey and Algeria, well above that obtained with the international threshold of \$3.20.

8. The Gini coefficient is the most commonly used inequality indicator. It calculates to what extent the distribution of income or, more often than not, the distribution of consumption expenditure between individuals or households deviates from a perfectly equal distribution. The coefficient is between 0 and 100, with 0 corresponding to perfect equality (each individual receives the same income or spends the same amount) and 100 to extreme inequality (income is held or expenditures are made by a single person). One of the limits of the Gini coefficient is that it underestimates economic inequalities insofar as it does not consider the personal wealth of individuals (World Bank, 2015).

9. The technological content of exports has been calculated on the basis of the OECD classification.

10. If we remove trade in petroleum products, this trade deficit is even greater.

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## CHAPTER 2

# Reflection on explanatory factors

by Patricia AUGIER

*The previous chapter shows that the growth of Mediterranean countries has been insufficient and that, despite positive signals, their international integration has room for considerable improvement in their international integration. It is obvious that, as explained in the first section, these countries display all the characteristics of countries whose economies have fallen into the “middle-income trap”. This gives rise to a number of questions that will structure the rest of this chapter: Have Med countries invested sufficiently? (section 2); Is it in their interest in making greater use of foreign direct investment?? (section 3); Are they innovating sufficiently? (section 4); Lastly, in section 5, we will deal more specifically with the question of the business environment.*

### I. A region grounded in the middle income trap

Although there is no consensus around its definition, nor on how to obtain its empirical verification [1], the middle-income trap concept introduced by Gill and Kharas (2007), refers to the situation of countries in which the convergence process towards the category of high-income countries is extremely slow or even blocked.

After a phase of development driven by the reallocation of agricultural resources towards industry and by growth generated by the accumulation of production factors (work and capital), which allowed them to progress from

the group of low-income countries to that of middle-income countries, Med countries entered a lengthy period of insufficient growth that did not allow them to pursue a significant increase in the average income per capita [2]. On the one hand, their wage levels became too high to compete with lower-income countries in traditional labour-intensive and unskilled sectors and, on the other, they have trouble competing with more advanced countries in sectors that require a certain technological level and a sufficiently skilled workforce.

How can countries extricate themselves from this trap? From a theoretical standpoint, even though, as underlined by Gill and Kharas (2015), “three quarters of the world's population now live in middle-income countries”, economists have not yet provided a theoretical growth model to help policy makers lead the transition to the high-income category. These authors specify that the two main theoretical frameworks for growth are not adapted to the cases of middle-income economies: (i) the Solow model (in which productivity is considered, but in an exogenous model) helps to explain the growth phenomenon in low-income countries (taking into account a given level of productivity,



growth comes mainly from the accumulation of labour and/or capital) and, (ii) endogenous growth models (Romer, 1986; Lucas, 1988; Aghion and Howitt, 1996) explain the growth of developed countries or the few emerging countries that have converged, since these models are based on the fundamental role of technological progress, innovation and the quality of human capital, factors that are the weak points of most middle-income countries. However, **all the literature in this subject agree on the fact that the weak growth of income per capita of countries stuck in the middle-income trap is related to a problem of productivity.** Eichengreen et al. (2013) show, in an empirical analysis that includes all countries for which data is available, that 85% of the slowdown in production growth rate can be explained by the slower total factor productivity growth.

Therefore, Mediterranean countries have only two possible outcomes:

- (i) either they must regain competitiveness in traditional (or mature) sectors through a drastic reduction in wages, which would further weaken these countries politically and socially and which, economically, can only be effective if countries have a productive system that is sufficiently responsive and competitive to rapidly gain export market shares;
- (ii) or they must adopt a new growth strategy based on gains in productivity.

In the case of the Mediterranean region, the first outcome mentioned would most likely be economically ineffective and would be far too risky from a political and social point of view. At their stage of development, **only improved productivity can trigger and nurture stronger growth in income per capita and relaunch the convergence process.**

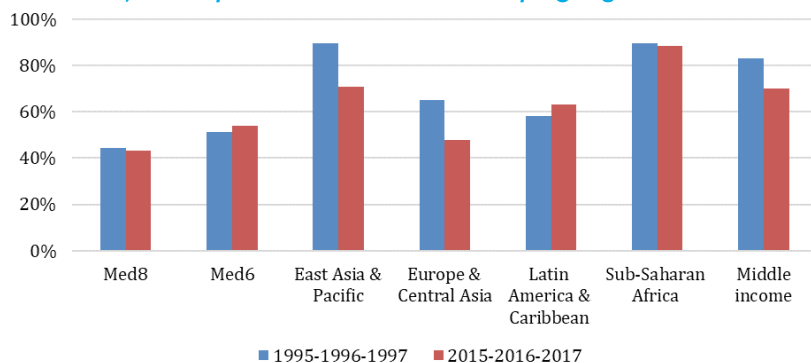
Yet, since the beginning of the Barcelona Process, Mediterranean countries have not managed to reduce their productivity gap with the EU. If we do not consider Israel and Turkey (Med6 in Figure 2.1), we can see that it has even slightly increased. The positive point is that this productivity gap is only 54% for Mediterranean countries compared to 70% for all middle-income countries. This is one of the lowest in comparison with other developing regions.

Productivity gaps with the EU differ greatly between Mediterranean countries. Four of them have a gap of more than 50% with European countries: Jordan (52%), Egypt (55%), Tunisia (57%) and Morocco (which curiously has a gap of more than 70%). Although the results obtained should always be considered with caution, they do show that Mediterranean countries have clearly made little progress in terms of productivity.

The question, therefore, is how can productivity levels be increased in these countries? A number of mechanisms can be used to achieve this:

- Firstly, the reallocation of resources between sectors (from the least productive to the most productive) and between companies within sectors, which concretely means creating some companies and closing down others, and modifying their size (the most productive grow at the expense of the least productive). The literature shows that reallocations between firms produce significant growth in productivity (Bartelsman, Haltiwanger and Scarpetta, 2013 ; Melitz et Polanec, 2015). However, we know that in the Med countries, inputs/outputs are lower compared to other developing and emerging countries (Jaud and Freund, 2015).

**Figure 2.1.**  
**Evolution of the productivity gap\* between Mediterranean countries and the EU, in comparison with other developing regions**



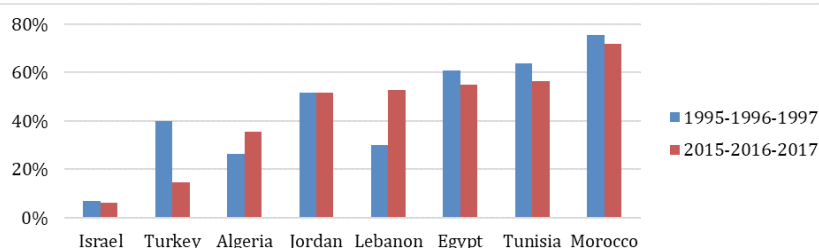
Source: Calculations by the authors based on WDI 2018 data.

\*Productivity is measured by the ratio of GDP (in constant 2011 \$ in PPP) to the number of people employed. The gap with the EU is expressed as a percentage. The average over 3 consecutive years was used to take into account the potential large fluctuations from one year to the next.

Med8: Algeria, Egypt, Israel, Jordan, Lebanon, Morocco, Tunisia, Turkey. Med6: Med8 without Israel and Turkey.

**Graphique 2.2.**

**Evolution de l'écart de productivité\* entre les pays méditerranéens et l'UE**



Source : Calculs réalisés par les auteurs à partir des données du WDI 2018.

\*La productivité est mesurée par le ratio PIB (en \$ constant de 2011 en PPA) sur le nombre de personnes employées. L'écart avec l'UE est exprimé en pourcentage. La moyenne sur 3 années consécutives a été

## II. Has there been sufficient investment?

Investment plays a key role in the growth process [3]. It can be a factor in both job creation and productivity growth. Whether public or private, it stimulates the demand for goods and services, similarly to household consumption, but its impact on a country's economy goes far beyond this demand effect alone.

Private investments (made by companies), increase the companies' production capacities while providing the possibility of integrating technological progress and, hence, increasing productivity. Public investments, through the improvement of infrastructures (transport, logistics, communication, energy, etc.) and human capital (education, health,

- Secondly, increasing productivity within the companies themselves, through innovation, technological transfers, employee qualifications, better organisation of work, using economies of scale, etc.

Both productivity gains at the firm level and inter and intra-sectoral reallocation mechanisms are required to enable industries to achieve an upgrade in quality, which in turn will create higher added value.

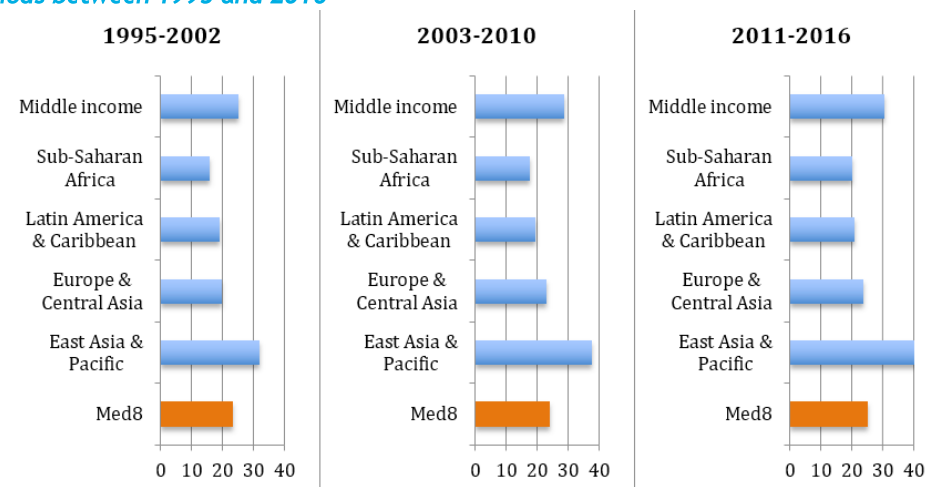
We will next try to understand how these countries can increase their productivity and exit the middle-income country trap.

people's living standards, integration of women in economic activities, etc.), can indirectly enhance company competitiveness by increasing the productivity of production factors and reducing transaction costs for firms.

The effect of private investment on growth, employment and productivity depends largely on the support provided by public investment, thanks to which the general business environment is improves. This synergy between private and public investment is key in

Figure 2.3.

**Investment rate\* of Mediterranean countries in comparison with reference countries over 3 periods between 1995 and 2016**

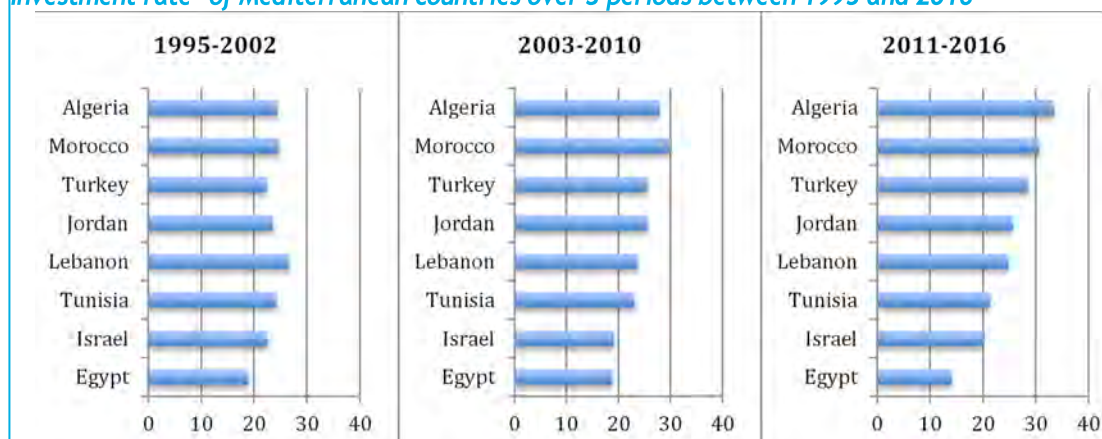


Source: WDI 2018, World Bank. Calculations made by the auteurs.

\* Average annual investment rate over each period (simple average). Med8: Algeria, Egypt, Israel, Jordan, Lebanon, Morocco, Tunisia, Turkey.

Figure 2.4.

**Investment rate\* of Mediterranean countries over 3 periods between 1995 and 2016**



Source: WDI 2018, World Bank. Calculations made by the authors.

\* Average annual investment rate over each period (simple average).

allowing emerging or developing countries to accelerate wealth creation and to achieve efficiency gains. Public investment is a kind of "catalyst for private sector development and productivity growth" (FMI, 2016). Another positive effect of public or private investment, highlighted in the literature, yet rarely mentioned, is that in developing and emerging countries it can encourage foreign direct investment (Lautier and Moreaub, 2012). By

controlling the risk of reverse causality (i.e. the effect of foreign direct investment on domestic investment), the authors have shown that a 1% increase in the investment rate leads to a 0.1% increase in the foreign direct investment to GDP ratio.

The converging views expressed by economists on the central role played by investment in growth, are further supported by historical facts: the only countries to show

sustained growth over a long period of time (see for example Krueger, 1995 or Rodrik, 2018), also recorded high investment rates of around 30 or 40% at the time of their take-off, be this Hong Kong, Singapore, Korea, Taiwan, Malaysia, Thailand or later China.

**The investment rates of Mediterranean countries are far from these levels. Over the past 20 years, they have remained relatively stable, at levels between 23% and 25%**, which places them before the Sub-Saharan countries, Central American countries and European and Central Asian countries. However, they are below all middle-income countries and, especially, East Asian countries, in which investment accelerated sharply throughout this period, from an average of 32% over 1995-2002 to 41% over 2011-2016 (Figure 23)

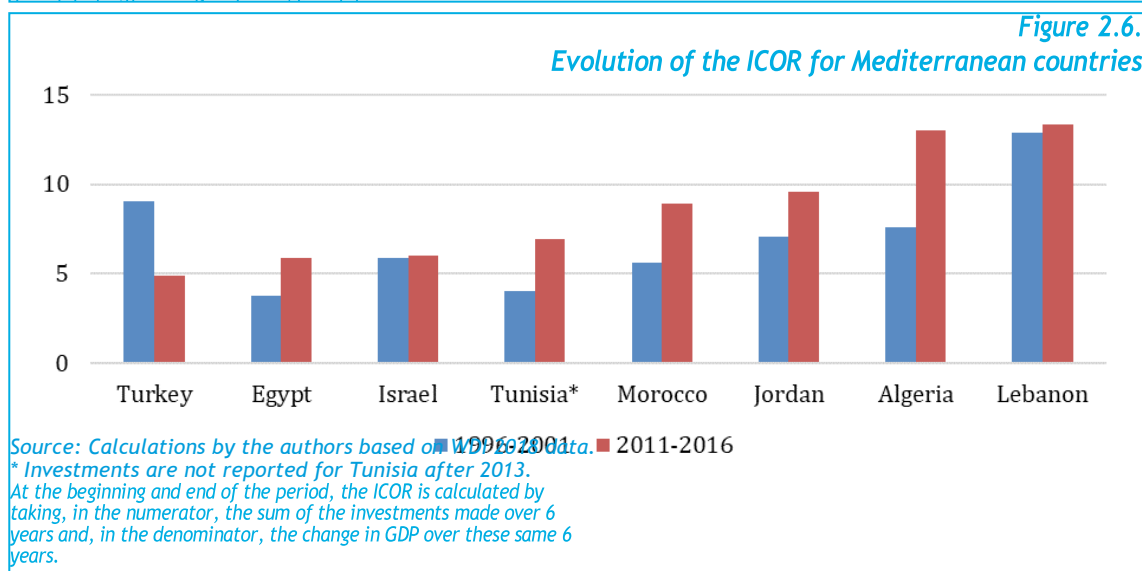
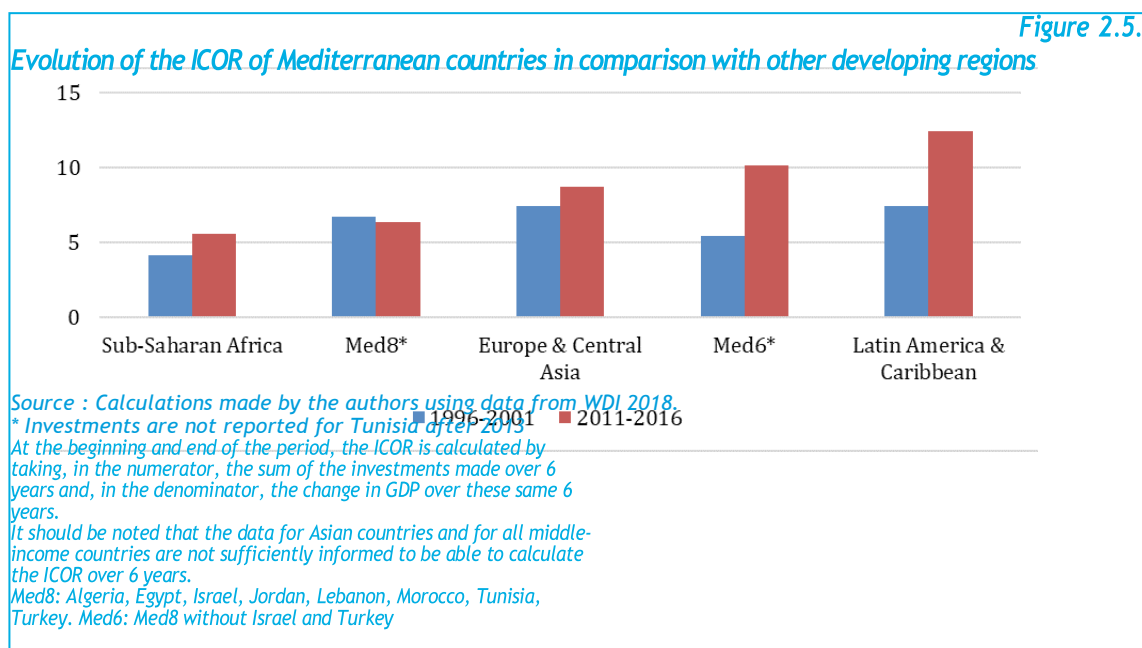
Within the region, the heterogeneity of investment dynamics has been even more pronounced in recent years since the average rates range from 14% for Egypt to 33.5% for Algeria (Figure 2.4). In addition to Algeria, the countries that performed better than the regional average were Morocco (30.6%), Turkey (28.5%), Jordan (25.7%) and Lebanon (25%, despite a slight decrease over the whole period). Three countries that have seen their investment rate slow down are below the regional average: Israel (20%), Tunisia (21.3%) and Egypt (14%).

These investment rates concern both public and private investment. The IMF (2016) estimated that, over the period 2000-2014, the rate of private investment (in total GDP) averaged about 17% and that of public investment about 6%. [4]. Data by country are only available for 3 countries [5]: Egypt (with an average private investment rate over the period 2011-2017 of 8.3%), la Jordan (20.7%) and Lebanon (22.5%). Investment in Jordan

and especially in Lebanon is therefore mainly made by the private sector.

In addition to these investment rates, in other words the amounts of public or private investment mobilised, there is the question of **the quality of these investments and therefore, more broadly, their effectiveness in creating growth**. The ICOR [6] (Incremental Capital Output Ratio) which corresponds to the ratio between annual investment and annual GDP growth, measures the amount of investment required to generate the increase of a production unit. A decrease in this indicator means an improvement in investment efficiency. **In the case of the Mediterranean countries (excluding Israel and Turkey), from the beginning of the Barcelona Process until recently, the ICOR has increased very significantly, indicating that investment has become less effective throughout the region** (Figure 2.5). This finding is observed in all Mediterranean countries, with the exception of Turkey and Israel (Figure 2.6). This is confirmed by the low correlation between the investment rate and the growth rate for Mediterranean countries compared to all low- and middle-income countries (Figure 2.7). This correlation also deteriorated for the region, and has become negative over the last 10 years (Figure 2.7). Lastly, these two graphic displays show that Algeria, Morocco, Tunisia and Lebanon should have higher growth rates due to their annual investment rate.

This investment analysis shows that, although sustained efforts have been made in Morocco, Turkey and Algeria, the amounts invested, whether public or private, remain insufficient overall to instigate a boost in growth. But, from our point of view, it above all shows that,



**Mediterranean policy makers should place the priority first and foremost on improving the efficiency of investment.**

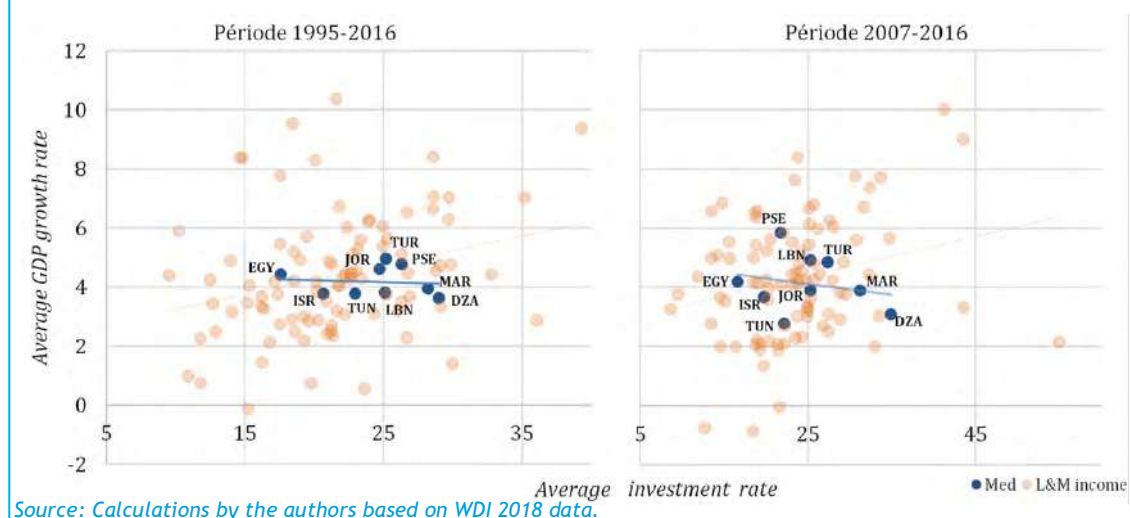
Public or public-private partnership investments may not be sufficiently effective, either because they are misdirected or because they do not sufficiently benefit the private sector, in the sense that other operational problems prevent these investments from resulting in lower transaction costs for companies and

in enhanced productivity. An example of this are the investments in airport development made in Morocco, which only partially benefit companies insofar as air freight development remains very limited. Another example that can also be drawn from the significant investments recently made by Morocco in logistics, is the creation of integrated platforms that are very often empty because they are mostly put on sale (which locks up capital) at prices that are too high and therefore inaccessible for SME that



Figure 2.7.

*Correlation between the investment rate and the growth rate for Mediterranean countries and all low- and middle-income countries*



Source: Calculations by the authors based on WDI 2018 data.

have trouble finding funding.

As far as private investments are concerned, their lack of effectiveness can be explained in several ways. Investments made by companies might:

- Not give rise to product innovation,
- Not to incorporate technological advances, or
- Not include sufficient added value because of the lack of qualification and competence of the workforce. Complementarity between the technology contained in the investment (or, more broadly, all inputs) and the quality of human capital is, indeed, essential to improve the efficiency of companies. The quality of human capital determines the ability of firms to absorb technology [7].

### III. Should more use be made of foreign direct investment?

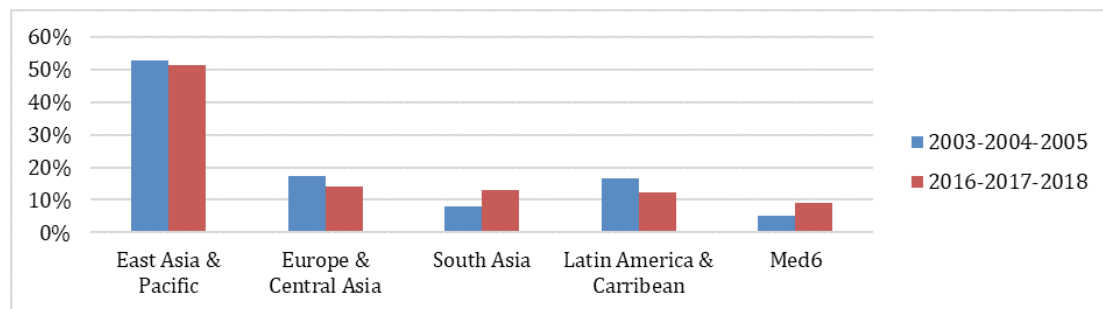
#### III.1. What do Mediterranean countries receive?

Out of total foreign direct investments (FDI) made in developing

and emerging countries [8], half is directed towards East Asian countries. The remaining half is split between Europe (14%), South Asia (13%), Latin America (12%) and the Med countries [9] (9%) (Figure 2.8). This share has increased by 4 percentage points in about 15 years, as it was 5% in the early 2000s.

However, **Med countries have the highest ratio of FDI to GDP**, although it has declined over the past 15 years, **from 6.7% at the beginning of the 2000s, to a current 3.8%** (Figure 2.9). Among the 6 Med countries, Egypt has received the most FDI as a proportion of its GDP (10.6%) over the last 3 years, followed by Morocco (4.7%), Jordan (4.2%), Algeria (2%), Tunisia (1.2%) and Lebanon (0.2%). The share of FDI in GDP has fallen for Lebanon (it was 8.2% in the early 2000s), Jordan (from 10.8% to 4.2%), Algeria (from 5.8% to 2%) and Tunisia (from 4.1% to 1.2%). For Morocco, the share has remained almost stable, rising from 4.1% to 4.7% and for Egypt, from 7.2% to 10.6% (Figure 2.9).

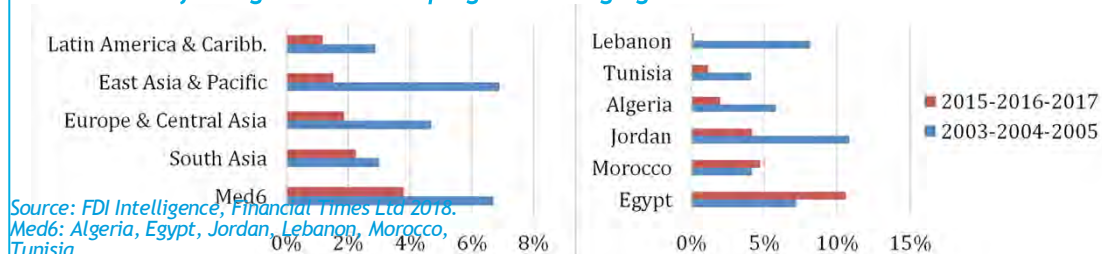
Figure 2.8.  
Regional distribution of FDI towards developing and emerging countries



Source: FDI Intelligence, Financial Times Ltd 2018.  
Med6: Algeria, Egypt, Jordan, Lebanon, Morocco,

Figure 2.9.

FDI/GDP ratio for regions in developing and emerging countries and in Med countries



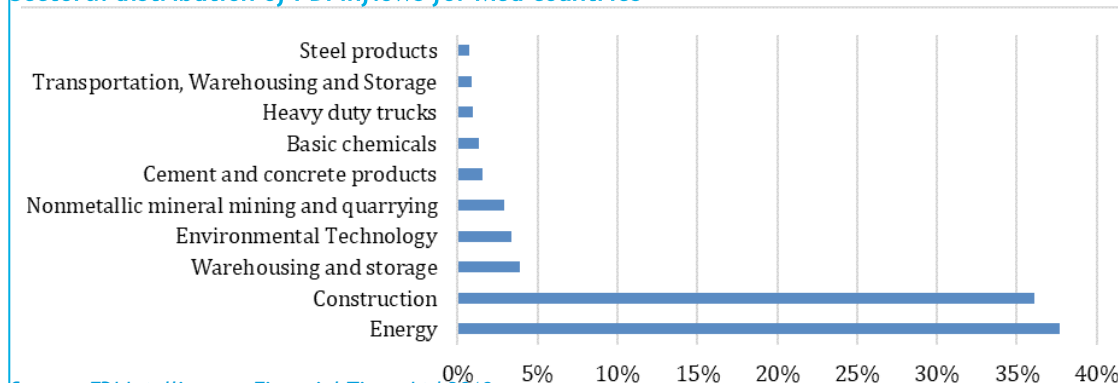
Source: FDI Intelligence, Financial Times Ltd 2018.  
Med6: Algeria, Egypt, Jordan, Lebanon, Morocco, Tunisia.

In **Algeria**, almost two-thirds of FDI are directed, in almost equal proportions, towards warehousing and the sector of mining and quarrying of non-metallic minerals. Next comes basic chemicals (12%), followed by the construction of commercial and institutional buildings (8%), steel production (7%), automotive industry (3%) and oil and gas extraction (3%). In **Jordan**, 74% of FDI were directed, in equal shares to solar **electric power**

(38%) and fossil fuel electric power (36%). The third largest sector, but which represents only 10%, is the construction of residential buildings, followed by wire telecom networks (internet telephone services), with 3%. The concentration of FDI is even higher in Egypt [10]: more than 90% of FDI went to 2 sectors (construction, 46% and energy, 44%). Then come environmental technologies (5%).

Figure 2.10.

Sectoral distribution of FDI inflows for Med countries



Source: FDI Intelligence, Financial Times Ltd 2018.

FDI in **Morocco** are for more diversified. 13% are invested in **cement and concrete products**, 11% in **wind turbine energy**, 8% in the manufacturing of trucks, 7% in warehousing, 7% in industrial building construction, 4% in housing, 4% in aluminium production, 4% in freight and distribution services and 3% in hydroelectric power. In **Tunisia**, **wind turbine energy** attracted 24% of FDI, followed by **biomass energy** (12%), housing (10%), automobiles (7%), banking (5%), software publishing (5%), wire and cables (5%), railway equipment (5%), machinery production (4%), freight and distribution services (4%) and vehicle engines (3%).

### III. 2. Are foreign direct investments an essential factor for growth?

The analysis of the role of foreign direct investment (FDI) on the growth of developing or emerging countries reveals a paradoxal situation: on the one hand, there is the commonly accepted idea that FDI has a positive effect on job creation, competitiveness and, more generally, economic development, which explains why almost all countries in the South have put in place incentive policies to attract foreign investment to their countries yet, on the other hand, the economic literature does not clearly illustrate this positive effect.

The favourable perception of FDI is theoretically justified by the following two main mechanisms:

- In the short term, they increase capital and labour factors in the host country, which automatically leads to increased production. This is the direct effect of FDI induced by extensive growth.
- In the medium to long term, FDI brings intensive growth (which is driven

by increased productivity) by allowing a transfer of technology, knowledge and know-how. This indirect effect of FDI linked to this "technological" transfer, in the broad sense of the term, can be achieved through several channels: (i) labour mobility (the workforce trained in foreign companies labour mobility (the workforce trained in foreign companies passes through domestic companies), (ii) mimicking by local companies working in very similar sectors, (iii) the establishment of customer-supplier relations when foreign companies buy their inputs in the host country (foreign companies can provide technical or even financial support to improve product quality, integrate innovations, improve the organisation and management of the local company and even set up and manage an ecosystem in a specific sector), (iv) the export activities of foreign companies that can reduce the export costs of domestic companies and thus open international markets to them, either because domestic companies try to emulate the export procedures followed by foreign companies, or because foreign companies and domestic companies collaborate.

**While the direct effect of FDI has been generally verified (Makiela and Ouattara, 2018), the fact that there might be a positive medium- to long-term effect on growth through improved productivity and competitiveness remains highly controversial in practice.** The analyses that have been carried out using company data have not succeeded in showing a "spill over" effect of productivity from foreign capital companies to domestic capital companies: in developing and emerging countries [11], the presence of multinationals has no impact on the productivity of local firms. Studies based on aggregated data

show that the relationship between FDI and growth (or any other factor favourable to the development of countries [12]) remains undetermined: in this case, it is positive; in others, it is non-significant while in yet others, it is even negative [13].

How can we explain this paradoxal situation in which the expected effects are positive while the observed effects rarely are? Much of the recent literature on FDI focusses on this issue. The answer is that **the positive effect of FDI on growth is not an automatic mechanism but depends, firstly, on the absorption capacity of the host country and its firms**, that is, its human capital [14], its level of research and development, the quality of its infrastructure, the functioning of its financial market [15], the managerial quality of company managers, the country's production structure and the general business environment **and, secondly, on the nature of the FDI implemented**, mainly their destination sector and the type of agreements and relationships concluded with the host country and local companies [16]. Papers such as the one by Amendolagine et al. (2019) stress the importance of multinationals buying their inputs locally and, above all, the importance of the quality of the relationships established by multinationals with their local suppliers. At the same time, Javorcik and Spatareanu (2007) showed that in Czechoslovakia, local companies that had become suppliers to multinationals located in the country were those that initially had the lowest financial burdens. We see here, therefore, that a local condition that characterises the business environment of domestic firms (access to financing and liquidity constraints) may have an influence on the ability of these domestic firms to benefit from FDI through the possibility or not of becoming

a supplier of the multinational company located within the territory.

Iamsiraroj (2015) revealed a positive effect of FDI on growth including, in his empirical analysis, 124 countries between 1971 and 2010. When looking at the effects by major region, we can see that this positive impact is true only for developed countries: for countries on the African continent (including Mediterranean countries) and for countries in the Asia-Australia region, there is no effect on growth.

For Latin American and Caribbean countries, however, the effect of FDI is negative. Another recent study (Alvarado et al., 2017), carried out this time over the period 1980-2014 and concerning only Latin American countries, confirms that FDI has not been beneficial to growth: a positive effect is only observed for the two countries that are in the category of high-income countries, namely Chile and Uruguay. In contrast, FDI has no effect on growth for upper-middle-income countries (Argentina, Brazil, Colombia, Costa Rica, Dominican Republic, Ecuador, Mexico, Panama, Paraguay, Peru and Venezuela) and its effect has even been negative for lower-middle-income countries (Belize, Bolivia, Salvador, Guatemala, Honduras and Nicaragua). One of the main reasons given for this result is the production structure of these countries, which is largely based on the exploitation of natural resources, sectors to which FDI inflows are directed. It is also possible that these FDIs have contributed to increasing inequalities [17] and social tension, which may have played a negative role in growth. Concerning the Mediterranean countries, to our knowledge only one study, that of Cecchini et al. (2008), carried out within the framework of Femise, focused specifically on this region. It shows that FDI, between 1980 and 2000, could only benefit productivity if the level of qualification of the labour force was above a certain threshold.

Finally, it should be noted that countries such as Korea and Taiwan, during their economic take-off period, benefited from only low FDI inflows. Indeed, in these two countries, they represented less than 3% of the total investment before 1998. The opening to FDI started after their industrialization (Chaponnière et Lautier, 2018). However, these countries chose, during the 1970s and 1980s, to benefit from technology transfers through licensing agreements and knowledge transfer contracts. With regard to China, which is one of the countries that received the most foreign investment, Yalta (2013) showed that at the aggregate level, there was no causal link between FDI and the country's strong economic growth between 1982 and 2008.

**Should it be deduced from this observation that Mediterranean countries could do without foreign direct investment? The answer is clearly no.**

**Nevertheless, a clear message to decision-makers is that the positive effects of foreign investment the national economy are far from automatic. For FDI to produce these positive externalities, it is incumbent on Mediterranean countries to create a sufficiently strong internal "absorption capacity", to promote the establishment of ecosystems around multinationals in key sectors, and to do everything possible to ensure the development of sustainable relationships between multinationals and local companies.** Even if the attractiveness of foreign investments, whatever their form (green-fields or mergers and acquisitions), requires improvement in certain countries, it is important to stress that government action goes far beyond the sole objective of attracting foreign investment. The way in which FDI will impact the national economy (type of effect / positive-negative / scale)

also largely depends on their responsibility

It is in the interest of Mediterranean countries, we believe, to:

**1/ Establish a regulatory framework for investment**, (i) that is transparent, clear and non-discretionary to ensure fair treatment of foreign investors and reduce exposure to corruption and, (ii) which consolidates investor guarantees. For example, it is important that the procedures for repatriating capital and profits are clear and not subject to the discretion of the central bank administration. Clarifying the framework that governs foreign investment means, for some countries such as Tunisia, that they should review the many tax and financial incentives that create a great deal of opacity and administrative barrier for investors (World Bank, 2014) Without giving them up completely, public authorities should make better use of these tax and financial incentives:

- (i) either **encourage the transfer of technology and know-how between foreign companies and the domestic economy as a whole** (companies, human capital, research centres, national institutions, etc.),
- (ii) or to **push for the implementation of training schemes organised by foreign investors for the employees of domestic companies or, more generally, for people seeking employment**;
- (iii) or to **be consistent with industrial policy or, more broadly, with the national strategy decided by each country**. Tax incentives could thus be designed to meet the needs of developing, isolated and disadvantaged regions, to target strategic sectors or to address environmental concerns.



**2/ Recognise that the presence of foreign investors is an opportunity for the national economy that the public authorities must be seize and not just leave the private sector to "get on with it".** If the local private sector must rely solely on itself, without the support of public action, it will not be able to derive all the potential benefits offered by foreign investors. Public authorities should encourage any form of rapprochement between foreign and domestic companies to promote the transfer and acquisition of technology and knowledge as much as possible. Depending on the situation in each country, consideration should be given to facilitating the different forms of joint venture agreements (i.e. alliances between two companies with or without equity participation) and adapting regulatory and legal frameworks to the needs of countries and local companies. Access to information and appropriate support regarding the different possibilities for domestic firms to access new processes, products and technologies, for example through licensing agreements, should be better developed in some countries. Finally, the sine qua non condition for encouraging company agreements and the dissemination of knowledge is for public authorities to ensure that legal provisions on intellectual property rights work properly. In general, the private sector, whether foreign or domestic, needs a clear and stable environment established by the public authorities in order to engage in medium- to long-term projects.

**3/ Create, for countries that have not yet done so, a specific agency dedicated to foreign investments, responsible for both promotion and regulatory functions,** in order to,

**(i) considerably simplify all the procedures to be undertaken by**

**foreign investors, with the creation of a one-stop shop** which would integrate all procedures, including those that are often long and complicated regarding access to land ownership;

**(ii) provide more effective support for the establishment of foreign companies** within each country;

**(iii) facilitate contacts between local companies and multinationals.** To this end, the agency could set up a list of local companies and start-ups, by sector and location, as well as a list of innovative projects, to facilitate and automate this relationship.;

**(iv) establish a system of permanent and transparent dialogue between foreign investors and public authorities,** in order to have continuous feedback on the difficulties encountered by these foreign investors, to respond more quickly to their problems, to improve the system for receiving and setting up foreign companies and to better control corruption.

**4/ Carry out surveys among foreign companies** to identify the problems they face in each of the countries, according to their sector of activity and geographical location, and to better understand the priorities towards which public action should be directed.

**5/ Give absolute priority in Mediterranean countries to improving the "absorption capacity" of each of the economies,** which amounts to setting up or pursuing, depending on the situation of each country, a real strategy for the development of the private sector. Public action is complicated by the fact that so many areas require imperative action. These mostly concern everything that makes up the business environment (infrastructure, education/ employability of labour supply, access to

financing, administrative barriers, corruption, taxation, etc.). This question of the business environment, which, as we will see, is at the heart of the difficulties faced by Mediterranean countries, will be addressed below. We must, however, bear in mind that the business environment largely determines the countries' "absorption capacities", which in turn determines the effect of FDI on the economy i.e. its contribution to the development of countries.

#### **IV. Do Mediterranean countries innovate sufficiently?**

##### **IV.1. Why do they need to innovate?**

Innovation is not limited to technological change. Innovation also includes new or improved products, new production processes, new management practices or new marketing methods [18]. It should also be noted that an invention is not an innovation. A novelty, change or invention only becomes an innovation if it is put into practice, circulated or disseminated by companies within the economy. Companies are at the heart of innovation because they are its driving force. They make it possible for an innovation to exist.

Innovation is a major driver of productivity improvements and enables companies to enhance their competitiveness. It also helps to increase and improve people's living standards. An innovation policy must also include objectives that address the countries' socio-economic needs (regional inequalities, very high youth unemployment, economic exclusion of women, etc.) and the constraints that they must deal with, such as those related to climate change, water stress,

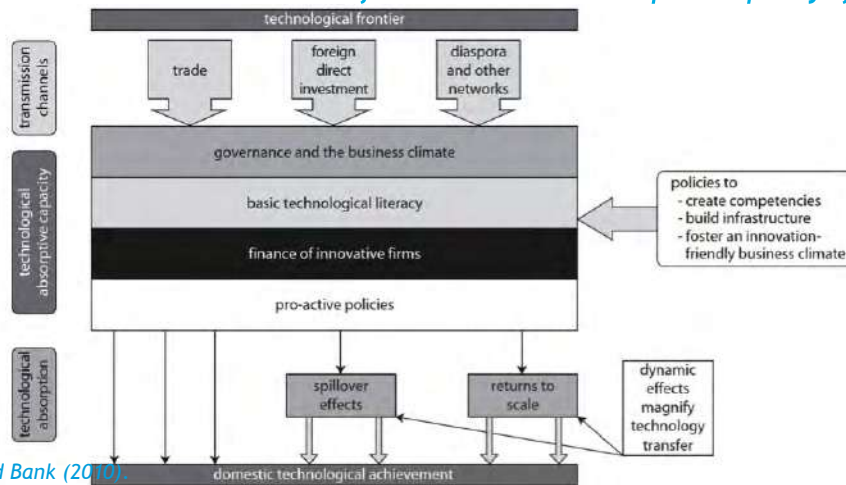
the necessary energy transition, etc. An innovation policy must therefore include (i) a clear and ambitious medium- to long-term vision, capable of bringing together all stakeholders, civil society and the population and, (ii) shorter-term objectives to gradually help the country progress towards the desired outlook.

In developing and emerging countries, a large proportion of innovations are based on the transfer of technology and knowledge, i.e. on "the adoption, adaptation and recombination of existing innovative technologies, practices or products" (World Bank, 2010), which does not prevent countries from developing their own innovations at the same time. The transfer of technology and knowledge requires, as discussed in the previous section, foreign direct investment, trade [19], the purchase of licenses and, possibly also, the involvement of diaspora networks. Therefore, as shown in Figure 2.1, a country's innovative capacity is a key element in ensuring what have previously named as "absorptive capacity" which allows an economy to benefit from the positive externalities of FDI, trade and acquired licenses. Thus, innovation capacity building is a major challenge for developing and emerging countries as it has a dual impact on their economies (Figure 2.2):

- a direct effect because it promotes innovative processes within companies, enabling them to achieve productivity gains and to become more competitive;
- an indirect effect as by increasing absorption capacities, both companies and the economy as a whole benefit from the transfer of technology and knowledge linked to relations with the rest of the world, mainly through trade, FDI and licensing agreements.

Figure 2.1.

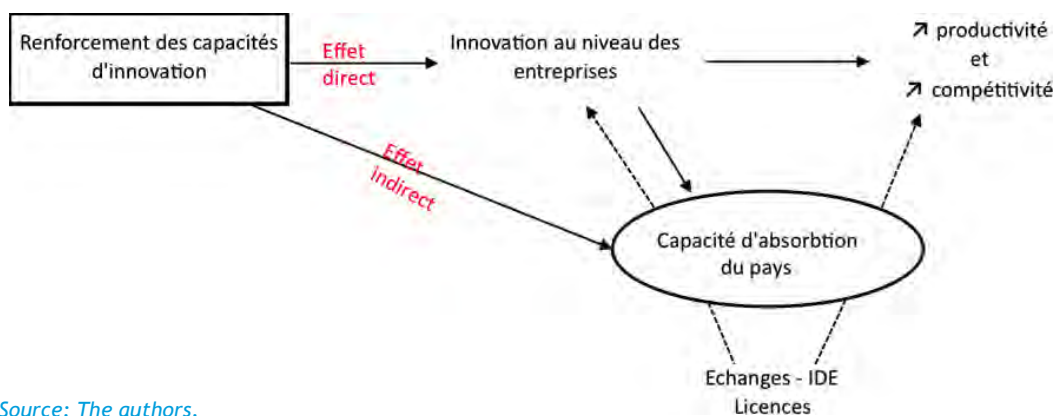
### The role of innovation in the absorptive capacity of an economy



Source: World Bank (2010).

Figure 2.2.

### Direct and indirect impact of innovation capacity building



Source: The authors.

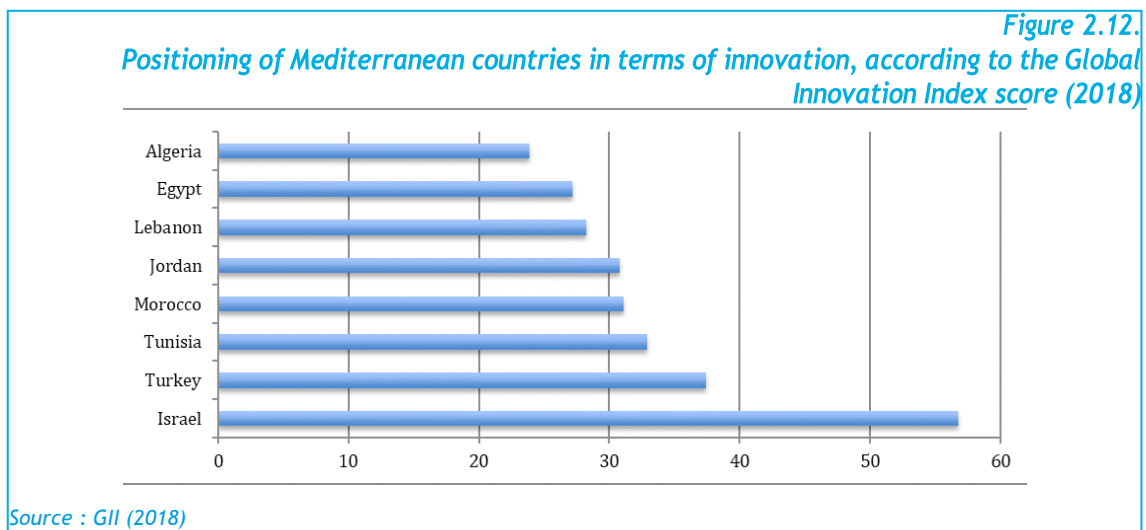
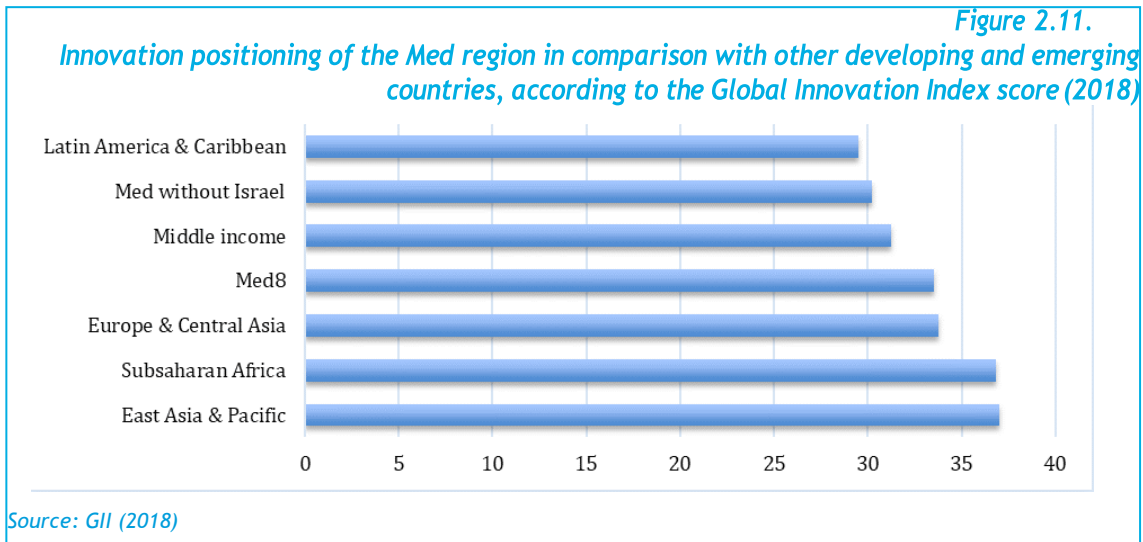
Strengthening innovation capacities is thus the condition for the installation of a virtuous process: the more a country innovates (either by launching of its own new innovations or through technology transfer), the closer it gets to the technological frontier and the greater its absorption and innovation capacities.

#### IV2 Where do Mediterranean countries stand in terms of innovation?

The customary global indicators do not give a positive picture of innovation in Mediterranean countries. According to the Global Innovation Index [20]

(GII), the score of all Mediterranean countries without Israel is only 30 (on an increasing scale from 0 to 100), which is the worst score, along with the South American continent, of all developing and emerging countries. All Mediterranean countries, with the exception of the lowest score (24 for Algeria) and the highest score (57 for Israel), are around the regional average.

The advantage of these international indicators is that they allow us to compare almost all countries using multiple criteria, however criteria used are more appropriate for the assessment of developed countries than developing countries [21]. In the following



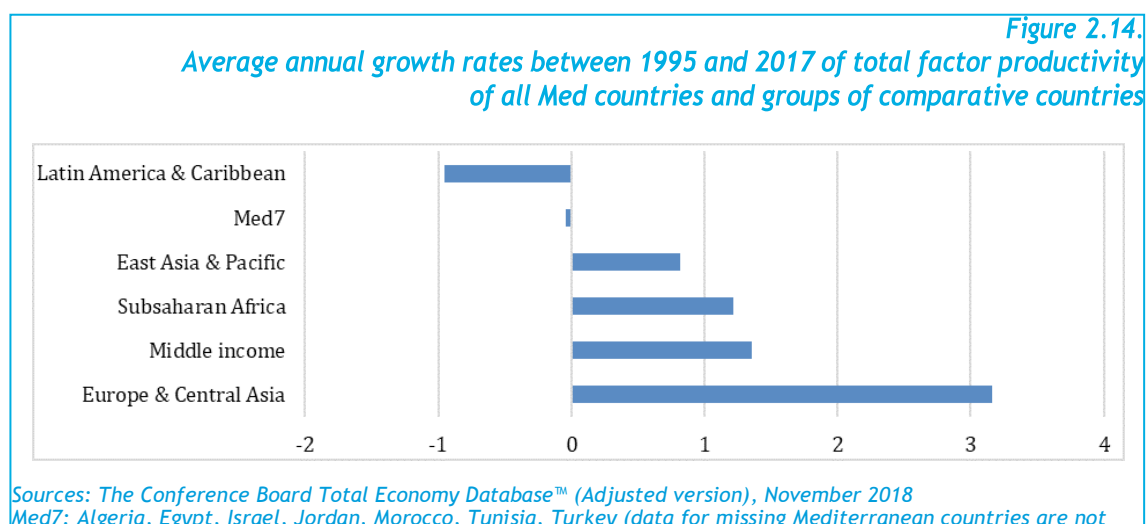
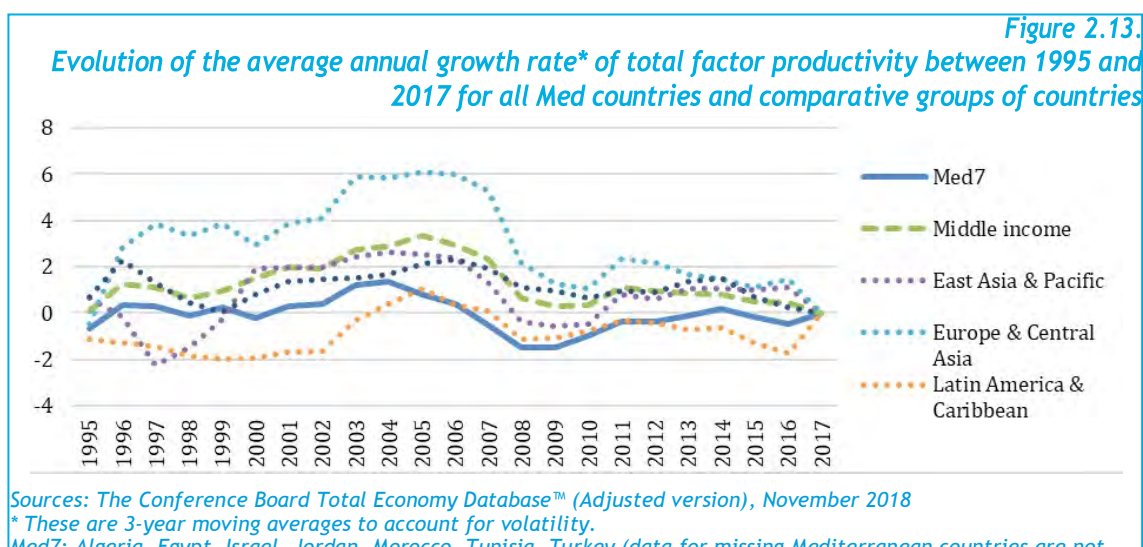
we therefore add to this composite index (which also has the disadvantage of being too general and therefore not very meaningful) indicators that are more enlightening within the context of Mediterranean countries in the scoreboard that Femise is currently developing (see footnote 21), the indicators selected are grouped into 3 categories:

- Those that measure innovation outputs,
- Those that evaluate the innovation process
- Those that measure innovation inputs

In this report, we will consider only some of the main outputs of innovation.

The preferred criterion to measure the innovation outputs, which corresponds to the results

yielded by active policies in favour of innovation and decisions made by companies, is productivity. Section 1 of this chapter has already demonstrated that the return on investment (approximated by the ICOR) and the gap in labour productivity relative to that of European countries had deteriorated on average over the past 20 years. If we look at total factor productivity (TFP), the finding, which is not very encouraging, is confirmed: since 1995, TFP annual growth rates have remained close to 0 and have never exceeded 1.4% (Figure 2.13). As they have often been negative, the average of these annual growth rates in total factor productivity between 1995 and 2017 is **slightly below 0%**.



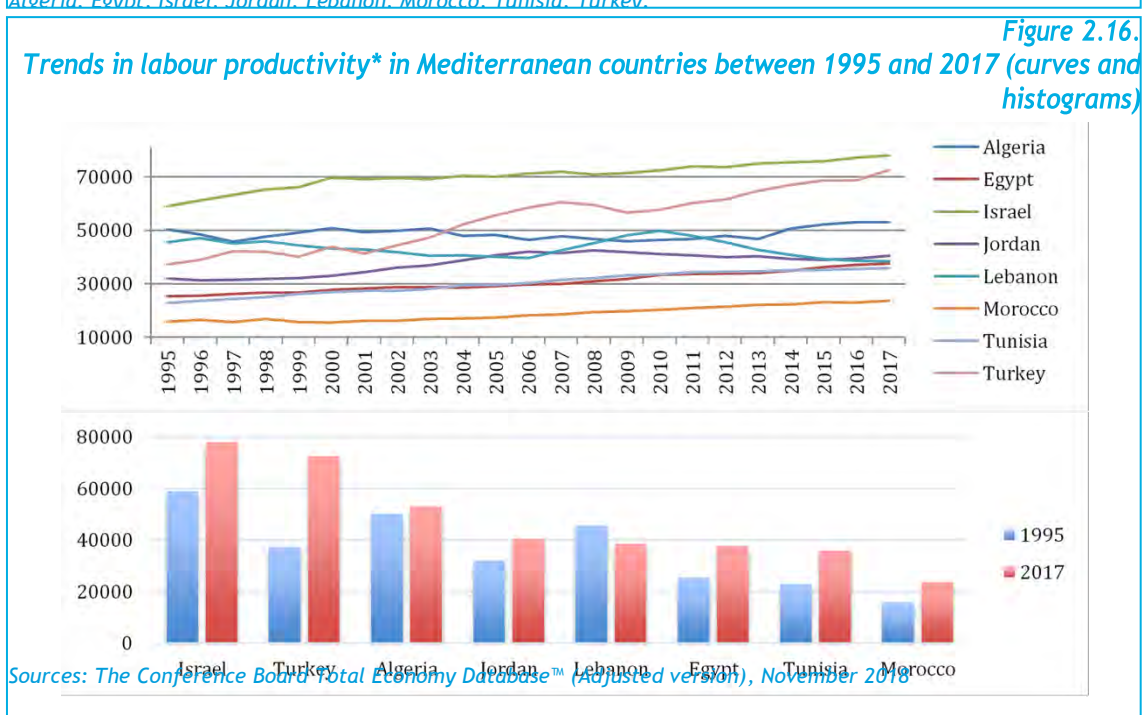
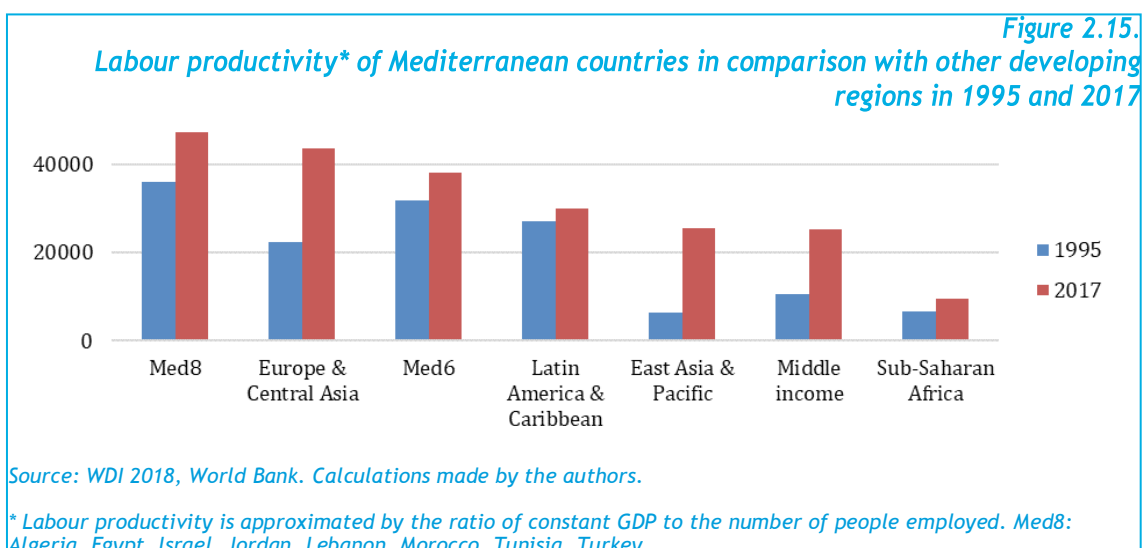
It is obvious that along with the Latin American and Caribbean countries, **Mediterranean countries have recorded the worst performance in terms of overall productivity progress.**

If we look at the apparent labour productivity, we see that its level is relatively high, but that, if we remove Israel and Turkey (Med6), **the apparent labour productivity increased very little between 1995 and 2017**, as is also the case for Latin American countries and Sub-Saharan African countries. By contrast, in other developing regions and also in all middle-income countries, labour productivity has increased significantly (Figure 2.15). The following double graph (curves and histograms,

Figure 2.16) show the evolution of labour productivity for each Mediterranean country. **Israel and Turkey stand apart, with a significant increase in labour productivity, whereas for all other Mediterranean countries these increases have been more modest, if not inexistent:** in Tunisia, Egypt, Morocco it has increased slightly and to a lesser extent in Jordan, while it has stagnated in Algeria and declined slightly in the case of Lebanon (Figure 2.16).

To assess the output of innovation, it is also possible to use the share of high- and medium-technology products in each country's exports and the number of patents filed as a proportion of the population.

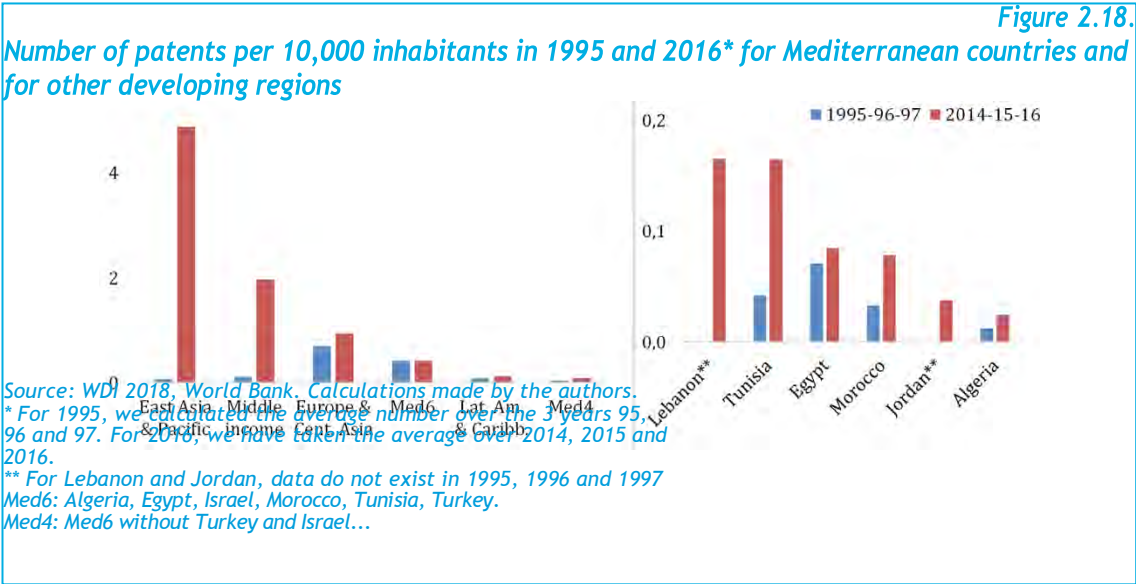
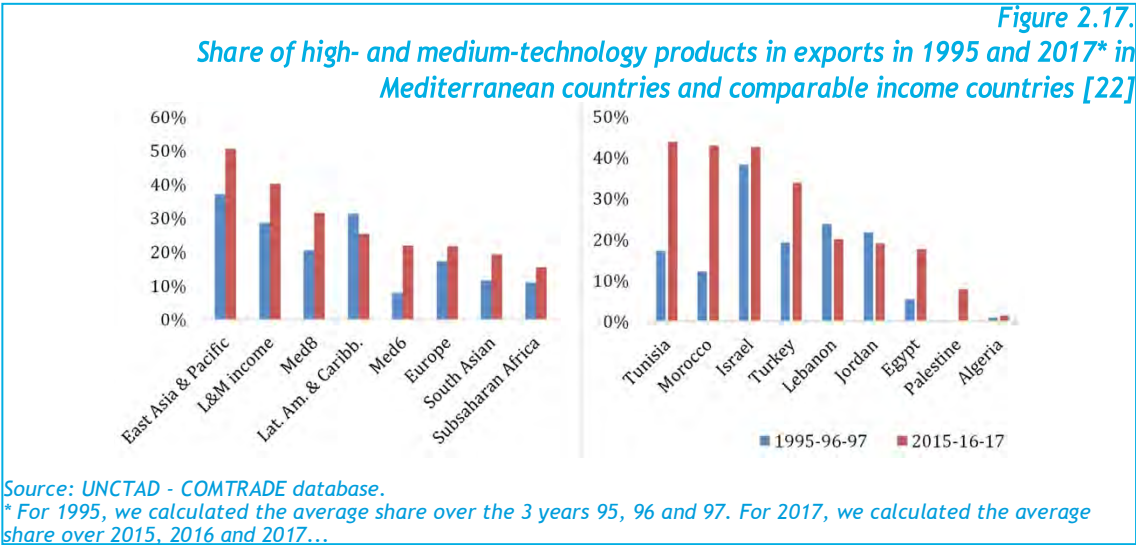




As seen in Chapter 1, almost all Mediterranean countries have seen an increase in the share of high- and medium-technology products in their total exports. With a share of about 40%, Tunisia and Morocco have even managed to catch up with Israel. **The Med region exports on average 30% of high and medium technology products. This same share falls to 20% without Israel and Turkey, which is far from the average for middle-income countries (almost 40%) and East Asian countries (50%).** Regarding the number of patents

as a proportion of the population, this indicator has increased very slightly in the region (reaching at best 0.15 per 10,000 inhabitants in Tunisia and Lebanon and less than 0.1 for Morocco and Egypt), but, once again, it remains well below the average for middle-income countries (2 per 10,000 inhabitants) and East Asian countries (5 patents per 10,000 inhabitants) (Figure 2.18). **Overall, these indicators show that in the field of innovation, a significant gap has accumulated with most developing and emerging countries.**





Innovation inputs are considered to be everything that contributes to the business environment, in the broad sense of the term. These include education, infrastructure, the general business environment (administrative procedures, access to finance, regulations, customs, etc.). There are many reasons for this lag, some of which are related to the business environment and the general framework (education, infrastructure, administrative procedures, access to finance, regulations, customs, etc.). These points, which fall within the scope of what we may term the "supply part" of innovation, will be dealt with below.

On the "demand" side, however, certain less frequently mentioned factors can also contribute to the development of innovation. Among these factors, it has been shown, in the case of industrialised countries, that public procurement is an important source of innovation. For example, Edler and Georghiou (2007) found that of all the successful innovations marketed in Finland between 1984 and 1998, 48% were triggered by a public order. Similarly, a European Commission report (2008) highlighted the importance of public procurement on innovation dynamics, particularly in e-Health, pharmaceutical,

energy, environmental, transport and logistics, security and digital content sectors. Therefore, where public finances allow for it, decision-makers in Mediterranean countries must take into account the very important role of public demand as a factor of innovation. Projects led at the regional scale, particularly in the fields of energy, the environment, digital technology and pharmaceuticals, can lead to regional innovation, which in turn can have a positive impact in all these countries.

More specifically concerning developing and emerging countries, and therefore Mediterranean countries, customs duties and non-tariff measures may give rise to a lack of incentive for companies, for two main reasons. Firstly, even if tariffs have fallen significantly, developed regions maintain tariff peaks and a number of barriers in sectors where Southern countries have a comparative advantage (agriculture, agri-food, textiles and clothing, footwear, leather, etc.). Secondly, as pointed out in a World Bank report (2010), “it is mainly the very structure of customs duties itself that forms a serious obstacle to innovation, technology transfer and the move upmarket.” Indeed, developed countries have higher tariffs on processed products, especially in the sectors just listed. In fact, the tariffs applied by developed countries on imports from the South increase with the amount of transformation and value added incorporated in the products. This situation can be detrimental to Mediterranean companies and hinders product innovation, upscaling and diversification of exports.

**Femise believes that the level, and above all the structure of customs duties applied by developed countries in strategic sectors where the Mediterranean countries have a comparative advantage, should be renegotiated to create opportunities to export higher value-added products and to provide greater incentives for companies to innovate.**

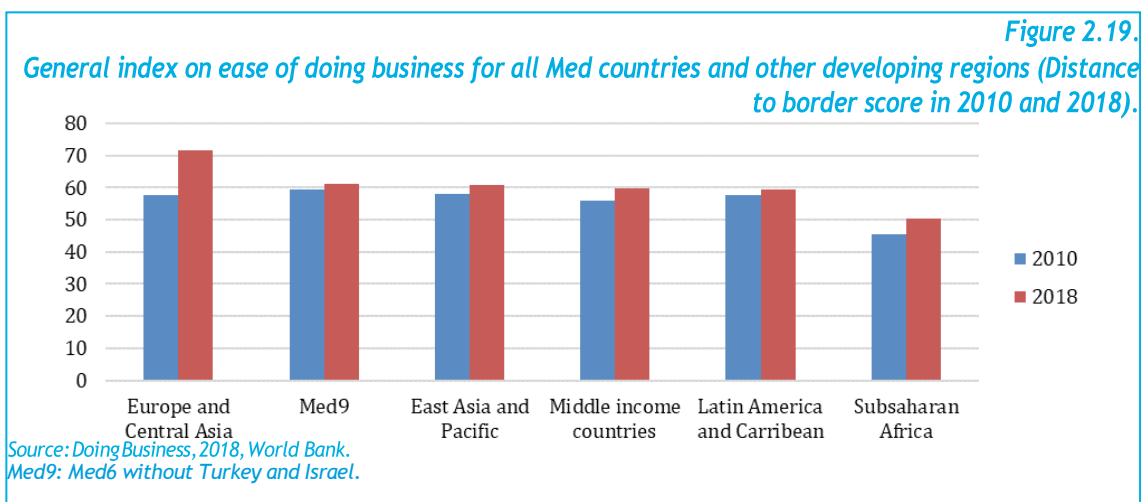
#### **V. A combination of unfavourable factors for the private sector in Mediterranean countries**

##### **V. 1. A fairly positive, yet fragile, image of the business environment**

**The general index on the Ease of Doing Business** (box V.1) shows that Mediterranean countries are generally at the same level as all comparable income countries. Figure 2.19 shows that their score of 60, which represents the distance from the best practices observable in all economies, is equivalent to that of Asian and Latin American countries. It stands between the countries of Europe and Central Asia (score of 70) and those of Sub-Saharan Africa (score of 50).

This observation is confirmed both by the Competitive Global Index of the World Economic Forum (box V.2) and by the Heritage Foundation's Index of Economic Freedom (box V.3). For these two indicators, the overall score for all Mediterranean countries is slightly higher than that of all equivalent income countries (Figures 2.20 and 2.21).

This comparable, or even slightly higher level than other developing or emerging countries regarding the overall business environment assessment can be explained by



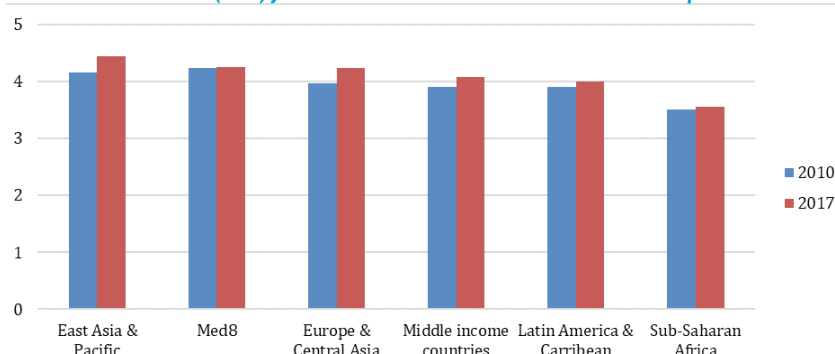
#### **Box V.1. The general index on the ease of doing of Doing Business**

This measurement of the quality and efficiency of the countries' regulatory frameworks is carried out annually by the World Bank and has been in existence since 2003. Although it has a number of limitations (see the 2013 Trevor Manual Commission Report, based on which methodology has been improved in recent years), the Doing Business Report has become an important reference for assessing the ease of doing business in almost every country in the world. Its particularity is to focus on regulations that promote economic activity and those that limit it, considering only ten main areas (business creation, obtaining a building permit, connecting to electricity, transferring ownership, obtaining loans, protecting minority investors, paying taxes, cross-border trade, enforcing contracts and settling insolvency). Data collection is mainly based on a detailed reading of national laws and regulations and administrative rules. This information base is complemented by a series of exchanges with interviewees (private sector specialists and government representatives) in the form of questionnaires, conference calls, written correspondence and field visits. The indicators provided by the Doing Business index represent a benchmark barometer on the business environment for international private investors.

#### **Box V.2 Le Competitive Global Index du World Economic Forum**

The Competitive Global Index (CGI) was developed by Xavier Sala-i-Martin and Elsa V. Artadi and gives an assessment, beginning in 2004, regarding the situation of factors that lead to an increase in productivity and therefore growth in the countries for which the information is available. The particularity of the CGI is that it encompasses, in a single indicator, both the macroeconomic dimension and the micro/business aspects. Its content has evolved over time. The latest version of the CGI (version 4.0), the version used to calculate the 2018 index, includes 12 pillars (Institutions, Infrastructure, ICT Adoption, Macro Stability, Health, Skills, B&S Market, Labour Market, Business Dynamics, Innovation Capacity) and a total of 98 indicators. Each of the pillars now carries the same weighting, whereas beforehand, the weightings depended on the countries' levels of development. In addition, in version 4.0, the CGI scale has been increased from 0 to 100 (instead of 0 to 5), with 100 representing the border, i.e. a target to be achieved for each indicator. The overall index of a country or the score of one of the pillars (or indicators) thus represents the distance to the border. A change in this index or score corresponds to a progress or decline specific to the country in question, regardless of how other countries have evolved. About two thirds of the 98 indicators are informed on the

**Figure 2.20.**  
Competitive Global Index (CGI) for all Med countries and other comparable income countries.



Source: Global Competitiveness Index 2017-2018, World Economic Forum.\*

Data are not available for Palestine.

Med8: Algeria, Egypt, Israel, Jordan, Lebanon, Morocco, Tunisia, Turkey

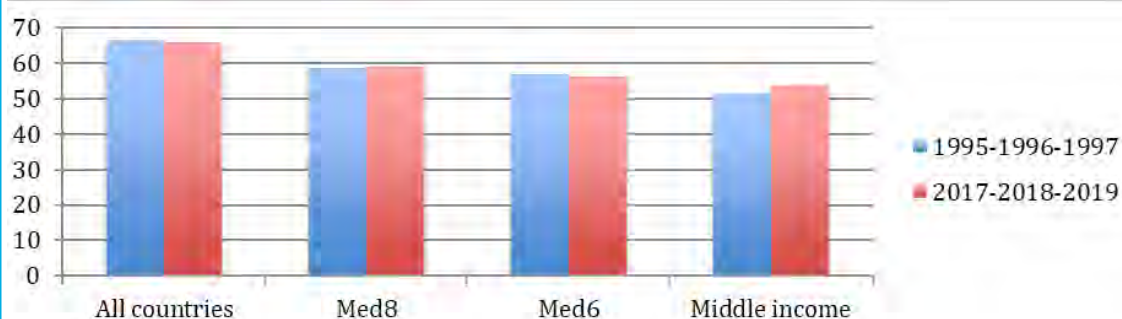
Note: The GCI can only be compared over time with 2017 as the most recent year as from 2018 the scale of the index has been changed from 0 to 100 (instead of 0 to 5)

basis of opinion surveys conducted by the WEF (Executive Opinion Surveys) and the other third of the indicators come from existing data sources (United Nations, World Bank and IMF). The CGI is therefore much more comprehensive than the general index on the ease of Doing Business, but it is less focused on the business climate itself. For more details on the methodology and data sources, please refer to the latest report of 2018, available at the following address:

<http://reports.weforum.org/global-competitiveness-report-2018/>

the progress made by Mediterranean countries in this field and by a number of initiatives implemented in recent years. Among these initiatives, we can note the partnership between the EU and the 10 countries of the southern neighbourhood, namely Algeria, Egypt, Israel, Jordan, Lebanon, Libya, Morocco, Palestine, Syria and Tunisia. This partnership, which is part of the EuroMed Industrial Cooperation, aims to contribute to the development of a business environment favourable to micro, small and medium-sized enterprises (SMEs) in the Med region, using as a reference framework,

**Figure 2.21.**  
Index of Economic Freedom for all Med countries and other comparable income countries.



Source: Index of Economic Freedom 2019 (The Heritage Foundation). To more accurately reflect the business environment, the overall score was recalculated by the authors (Box V.3).

Med8: Algeria, Egypt, Israel, Jordan, Lebanon, Morocco, Tunisia, Turkey Med6: Med8 without Israel and Turkey

**Box V.3. The Economic Freedom Index of the Heritage Foundation**

The Economic Freedom Index was created in 1995 by the Heritage Foundation and the Wall Street Journal. This index is based on existing data, most of which comes from the World Economic Forum, the World Bank (WDI, Doing Business), the Economist Intelligence Unit and the International Monetary Fund. The index focuses on the following four areas: rules of law (property rights, effectiveness of the legal system, government integrity/corruption), government size (tax burden, government spending and public debt), regulatory efficiency (freedom to do business, labour market freedom, monetary freedom) and market openness (free trade, freedom of investment and financial freedom). Each of these 12 sub-indices is assigned a score between 0 and 100 (100 being the best score) and the overall index is obtained by averaging these 12 scores. For more details on the methodology and data sources, please refer to the latest report of 2019 available at the following address :

[https://www.heritage.org/index/pdf/2019/book/index\\_2019.pdf](https://www.heritage.org/index/pdf/2019/book/index_2019.pdf)

It should be noted that in order to have an indicator that more accurately measures the quality of the business environment, we have recalculated the global Economic Freedom Index by focusing on the rules of law, the weight of taxation, the freedom to do business and the opening of markets. In 2019, however, there is very little difference between the overall index we recalculated and the Heritage Foundation's overall index (average of the 12 sub-indices).

**Box V.4. The Small Business Act for Europe (SBA) and the Policy SME Index**

The SBA, adopted by the EU in 2008, gradually supplemented and replaced, from 2011 onwards, the Euro-Mediterranean Charter for Enterprise, which was adopted in 2004 and provided guidelines to improve and homogenise the business climate throughout the Euro-Med area.. The SBA is structured around the following 10 principles:

1. Entrepreneurship education and training, including women's entrepreneurship
2. Efficient bankruptcy procedures and the "second chance" for entrepreneurs
3. The institutional and regulatory framework for the development of SME policies
4. The operational environment for the creation of companies  
Les services de soutien aux PME et les marchés publics
5. Access to finance for SMEs
6. Access of SMEs to EU-Med networks and partnerships
7. Company skills and innovation
8. SMEs in a green economy
9. The internationalisation of SMEs

These 10 principles have replaced the previous 11 principles of the Charter "on which the business policies of the Mediterranean partners should be based"\*. The SBA aims to guide Euro-Med cooperation in the development of SMEs. It thus serves as a framework for the establishment of a set of programmes and projects launched by the EU, which aim to strengthen Mediterranean companies and improve their competitiveness, such as the COSME project, Erasmus+ and the Horizon 2020 programmes.

At the same time, an evaluation tool, the Policy SME Index, structured around the 10 principles of the SBA, was introduced to measure the stage of development of policies., level 1 corresponds to the absence of a specific policy or measure and level 5 corresponds to



full compliance with good practices. A first evaluation of policies and measures in favour of SMEs in the Med countries was carried out in 2008 on the basis of the Charter. A second evaluation was carried out in 2013 on the basis of the SBA by the European Commission, the OECD, the European Training Foundation and the EIB. A new one is in progress. It should be noted, however, that the use of the Policy SME Index is limited, on the one hand, because the data are not available (the indices are given only in the reports through graphs or tables), and on the other hand, because it is applied only for countries in the region and therefore does not allow for international comparisons.

Following this evaluation, the EU launched the project EBESM (Enhancement of the business Environment in the South Mediterranean) whose objective is to support the beneficiary countries in implementing the recommendations of the priority reforms identified by the evaluation and, in this sense, to contribute to the development of a business environment favourable to micro, small and medium-sized enterprises in the Med region, in accordance with the good practices defined by the SBA principles. The project also aims to raise public awareness and strengthen policy dialogue on small business development issues..

\* Extract from the presentation of the Euro-Mediterranean Charter for Enterprise, p. 1,

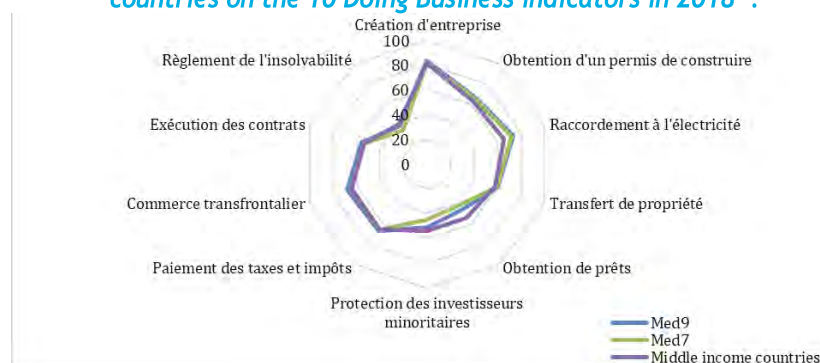
EU best practices as defined in the Small Business Act for Europe (SBA)).

The breakdown of the general index on the ease Doing Business (see Figure 2.22) shows that Mediterranean countries do as well and sometimes better than comparable income countries as a whole in the fields of business creation (it takes, for example, 7 days in Turkey to start a business, 8 in Tunisia, 9 in Morocco, 11 in Egypt, 12 in Israel, 15 in Lebanon, 17.5 in Algeria and 43 in Palestine), obtaining a building permit, electricity connection, transfer of ownership, payment of taxes, cross-border trade and contract enforcement.

The breakdown of the Economic Forum's Global Competitiveness Index into different pillars confirms that a number of advances have been made in the region, since Mediterranean countries are well positioned in terms of infrastructure [23] (Figure 2.23), adoption of information and communication technologies[24] (Figure 2.24), health (which measures only life expectancy, Figure 2.25) and, more surprisingly, the financial system[25] (Figure 2.26) and innovation capacity [26] (Figure 2.27).

Figure 2.22.

Position of Med countries in relation to all comparable income countries on the 10 Doing Business indicators in 2018\*.



Source: Doing Business, 2018, World Bank.

\* Distance to the border measurement of best practices.

Yet, can we deduce that the economic environment is not a problem in Mediterranean countries? The answer, of course, is no. Beyond these global indicators, several elements must be considered.



- The first is that there is a **wide disparity in the situation** between Mediterranean countries and **at least half of them are characterised by relatively low indicators.**

Doing Business gives high scores to 3 of the countries in the region: Israel (71), Turkey (69) and Morocco (68). The World Economic Forum and the Heritage Foundation add Jordan to this group of countries. For Doing Business, Tunisia (63) and Jordan (60) are around the regional average and 4 Med countries are below. These are Palestine (58), de Egypt (56), Lebanon (55) and Algeria (47). The World Economic Forum and the Heritage Foundation rank Tunisia among the least well-positioned countries in terms of business environment (Figure 2.28). In total, for the Heritage Foundation, out of the 8 Mediterranean countries listed, half are either in the "Mostly unfree" group of countries (Tunisia, Egypt and Lebanon) or in the "Repressed" group of countries (Algeria) (table II.1).

Figure 2.23.

**Score of the infrastructure pillar of the CGI for Mediterranean countries in comparison with other comparable income countries**



Source: Global Competitive Index 2018, World Economic Forum.  
Med8: The 9 med countries without Palestine (data are not available in this database).  
Med 7: Med 8 without Israel.

Figure 2.24.

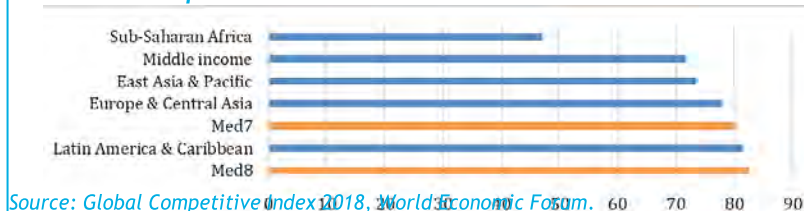
**CGI score for the adoption of information and communication technology pillar for Mediterranean countries compared to other comparable income countries**



Source: Global Competitive Index 2018, World Economic Forum.  
Med8: The 9 med countries without Palestine (data are not available in this database). Med7: Med 8 without Israel.

Figure 2.25.

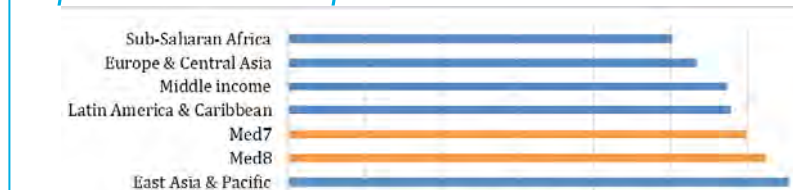
**CGI score for the health pillar Mediterranean countries in comparison with other comparable income countries**



Source: Global Competitive Index 2018, World Economic Forum.  
Med8: The 9 med countries without Palestine (data are not available in this database).  
Med7: Med 8 without Israel.

Figure 2.26.

**CGI score for the financial system pillar for Mediterranean countries in comparison with other comparable income countries**

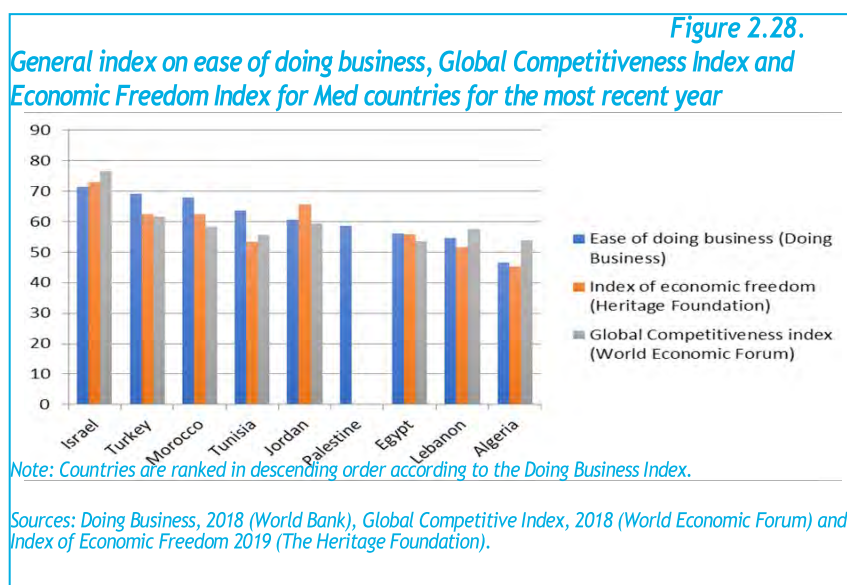
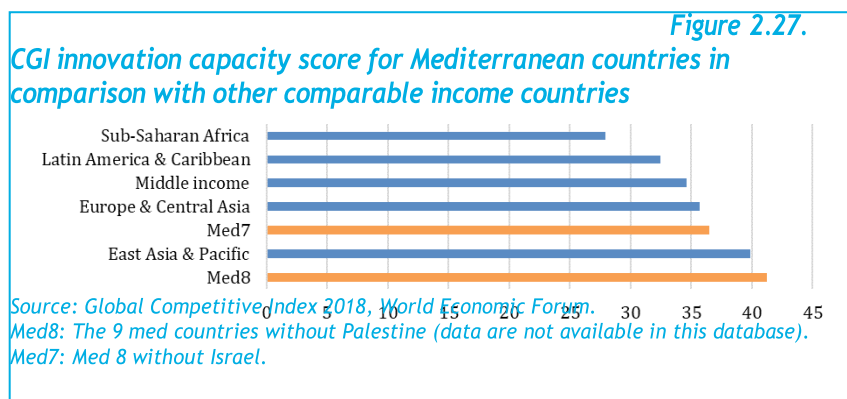


Source: Global Competitive Index 2018, World Economic Forum.  
Med8: The 9 med countries without Palestine (data are not available in this database). Med7: Med 8 without Israel.

- The second element is that the progress made in the business environment and measured by international indicators has generally remained modest. The overall indices for all Med countries (Figures 2.19 and 2.20) have remained virtually unchanged. Taken individually, they even declined for Algeria, Lebanon and Tunisia (Figures 2.29 and 2.30) [27].

- The third is that, despite the progress achieved, the breakdown of these international indicators shows persistent weaknesses. For Doing Business, Mediterranean countries are less well positioned than all other developing and emerging countries, regarding **obtaining loans** [28], **measures to protect investor**

**29] and insolvency settlement** [30] (Figure 2.22). By breaking down the Global Competitiveness Index and the Global Innovation Index, which cover areas broader than the Ease of Doing Business Index, other



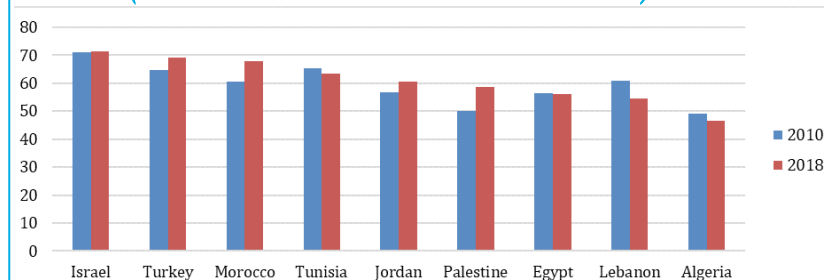
**Table II.1.**  
*Classification of Med countries according to the global international indices for the most recent year*

Classification	Doing Business	Global Competitiveness Index (World Economic Forum)	Classification	Index of economic freedom (Heritage Foundation)
Above regional average	Israel Turkey Morocco	Israel Turkey	Mostly free	Israel
Similar to regional average	Tunisia Jordan	Jordan Morocco Lebanon	Moderately free	Jordan Turkey Morocco
Below regional average	Palestine Egypt Lebanon Algeria	Tunisia Algeria Egypt	Mostly unfree	Egypt Tunisia Lebanon
			Repressed	Algeria

Sources : Doing Business, 2018 (Banque Mondiale), Global Competitive Index, 2018 (Forum économique mondial) et Index of Economic Freedom 2019 (The Heritage Foundation).

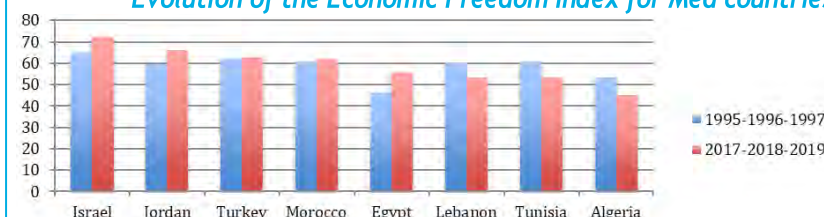
shortcomings in the Mediterranean business environment have been identified. These are (i) the lack of macroeconomic stability (which includes inflation and the burden of public debt, Figure 2.31), (ii) the lack of equity, competition and opening-up of goods and services markets

**Figure 2.29.**  
**Evolution of the General Index on Ease of Doing Business for Med Countries (Distance to Border Score in 2010 and 2018)**



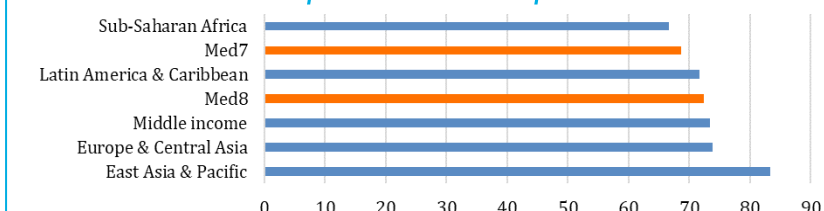
Source: Doing Business, 2018, World bank.

**Figure 2.30.**  
**Evolution of the Economic Freedom Index for Med countries**



Source: Index of Economic Freedom 2019 (The Heritage Foundation). To more accurately reflect the business environment, the overall score was recalculated by the authors (Box V.2).

**Figure 2.31.**  
**CGI Macroeconomic Stability Score for Mediterranean countries compared to other comparable income countries**

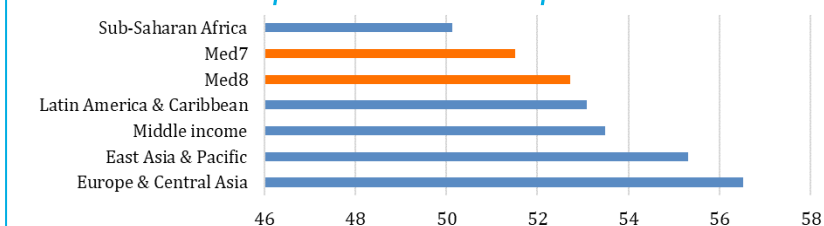


Source: Global Competitive Index 2018, World Economic Forum.

Med8: The 9 med countries without Palestine (data are not available in this database).

Med7: Med 8 without Israel.

**Figure 2.32.**  
**CGI goods and services market score for Mediterranean countries in comparison with other comparable income countries**



Source: Global Competitive Index 2018, World Economic Forum.

Med8: The 9 med countries without Palestine (data are not available in this database).

Med7: Med 8 without Israel.

**Box V.5. Main results of the evaluation carried out by the EC, OECD, European Training Foundation and EIB, as part of the Policy SME Index**

According to the summary note for Ministers on the implementation of the "Small Business Act" for Europe in the Mediterranean Basin, in the Middle East and North Africa 2014 (OECD), "The most significant constraints highlighted by this assessment are as follows:

- The quality of regulatory and business environments, which is characterized by relatively low incentives for entrepreneurship; high barriers to entry for new companies, including cumbersome procedures for registration and licensing; restrictive market access, rigid regulations favouring existing companies and a large informal economy.

- Limited access to external sources of funding due to a combination of factors: weak creditor rights, underdeveloped guarantee registers, high imbalance

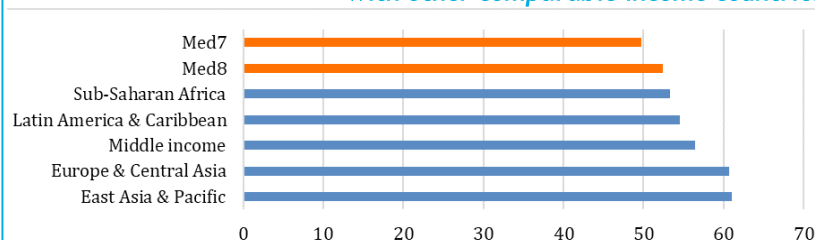
Regarding access to information and weak bank competition (bank credit is the main source of external finance for SMEs).

- lack of adequate professional and management skills to support SME growth and limited access to training schemes.

- Insufficient development of business support networks and services, such as business centres, incubators, innovation support schemes, etc. Another constraint: limited participation in international SME networks.

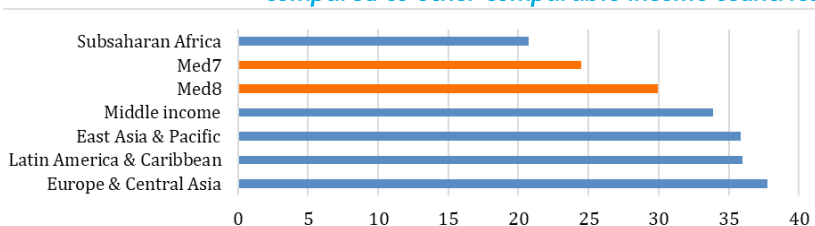
- Poor understanding and cooperation among stakeholders (governments, businesses, civic interest groups) to integrate entrepreneurship into the education system.”

Figure 2.33.  
CGI labour market score for Mediterranean countries in comparison with other comparable income countries



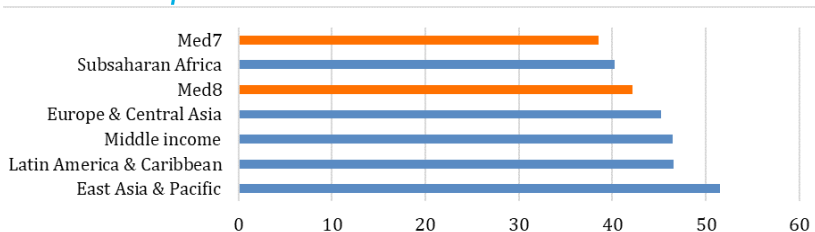
Source: Global Competitive Index 2018, World Economic Forum.  
Med8: The 9 med countries without Palestine (data are not available in this database).  
Med7: Med 8 without Israel.

Figure 2.34.  
GII employee Competence Indicator score for Mediterranean countries compared to other comparable income countries



Source: Global Competitive Index 2018, World Economic Forum.  
Med8: The 9 med countries without Palestine (data are not available in this database).  
Med7: Med 8 without Israel.

Figure 2.35.  
GII policy environment score for Mediterranean countries in comparison with other comparable income countries



Source: Global Competitive Index 2018, World Economic Forum.  
Med8: The 9 med countries without Palestine (data are not available in this database).  
Med7: Med 8 without Israel.

(Figure 2.32), (iii) **lack of flexibility and misuse of human capital in the labour market** (Figure 2.33) and (iv) **the lack of employee skills** [31] (Figure 2.34). Another problem that emerges and weakens the environmental performance of companies is the poor perception of public services, the quality of civil servants and the lack of credibility regarding government commitments, as shown by the IGI's assessment of the **political environment**, which also includes

the perception of the risk of political instability and violence (Figure 2.35). The latest evaluation carried out by the EC, OECD, European Training Foundation and EIB, in the context of the Policy SME Index, which focused on identifying the constraints more specifically affecting SMEs in the region, draws fairly similar conclusions as to these weaknesses. These main constraints, highlighted by the Policy SME Index approach, are presented in Box V.5.

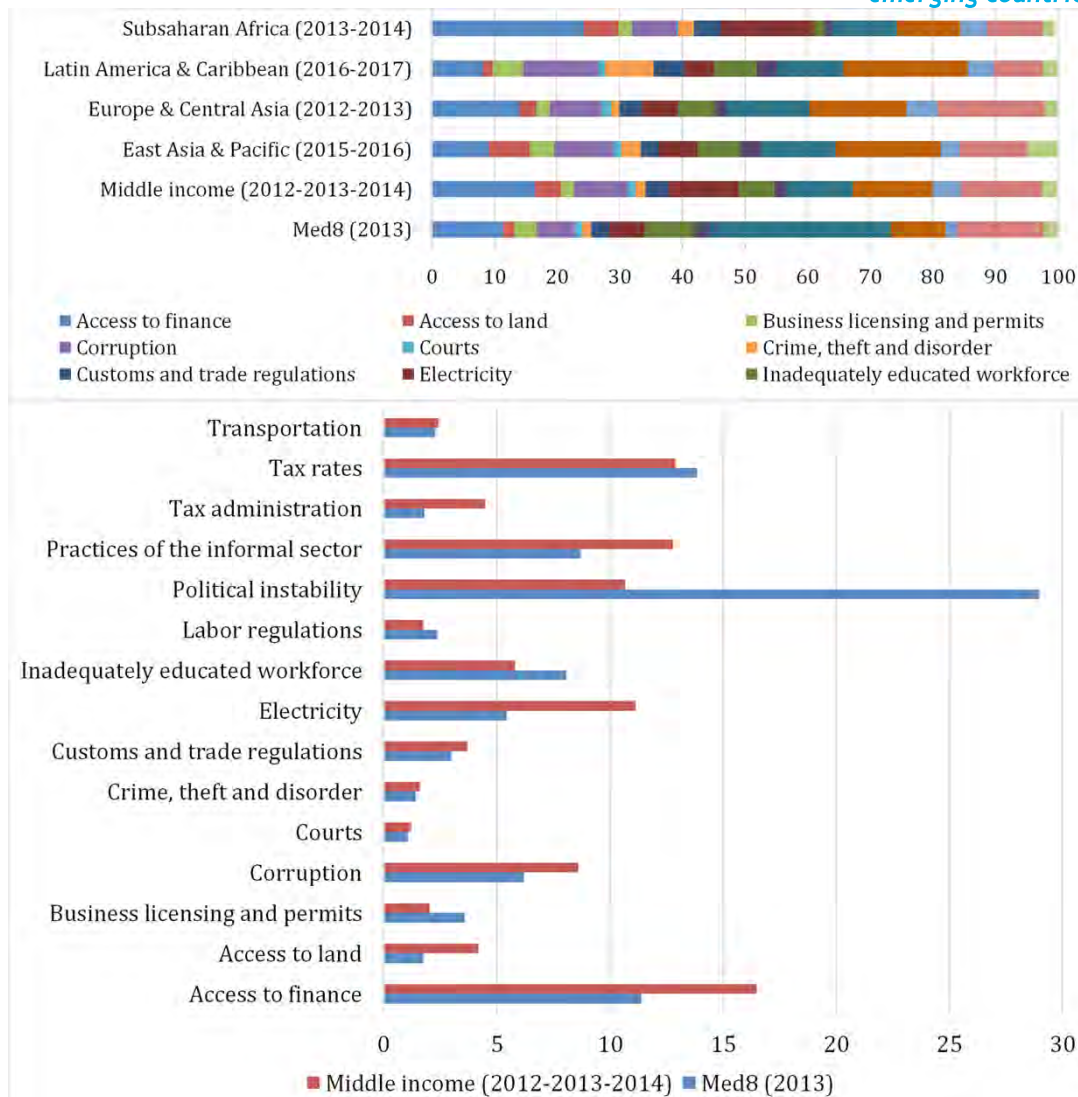


## V2. Difficulties confirmed by testimonies and the opinion voiced by companies

The latest available surveys conducted by the World Bank among companies in developing and emerging countries [32] show that the main obstacle in the Med region in 2013 was **political instability**, following the public protests that broke out in 2011, the unresolved social and economic tensions and the various conflicts in the region. The other

main concerns of companies are **taxes and duties** (including the time required to complete the administrative processes) and **access to financing** (Figure 2.36). This problem of political instability is particularly significant in the case of Lebanon, Egypt, Tunisia and Palestine. In the other Med countries, the main obstacle expressed by companies is access to finance for Jordan, **corruption for Morocco**, insufficiently qualified labour for Israel and taxes and duties for Turkey (Figure 2.37)

**Figure 2.36.**  
*The main obstacles expressed by companies in the Med region and in other developing or emerging countries*



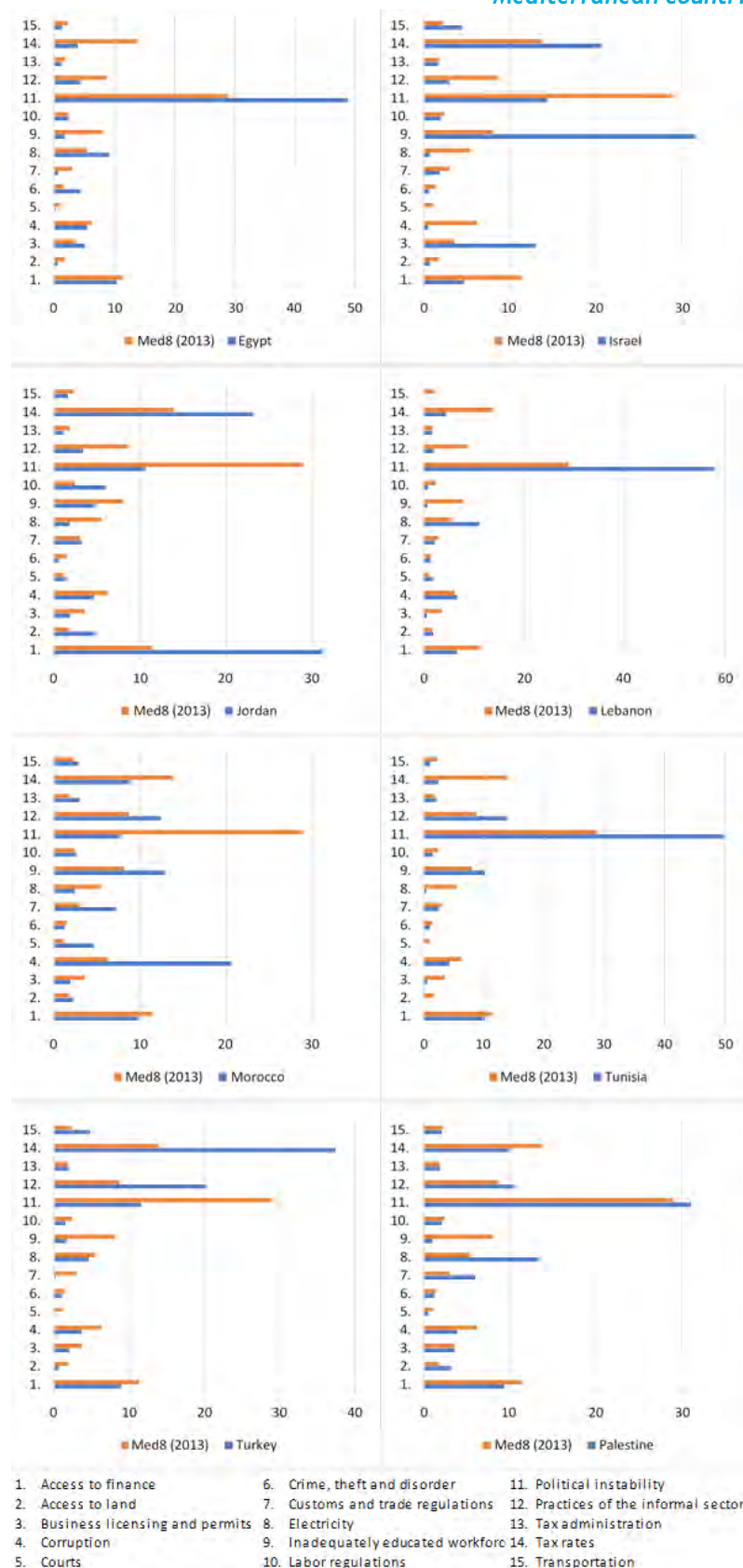
Source: Enterprise Survey, World Bank.

Med8: Egypt, Israel, Jordan, Lebanon, Morocco, Palestine, Tunisia and Turkey.

The World Bank report (2016), which analysed these obstacles in the case of the MENA countries, places particular emphasis, in addition to political instability, on the issue of corruption, access to finance and an unreliable electricity supply, a constraint that affects Egypt, Lebanon and Palestine more specifically and which, on the other hand, is not reflected, as mentioned above, in international indicators. Another important point raised in this report is that dysfunctions in the business environment are more constraining for small and medium-sized companies (SME).

As for **corruption**, also discussed in the following section, this constraint is a major obstacle to private sector development. It includes both the payment of bribes and dysfunctions at the highest level of political power and the capture of rents by a political and economic elite. Corruption concerns a large number of operations carried out by companies since it can affect relations with all its partners and, above all, relations with the administration

Figure 2.37.  
The main obstacles expressed by companies in each of the Mediterranean countries



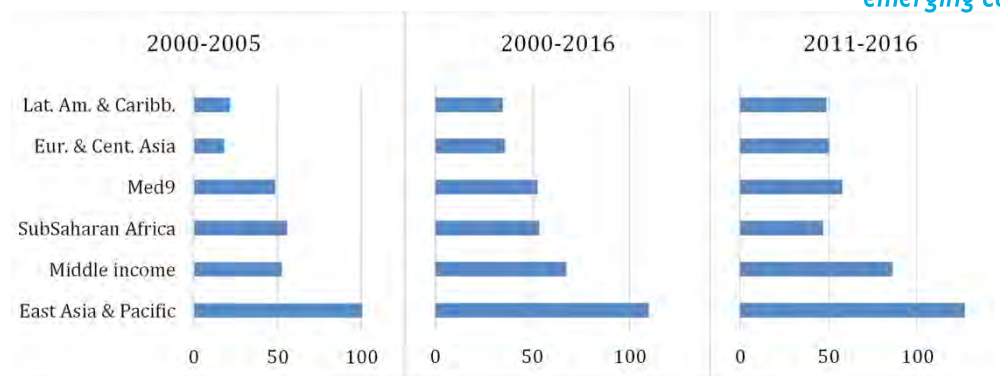
Source: Enterprise Survey, World Bank.

Med8: Egypt, Israel, Jordan, Lebanon, Morocco, Palestine, Tunisia and Turkey.



Figure 2.38.

*The ratio of loans to GDP in the Med region and in other developing and emerging countries*



Source: WDI, World Bank.

Med8: Algeria, Egypt, Israel, Jordan, Lebanon, Morocco, Palestine, Tunisia and Turkey.

and public services, this involves paying taxes and duties at central and local level, obtaining licences and authorisations, acquiring land, obtaining building permits, access to basic services such as water and electricity, etc. An article by Goedhuys, Mohnen and Taha (2016) highlighted, using data from Tunisian and Egyptian companies, the negative effect of corruption on innovation, firm development and job creation. These authors show that companies can use corruption to circumvent the regulatory obstacles they face (such as licences or other marketing authorisations). This system is perverse because the bureaucratic regulations, which, in themselves, are already harmful to growth (see next section), encourage companies to engage in corruption, which also has a negative effect on private sector dynamics.

Concerning **access to finance**, the ratio of loans to GDP, which averaged just under 60% for the region between 2011 and 2016, is slightly above that of developing and emerging countries of Europe, Latin America and Sub-Saharan Africa,

but is much lower than East Asian countries (almost 130%) and all comparable income countries (more than 80%) (Figure 2.38). Moreover, in Mediterranean countries, bank loans are mainly intended for a limited number of large companies and the majority of SMEs have almost no access to credit. One explanatory element is the high level of guarantees demanded by banks and perhaps also the lack of general certification of company accounts, which does not allow banks to have transparent information on the financial situation of SMEs (Augier, Dosis et Gasiorsek, 2012). One of the consequences of this problem of access to finance is that it makes it very difficult for very small businesses and SMEs to develop. Similarly, start-ups do not have trouble with seed funding to start their business as such mechanisms are well developed in certain countries (such as Tunisia), but rather with the financing of their growth [33].

Other difficulties are frequently mentioned by companies, such as **unfair competition from the informal sector, estimated at between 40% and 50% of GDP, problems related to**

**transport and logistics, the difficulty in recruiting people who meet the company's needs and the problem of closing down companies** [34], as bankruptcy proceedings take far too long. Through the testimony of network researchers or entrepreneurs with whom Femise is in contact, concrete difficulties were raised. These are essentially:

- In the case of Egypt, cumbersome labour market regulations and wage taxes, as well as the bureaucratic procedures that companies are required to comply with (Box V.6).
- In the case of Morocco, the burden of regulatory obligations such as licensing, which is supposed to have been virtually eliminated, but which, in fact, continues to be required. The testimony of a young entrepreneur is particularly instructive (Box V.7). It reveals (i) the vast amount of red tape to create a business, in a country that has implemented many initiatives to improve the business environment and has made the most progress among the countries in the region according to Doing Business criteria, (ii) the room left to the discretion of civil servants, corruption and favouritism (an issue that will be discussed in the next section) and, (iii) the limits of international indicators in assessing the business environment, which in this case, for example, included the abolition of the licence to operate, whereas in practice this administrative obligation is still applied.
- In the case of Algeria, the persistence of a system of rents (see the following section), access to capital and land that escapes the market, access to bank credit subject to discretionary power

**Box V.6. Testimony of Tamer TAHA (Founder of Yomken and Researcher)**

*I believe that it is mostly labour market regulations, including wage taxes that hinder the development of companies in Egypt. It is not the amount, but rather the bureaucratic procedures involved in paying taxes and the time spent doing this. As far as I know, there are no electronic methods to remedy this.*

*On the other hand, there is a lack of market information. Many companies have great difficulty in obtaining market data. Data are sometimes available but not accessible.*

of the administration, the weak rule of law and unsecured private property that discourage investment and a quasi-monopoly commercial sector (Box V.8).

- In the case of Palestine, the lack of a reliable legal system demotivates investors, the need to improve the education system so that training is better adapted to the needs of the private sector, the quality (including phytosanitary) of products must be improved, the lack of fair competition in markets, the burden of obstacles and restrictions on Palestinian exports and imports, weak infrastructure, unfair tax system, licensing requirements and lack of border security with Jordan and Egypt (Box V.8).

A number of the problems raised by the companies or the testimonies stem from a common deeper problem that gangrenes each of these companies to different degrees. This is the very close proximity that exists between the political world

**Box V.7. Testimony of Chaymae SAMIR  
(young entrepreneur)**

*A concrete example of an obstacle that comes directly to mind is the authorization to practice that is requested from the Prefecture. The law stipulates the need this document for specific activities, whereas, in practice, a license to operate is required for all commercial activities,.*

*According to the Commercial Code, anyone can start a business (except for activities such as doctors, pharmacists, or activities where the health of citizens must be protected). But in practice, even the most basic commercial activity cannot be undertaken without an a license to practise, in addition to the various licenses to be requested from the health services, fire brigades or others, depending on the business. When I started out, I saw that according to the law, about sixty activities could be carried out freely without this famous authorisation, and only about thirty were subject to the different authorizations and specifications. Whereas in practise, whatever the business, everyone must request a license to practise.*

*The application for authorisation to practice is first submitted to the municipality, with a file containing several documents, such as the lease contract, the commercial register, the company's articles of association, etc. Then the file goes to the prefecture, which assigns it to a commission, which then sends a team on site to carry out an investigation. The investigation team includes representatives of the prefecture, the municipality, the fire brigade, hygiene, local authorities, and finally, an expert on the activity in question. Then several exchanges between these different services and representatives are required (a real headache!) The entire process can take months and it takes at least ten signatures to obtain this document*

*The absence of a regulated and homogeneous procedure opens the field to truly arbitrary abusive decisions, sometimes even influenced by favouritism and personal relationships with the competitors of the company requesting the authorisation. Also, many banks require the administrative authorisation before granting funding. In this case, there is very frequently a misalignment between administrative and legal obligations. A company may exist legally: negative certificate, registration in the commercial register, patent registration, and tax ID registration, yet this same company might be prevented from operating if it does not hold the administrative authorisation.*

*Moreover, the legal registration of a company is laborious and may be considered an obstacle in itself: 4 fairly lengthy processes with several legalisations are required, which represent another barrier in themselves, especially compared to other countries such as the United Kingdom where you can register a business in 15 minutes online and start operating immediately.*

**V.8. Testimony of Najat ZATLA (Lecturer-Researcher, member of Femise)**

*1. I believe that the transition to a market economy, officially initiated in the 1990s, has not disrupted the social order. The apparent consent to the recommended institutional transformations and the adoption of many imported formal rules are circumvented. In fact, the opening up of trade or privatization is thus a model through which the tenants of social order maintain their rents, which often takes the form of transfers, within the same insiders' system, of monopoly rents transferred from the public to the private sector (distribution of oil rents, transfer of land rents, creation of commercial rents, etc.). Political elites continue to control access to all forms of rents.*

Access to capital and land, whether industrial or agricultural, largely escapes the market. The use of (or access to) bank loans is subject to the the administration's discretion. Abundant liquidity, a negative real interest rate during the period 2000-2014 and renewed social stability should have resulted in strong investment growth, which is not the case. As observed by N. Meisel and J. Oula Aoudia (2008), in a context characterised by a lack of institutionalised security and protection, the producer with a shortterm outlook and, in this case, the logic of risk diversification prevails. This results in a fragmentation of investments preventing returns to scale and productivity gains. According to the national statistics office (2011), nearly 90% of the companies surveyed operate in the tertiary sector, two-thirds of which are in trade.. Market services accounted for 27.8% of GDP in 2016, while manufacturing production accounted for only 5.6%.

2. However, although the commercial sector has grown strongly over the past two years, it is characterized by almost monopolistic positions: 0.23% of the companies surveyed report a turnover of more than DA 2 billion, while 97.7% of them report a turnover of less than DA 200 million.

3. The analysis carried out by Hibou (1998) for Algeria, can be matched to the situation in Tunisia at the end of the nineties: "There is no formal liberalisation, which would mean economic empowerment in relation to politics, competition, transparency and the abolition of rentseeking and monopolistic behaviour. The actual change combines, on the one hand, the decreased use of traditional protection instruments and the existence of some competition in certain market segments and, on the other hand, a concentration of economic activities around dominant actors and the perpetuation of political interference in economic affairs, even if it implemented in a different manner.

#### **V.9. Testimony of Mahmoud JAFARI (Lecturer-Researcher, member of Femise)**

##### *Obstacles affecting Palestinian exports*

- Administrative restrictions related to document ratification procedures, export licences, issuance of registration certificates), approval of export invoices and export insurance.
- Customs border procedures, transit period, examination of documents, inspection of goods and procedures, stocks and lower limits, security and customs services at Israeli checkpoints and ports.
- Technical restrictions, packaging, trademarks, health conditions, environmental conditions, veterinary conditions.
- Technical services: loading and unloading, customs clearance, technology, marketing information, sorting and distribution.
- Financial restrictions: fees, adoption of documents, loading and unloading fees, customs clearance fees, lack of financial capacity in banks.

##### *Import barriers*

- Administrative restrictions: document authentication procedures, customs border procedures (technical and security controls, storage and IT system).
- Technical restrictions: packaging, packaging, product weight, brands.
- Financial restrictions: transit fees, document certification, additional fees, disclosure, customer transfers, banking facilities, loading and unloading services.
- Non-technical restrictions: smuggling, reduction of dumping prices, lack of partners from importing countries (monopoly),
- Lack of information on export markets to the occupied Palestinian territories (OPT).

##### *Factors excluding direct investment from OPT-*

- Low confidence in the Palestinian economy.
- The confinement of the Palestinian economy by Israel.
- The subordination of Palestinian trade to the Israeli economy

- *Delay in the importation of raw materials, intermediate materials and machinery.*
- *Poor infrastructure (water, electricity, transport and other infrastructures).*
- *High land prices due to the difficulty of access to Zone C, totally controlled by Israel, which is equivalent to 60% of the West Bank.*
- *Shortages of electricity for manufacturing.*
- *Shortage of water for agriculture and industry.*
- *Unfair tax systems.*
- *The inability of Palestinian courts to implement their decisions.*
- *Difficulty of obtaining licences, requires a few days.*
- *Difficulties in establishing partnerships in small and local markets.*

and a few major business families and which generate rents for the privileged few. In Morocco, for example, about twenty large family groups alone accounted for between 25% and 30% of the GDP in 2010 [35]. The fall of presidents belonging to authoritarian regimes in Egypt and Tunisia and the social protests that have spread throughout almost all the region have not put an end to this system. Whereas, we are convinced that this is largely responsible for the lack of growth and job creation in these countries. This issue of collusion will be addressed in the following section [36].

### **V3. The persistence of relations based on connivance that hinder the development of the private sector**

The connivance between business and politics (also known as "cronyism" or "clientelism") has been common knowledge in Mediterranean countries for a very long time (Kienle, 2001; Sfakianakis, 2004) but has been ignored by the international community. We may recall,

as noted by Rijkers, Freund and Nucifora (2017), that "The World Economic Forum has repeatedly ranked Tunisia among the most competitive economies in Africa, and the IMF and the World Bank have presented Tunisia as a model to be followed by other developing countries". Only the short-sightedness created by the dominating conception of development and the naivety of the economic community, which has lost the habit of questioning dominant models, could lead to believe that the liberalisation of these economies (in particular through the reduction of customs duties, the increase in banking competition, the improvement of investment codes, etc.) would eliminate the rent-based situations.

According to Cammet and Diwan (2014), the cronyism between the State and the elite of the business world has actually been consolidated thanks to economic liberalism. This political and economic elite has adapted and taken advantage of the reforms implemented in most of the region's economies since the mid-2000s (see Cammet and Diwan, 2014 for Egypt; Nucifora, Churchill and Rijkers, 2014 for Tunisia and Boubekeur, 2013 for Algeria). The precise nature of these cronyism varies between countries, but many analyses show that in the region as a whole they have tended to increase over the past 20 years and continue to prevail, even after the Arab Spring protests.

The question here is whether this clientelist system has a causal link with the lack of private sector dynamism and, hence, with the extremely low level of job creation in the Med region? An overview of literature (Diwan et Schiffbauer, 2018; Diwan et Salehi-Isfahani, 2018; Rijkers et al., 2017; Diwan, Keefer et Schiffbauer, 2016; Diwan et Haidar, 2016; Schiffbauer et al., 2015; Bagchi et Svejnar, 2015) reveals that **cronyism**



**has a negative impact on the overall growth of these economies and such a system could explain why, despite reforms and the implementation of a large number of mechanisms, these countries have not yet achieved the expected results, as seen at the beginning of the chapter.**

Cronyism is a considerable obstacle to growth as it has both a direct and indirect impact on the economy:

**- Its direct negative effects** on private sector dynamics pass through several channels.

Firstly, **companies connected with the government capture a large proportion of bank loans.** This was not surprising in the 1990s when, in most Mediterranean countries, banks were largely controlled by the public sector [37]. It is more surprising to note that, as shown in the paper by Diwan and Schiffbauer (2018) in the case of Egypt, this phenomenon has not only continued but even accelerated since the mid-2000s, after the privatisation of domestic banks and the presence of foreign competition on the domestic market. In 2010, companies with the right connections obtained 92% of the loans granted to companies included in the Orbis database. "When companies are perceived as having advantages that unconnected companies do not have, they are likely to attract a disproportionate share of credit, even in a liberalised capital market, because their privileges make them more attractive to private banks, either directly, when they increase their profitability, or indirectly, when these advantages are perceived by the market as public insurance against corporate failure" [38].

Secondly, **connected companies benefit from a form of protection against both external and domestic competition**

through the implementation by the public authorities of a number of administrative measures in the sectors of activity in which these connected companies are active. Rijkers, Freund and Nucifora (2017) showed that in Tunisia, companies connected to the Ben Ali clan were over-represented in terms of production, employment and profits in sectors subject to operating permit applications and foreign investment restrictions. Whereas, these Tunisian companies connected to the Ben Ali clan represented only 0.9% of companies, 5% of production and 16% of the profits of the entire private sector, the share of these connected companies in protected sectors represented 43% of production and 55% of profits. In the other sectors, these shares fell to 1.2% and 3.3% respectively. Thus, a limited number of connected companies [39] can have a significant impact on the structure of the domestic market by limiting the level of competition in a number of activities and, hence, on the country's growth. It is clear that if incoming or existing companies need permits to operate, regulations can be misused to discourage business start-ups and hinder competition between companies operating in the market. Diwan, Keefer and Schiffbauer (2016), observed the same phenomenon in Egypt. As the country accelerated privatization and banking and trade reforms, the government was setting up new barriers and granting privileges to certain companies. Examples include the obligation to build real estate or tourism projects only on state-owned land, the obligation to obtain government licences for certain activities, the granting of exclusive licences for the import of certain products,



the implementation of non-tariff measures, etc. The sectors concerned are real estate, tourism, business services, oil and gas and manufacturing products (textiles, steel, cement, agri-food, etc.). In the case of Lebanon, this lack of competition in certain protected sectors has had a negative impact on net job creation (Diwan and Haidar, 2017). Schiffbauer et al. (2015) show that in the case of Morocco, there is a positive correlation between employment growth in start-ups and an environment characterised by more competition, fair tax treatment, less corruption and fewer dysfunctions in the legal system. In addition, young Moroccan companies that operate in sectors or localities where the administrative burden is greatest, create fewer jobs.

Thirdly, **cronyism inhibits innovation**. Based on the theoretical framework of Aghion et al (2001) [40] which shows, from a theoretical point of view, that in-novation gives companies the possibility to protect themselves, at least temporarily, from competition from other firms in their sector of activity, Diwan, Keefer and Schiffbauer (2016) demonstrate that connected companies that already have lower fixed costs due to the many privileges they enjoy (subsidies, tax benefits, etc.) and large market shares, have no interest in innovating because the benefits will be only low and marginal. At the same time, companies that are not connected and therefore have higher fixed costs in the same sector of activity have little incentive to invest because they are unlikely to be able to increase their market share. Generally speaking, in sectors where connected companies are present, it is in the interest of unconnected companies to remain relatively "discreet" and to work in niche markets, so as to avoid competing with firms that have a close relationship with the political authorities. They may therefore also have few incentives to develop. Generally speaking, in their book "Why Nations fail?", Acemoglu and Robinson (2012) explain that when

economic (and/or political) power remains in the hands of an elite (a situation they describe as non-inclusive economic and/or political institutions), it prevents the "right" incentive systems from influencing economic behaviour. Without the right signals, people make "biased" economic decisions that might seem irrational if the presence of this cronyism system is not taken into account. In their view, only inclusive political and economic institutions (guaranteed property rights, fair legal system, individual freedom, etc.) can guarantee sustainable growth because they are based on innovation and technological change. For the same authors, non-inclusive political and/or economic institutions can be compatible with strong growth only if there is strong political centralisation, capable of allocating resources to high productivity sectors (as is the case in China or South Korea). Moreover, in the case of East Asian countries and, in particular, South Korea, one of the factors explaining their economic take-off is the role played by the strong proximity between the political and business communities, particularly through the chaebols. Very close state-business relations and very proactive industrial policies have enabled the development of new sectors.

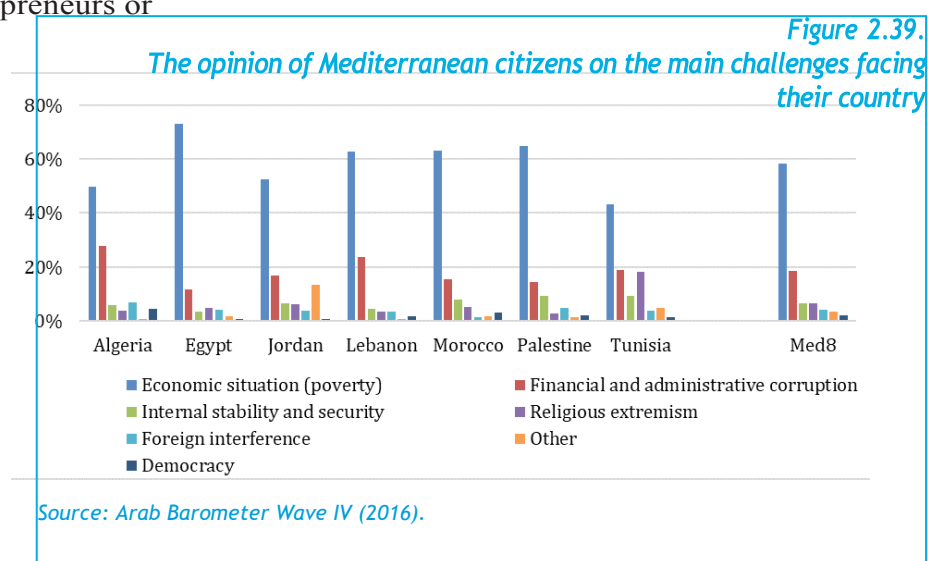
We might therefore question **why this proximity would be a factor of economic success in the case of South East Asian countries and an obstacle to growth in the case of Mediterranean countries?** In the case of South East Asian countries, policy makers aimed to build on the relationship between the political community and the business elite

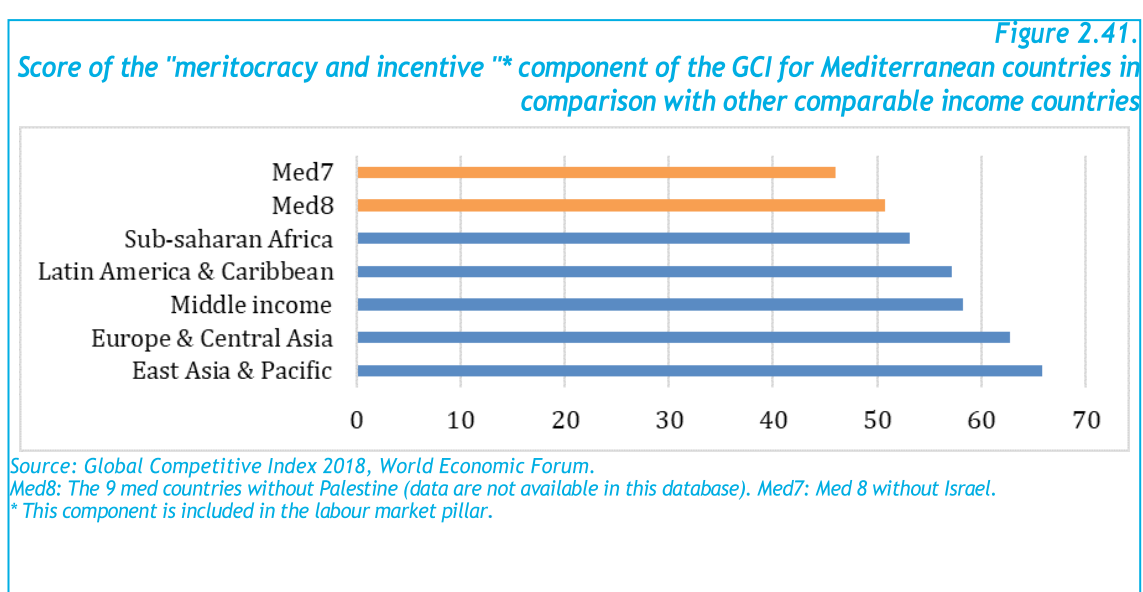
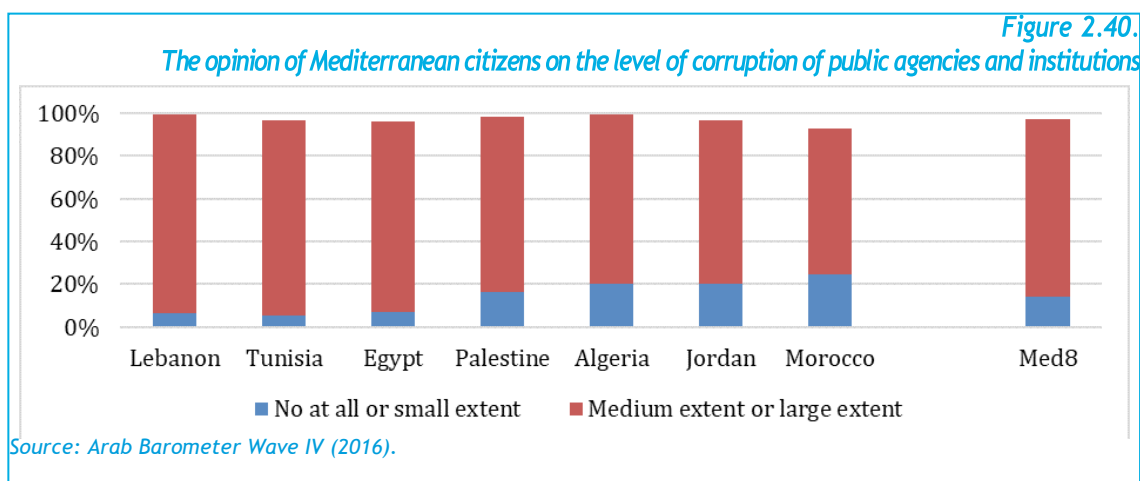
to develop the country's economy, and their choices or decisions were driven by the efficiency of the sectors identified as priorities. The objective was therefore for these large connected companies to become successful in the export market. Thus, even if they were operating in protected domestic markets, they had to face international competition, which forced them to innovate and improve their productivity. If a company in a priority sector did not meet the efficiency criteria, it could no longer be supported and might disappear. In the case of Mediterranean countries, relations between the political and business communities are not at all based on this long-term objective of economic development and export performance of the sectors supported through the connected companies. On the contrary, the objective is to satisfy short-term individual interests by setting up a system of rents through the granting of privileges, sometimes in exchange for political support or personal enrichment.

- **The indirect effects of cronyism** are more insidious and probably even more damaging to countries' growth and development than the direct effects because they have a deeper impact on society (through the behaviour of members of the population, whether employees, entrepreneurs or

households, through the habits adopted in the public service, through changes in representation and value systems, through the development of feelings of injustice and exclusion, etc.) and their consequences (poor governance, corruption, lack of trust in political leaders, in the business community and in the administration, development of the informal sector) are more difficult to contain through public action.

According to the latest survey carried out by the Arab Barometer, the main challenge to be met by the region's populations, after the economic situation of course, is corruption, and this is more marked in Algeria, Lebanon and Tunisia (Figure 2.39). Moreover, this same survey shows that corruption in public agencies and institutions is perceived as fairly or largely widespread by 83% of respondents across the region. This percentage rises to almost 90% or even higher in Egypt, Tunisia and Lebanon (Figure 2.40). As we have seen in the previous section, corruption is perceived by companies as an obstacle in their day-to-day business. We have also seen that it is an obstacle to innovation, their development and job creation.

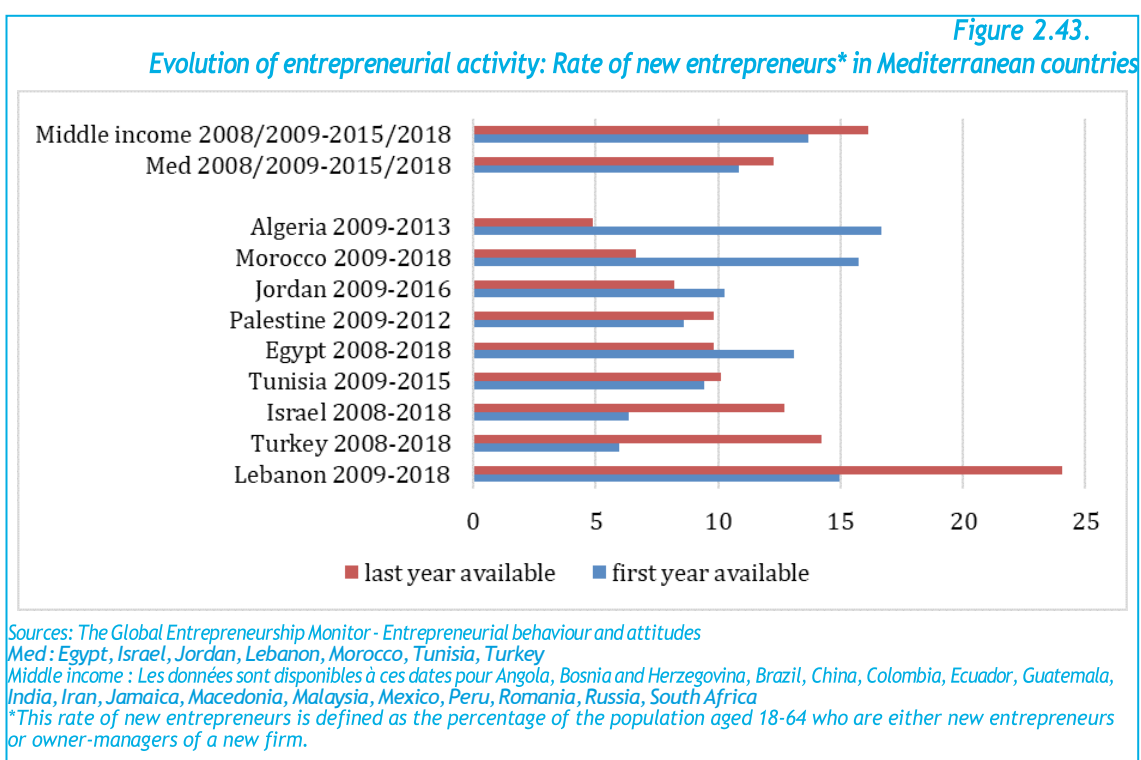
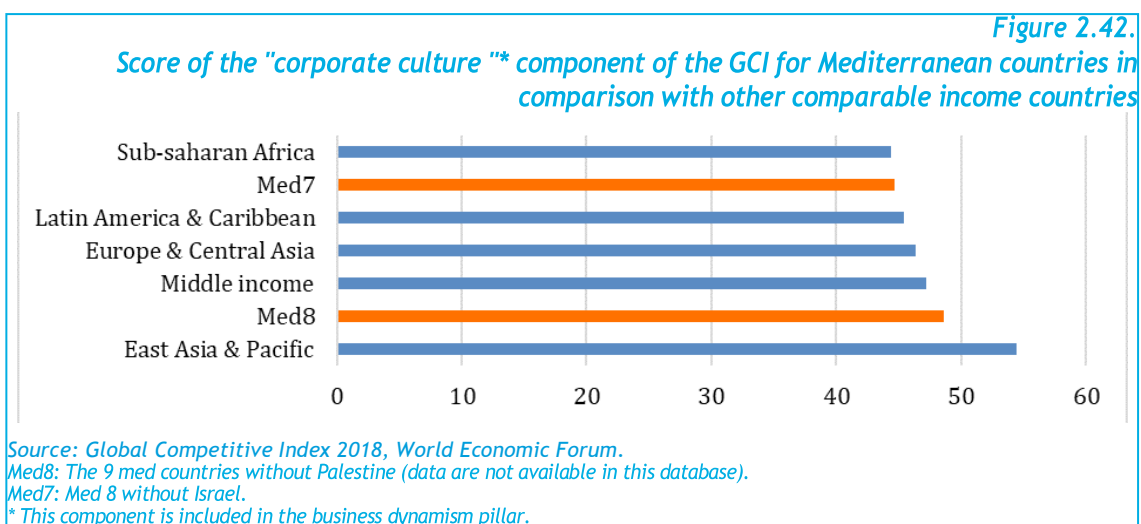




Another negative consequence of this crony capitalism is the weakening of the system of meritocracy and recognition of skills on the labour market. The Global Competitiveness Index shows that of all developing and emerging countries, the Med region has the weakest meritocracy and incentive system in the labour market (Figure 2.41). The administration does not escape this negative effect: an article [41] in the Huffpost of June 2017 denounced, for example, the Moroccan civil service recruitment methods, either by cronyism or by inheriting the position of a deceased or retired father, directly and without any competition. These illegal recruitment practices have reportedly become a custom

that is practically acknowledged by some administrative managers. It is estimated that a total of 26% of public service appointments are given to incompetent and unqualified people.

This unfair system of cronyism, consisting in granting a relatively wide range of privileges to only a few (for example, better access to finance, public procurement, land, subsidies, tax benefits, facilities for obtaining authorisations or licences, protection of certain sectors of competition, etc.) is a source of frustration, loss of bearings and values and, can be perceived as a violation of the fundamental elements of social justice.



The system does not value competence and entrepreneurial success and discourages risk-taking and personal effort. It is not surprising that the Mediterranean countries (without Israel) are poorly positioned in terms of corporate culture (Figure 2.42) and that the rate of new entrepreneurs is lower in the Med region than in other comparable income countries (Figure 2.43). It is also striking to note, first, that this rate of new entrepreneurs has fallen in Egypt, Jordan and, even more strongly in Morocco and Algeria and

secondly, that there is a significant disparity between Mediterranean countries, as this rate ranges from 24% for Lebanon to less than 5% for Algeria. In addition, almost all countries are below the regional average (which is 12%): 7% for Morocco, 8% for Jordan and 10% for Palestine, Egypt and Tunisia.

In total, although there is no evaluation in the literature on the overall economic cost [42] of this system in terms of growth rates

or in terms of non-created jobs, there is sufficient evidence to state with certainty that the negative impact of these crony relationships between the business and political communities is considerable. It can also be said with certainty that there is an urgent need to break down this barrier [43] that is holding back growth in the countries of the region.

Regarding recommendations, acknowledging the existence of a system of connivance that is particularly damaging for the dynamics of the private sector in Mediterranean countries, has a number of implications:

- It is preferable to implement transversal policies (i.e. policies that concern the entire productive system), rather than policies targeted at sectors that pose the risk of being captured by particular interest groups.
- There is an additional argument for replacing subsidies with targeted cash transfers to the neediest households.
- It shows that there is even greater urgency to continue to improve the business environment by integrating the realities or specific conditions involved in this system of cronyism. One of the priorities, for example, is to put an end to bureaucratic control over companies through licences and all other forms of authorisation, since it limits the entry of new companies and the development of existing ones. Another example of improvement would be the implementation of electronic procedures for all administrative services (e-government services), which makes it possible to speed up the various steps and limit (or even eliminate) intermediaries who are not essential and who can be sources of corruption and unfair treatment of entrepreneurs or future entrepreneurs. It is important that these

procedures should concern not only large urban areas but should also apply throughout the country. In general, it is essential to ensure fair and transparent treatment for all companies.

- It is necessary to restore people's confidence and listen to their needs and aspirations. We may take the example of youth, who are able to say today what young people really want in each of the Mediterranean countries; Do they still hope to get job in the public sector? In Tunisia, for example, this no longer seems to be the case. Generally speaking, in each country, it is necessary to find out about these needs and aspirations and take them into account in the development strategies proposed by the policy makers.
- To add to the above point, there is a need for a greater involvement of civil society in decision-making processes. In particular, it is essential that there be more dialogue between public and private sectors, a dialogue that will be essential at the local level to contribute to the economic development of the regions. The Start-up Act recently passed and ratified in Tunisia is a good illustration of the outcome of an initiative from civil society. Its success is based on 4 main elements: (i) the need to bring together initially very fragmented stakeholders to give them a voice, (ii) the involvement of the media and the creation of momentum and genuine emulation within society, (iii) the strong involvement of the private sector and genuine public/private collaboration; and (iv) the lead taken by a Minister, which made it possible to overcome the difficulty linked to the fact that several ministries were involved in this issue of start-ups, which complicated the progress of the project.

However, eliminating cronyism is not easy to achieve, as



it requires profound change, which is likely to come up against resistance on behalf of the beneficiaries of this rent system and on behalf of the public service. Although certain reforms, such as those concerning non-tariff measures or those mentioned above related to authorisations and licences, can be implemented without too much difficulty, such a change involves reworking areas where the design of reforms/measures is complex and where the effectiveness of public action is more difficult to achieve. For example, the action implemented may end up yielding worse implications than the dysfunctions it targeted. A good illustration of this is the fight against corruption in Tunisia, which led to many senior public service managers, in central, regional and local government, being prosecuted (often unjustly), leading to unfounded accusations and, consequently, to major dysfunctions in services [44].

Putting an end to cronyism and widespread corruption requires a competent public administration, both at central and decentralised level, which seems to be lacking at the moment in some Mediterranean countries. Finally, to put an end to this long-standing system that continues to prevail in these countries, requires strong states, capable of defining strategic choices and, above all, of implementing them by resisting lobbies opposed to change. It also requires enlightened, courageous decision-makers who are able to put the general interest before their individual interests, at the central level but perhaps even more so at the local level. The economic development of these countries' regions depends on this.

Although, as mentioned above, the actions to be implemented must be defined at the country

level and correctly prioritized according to the situation in each of them, succeeding in extricating the region from this renowned trap of middle-income countries and providing the entire population with prospects for employment and social progress will require certain pre-conditions that will undoubtedly benefit each of the countries in the region. These main conditions include:

- Intelligent cooperation between the public and private sectors, between decision-makers and civil society, between countries and donors and, also between the States of the region so that companies gradually benefit from the advantages of a large market ;
- An improvement in the position of women in society and their broader integration into the economic sphere: we know that women who study and work are the best vectors for the improvement of human capital formed by future generations and a significant growth factor for years to come;
- Development of training schemes to ensure that the unemployed and, especially among the young, quickly become employable with skills adapted to labour market demands;
- Considering, in the definition of their development strategy, the need to adapt to climate change and ecological concerns that can provide growth opportunities for the region;
- Better monitoring and evaluation of the reforms implemented, once again involving the private sector and civil society;
- Large-scale mobilization in favour of private sector development and, more broadly, entrepreneurship, which requires a multi-stakeholder ecosystem ranging from the education system, to financial institutions and administration. This also requires

better coordination of ministries and all public structures and mechanisms affecting the private sector.

A very positive signal from this region is the increasing involvement of civil society, especially young people and women, as evidenced by the emergence of a growing number of initiatives in the fields of ecology, women's entrepreneurship and, more broadly, new technologies. One of Femise's recent orientations is to support certain of these initiatives by participating in their development and providing them with them visibility. Our involvement in these initiatives is a way to better understand the realities on the ground and the needs of the various stakeholders, so as to better define the content of our recommendations. Public authorities and, probably also donors, should rely more on these initiatives.

## Notes

1. For a review of the literature, see Gill and Kharas (2015), Pruchnik and Zowczak (2017).
2. As seen in the previous chapter, this situation does indeed correspond to that of Mediterranean countries.
3. We should note that authors such as W. Easterly, have shown that it we cannot exclude the possibility of reverse causation : faster growth creates wealth and positive expectations, which boost investment. But as the central question here is how to accelerate growth, we will not include this literature here.
4. These average rates are estimated by the IMF over the period 2000-2014 for oil-importing Arab countries.
5. Data from WDI 2018.
6. The use of the ICOR to evaluate investment effectiveness has a certain number of limits. First, numerator amount includes different types of investments that will have an impact on production with variable delays, sometimes longer than the current year, in particular in the case of public investments. Second, this numerator also includes investments in very different sectors of activity (real estate, agriculture, services, industry, etc.). If data were available, the ICOR should ideally be calculated according to investment types and sectors, which is not possible. Moreover, given the volatility, both of annual investment amounts and the variation in GDP, it is preferable to apply the ICOR calculation over a period of several years.
7. Augier et al (2013) have shown from Spanish data over the period 1991-2002, that the effect of a firm's decision to source intermediate products and capital goods (supposed to have a higher technological content than domestic inputs) from abroad (mainly on the European market) depends on its absorption capacity, measured by the proportion of skilled workers in the firm.
8. We were unable to include the countries of Sub-Saharan Africa.
9. Data could only be obtained for 6 Med countries: Algeria, Egypt, Jordan, Lebanon, Morocco and Tunisia.
10. For Egypt, only a 2-digit sectoral breakdown is only available (NAIC). For the other 5 Med countries, we have the 3-digit distribution of FDI by industry i.e. at a more disaggregated level.
11. Positive effects on the productivity of domestic enterprises have been found only in the case of developed countries.
12. GuiDiby and Renard (2015) show, for example, that FDI had no significant

- impact on industrialisation in 49 African countries between 1980 and 2009.
13. For a summary of these studies, see for example Iamsiraroj (2016), Iamsiraroj and Ulubasoglu (2015), Herzer (2012), Alfaro and Rodriguez-Clare (2004).
  14. Borensztein et al. (1998) show that countries receiving FDI could benefit from the technology provided by multinational companies only when they had a minimum threshold of human capital. This result has been confirmed by several recent studies such as Malikane and Chitambara (2018).
  15. Limited access to financing and/or liquidity constraints prevent companies from benefiting from the presence of multinational companies, see for example Alfaro et al. (2010), Javorcik and Spatareanu (2007).
  16. For a summary of the conditions necessary, both in terms of absorptive capacity and the characteristics of FDI, for the effects of externalities to benefit host countries, see Crespo and Fontoura (2006).
  17. This effect of FDI on the increase in inequalities has been highlighted in particular by Adams et al. (2017) in the case of Sub-Saharan African countries between 1984 and 2013.
  18. This definition is very close to that of Manuel d'Oslo (OCDE and Eurostat, 2005).
  19. By interacting with their customers in foreign markets, exporters gain access to new practices, procedures and incentives to create new products. Similarly, it has also been shown in the literature that imports of inputs can contribute to technology transfer.
  20. The Global Innovation Index provides a very general measure of countries' innovation performance. It is estimated for 126 countries and includes 80 indicators divided into 7 main pillars (institutions, human capital and research, infrastructure, market sophistication, business sophistication, knowledge and technology results, creativity results, market sophistication). All these indicators are available on the website <https://www.globalinnovationindex.org/Home>.
  21. For example, in the part that evaluates the output of innovation, the indicators are the number of patents registered internationally, the number of scientific and technical publications, the H-index of all articles published in each country, international income from intellectual property rights, outgoing foreign direct investment, etc. In view of this observation, Femise, as part of the Next Society project (led by ANIMA), is currently preparing an innovation scoreboard adapted to the Mediterranean countries.
  22. More precisely, it is the score of the distance to the border. This measure indicates the distance of each economy (or group of economies) from a "border" that represents the best performance observed across all countries covered by the Doing Business Index since 2005. The distance to the border thus establishes a benchmark against the best practices observed (whatever the country and whatever the year), and not in relation to a reference country. This distance to the border of an economy is calculated on a scale from 0 to 100, where 0 represents the lowest performance and 100 represents the "border". A score of 60 for a country or group of countries means that the country or group of countries is 40 percentage points from the border, which is determined by the best performance recorded over all economies measured over time. A score of, for example, 65 the following year, means that its regulatory framework has improved.

Note that to present the evolution of the business environment through Doing Business indicators, we prefer to use this score of distance to the border rather than the ranking of the country or group of countries, insofar as the latter depends not only on changes in the country or group of countries in question but also in other countries. Since the "border", as defined, changes little, a change in the score of the distance to the border is most likely to be entirely due to changes specific to the country or group of countries.

23. The infrastructure pillar includes transport infrastructure and access to electricity and water.

24. The "adoption of information and communication technologies" pillar includes subscriptions to cellular and broadband phones (per 100 people), cable and broadband Internet subscriptions (per 100 people) and the percentage of people using the Internet.

25. The "financial system" pillar measures 9 indicators, including the percentage of domestic loans intended for the private sector, access to financing for SMEs, access to risk capital, the stock market valuation of domestic firms as a percentage of GDP, and the soundness of banks, etc.

26. The "innovation capacity" pillar comprises 10 sub-pillars including workforce diversification, cluster development, cooperative patents, multi-stakeholder collaborations, scientific publications, patents, etc.

27. The comparison of the World Economic Forum indicators between 2010 and 2018 could not be presented as the scale of the index has been modified from 0 to 100 (instead of 0 to 5).

This "Obtaining loans" indicator assesses (i) the legal protection of borrowers and lenders, (ii) the existence of certain

measures that facilitate lending under pledge and bankruptcy laws and (iii) the coverage, scope and accessibility of credit information available through credit bureaus.

28. "Investor protection" assesses the level of protection of minority investors in the event of conflicts of interest and shareholders' rights in corporate governance.

29. The "Insolvency Settlement" indicator examines the time, cost and outcome of insolvency proceedings for domestic companies and the soundness of the legal framework applicable to liquidation and receivership proceedings.

For more details on these different indicators that make up the Ease of Doing Business Index, see the methodology on the Doing Business website (<http://www.doingbusiness.org/en/methodology>) which also explains how information is obtained.

30. This indicator includes the share of employment in highly skilled services (in the labour force), the proportion of firms that provide training programmes, the share of research and development expenditure in GDP and the share of highly skilled women in total female employment.

For more details on the indicators that make up the Global Competitiveness Index and the Global Innovation Index, see the methodology in their respective reports (<http://reports.weforum.org/global-competitiveness-report-2018/> <https://www.wipo.int/publications/fr/details.jsp?id=4330>)

31. Enterprise Surveys (<http://www.enterprisesurveys.org>). For the Med region, these surveys are available for Egypt, Israel, Jordan, Lebanon, Morocco, Palestine, Tunisia and Turkey.

This observation of the lack of a continuum in the financing of start-ups was expressed by

- participants in the Next Society advocacy panel of February 26, 2019 in Tunis in which Femise participated.
32. This point was also raised during this advocacy panel (Tunis, 26 February 2019). The observation is that the capacity of entrepreneurs grows after learning from failures.
  33. Tarik Aguizoul (2010), Moroccan family businesses: beyond the cliché, North African Business Development Forum, 22 November 2010, Barcelona.
  34. For these authors, this is one of the two main factors explaining the civil discontent that triggered the Arab uprisings of 2011, the second factor being the dismantling of the State.
  35. As is still the case in Algeria.
  36. Diwan and Schiffbauer (2018), pp. 19.
  37. By choosing to consider only companies related to the Ben Ali family, the number of companies connected in this analysis is largely underestimated. It should also be noted that these authors have shown that the connected companies are generally the largest in the country.
  38. This theoretical framework shows that innovation allows companies to increase their profit by reducing prices and increasing their market share. The rents obtained through innovation are all the greater as the products can substitute those of competitors in their sector and as the fixed costs of these competitors are close to their own fixed costs.
  39. The author of this article is Hafid Ben-marzouq (community activist).
  40. Only sectoral analyses are available, as mentioned above. In terms of empirical valuation, some authors have tried to estimate the "overestimation" of the stock market value of firms that is directly related to the perception of the ability of connected firms to capture rents (Acemoglu, Hassan and Tahoun, 2018 ; Diwan and Haidar, 2017). This type of analysis does not, strictly speaking, give information on the economic cost of this crony capitalism but provides additional evidence of its existence.
  41. Military control of the economy in Egypt is not a step in the right direction. One can only hope that their objective is the long-term development of the country and not the short-term financial interests of an elite.
  42. According to Zine (2016), "this fight against corruption in Tunisia has led to officials not assuming or even shirking their responsibilities. The signatures that commit the department are transmitted to the supervisor, who in turn transmits them to his or her director, etc. Consequently, it is the Minister's Office, or the Minister himself, who is overwhelmed by letters to be signed such as ordinary purchase orders, or answers to ordinary mail, etc. In processing a case, the official no longer makes any effort to understand, takes no initiative, gives no advice and makes no proposals to solve a problem... The fear of being accused of corruption or connivance with the citizen, or of being prosecuted in the same way as his colleague, haunts the civil servant."

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## CHAPTER 3

# The role of Central Banks in Improving the Business Climate and the Attractiveness of Foreign Investment

Case study of Tunisia and Comparative Experiences (Egypt, Jordan, Morocco)

by Sami MOULEY

### I. Introduction background information and explanatory notes

*As shown in the previous chapter, Mediterranean countries face certain growth constraints, while labour supply is reduced by the informal sector that offers very low wages. At the same time, the transition from a model based solely on increasing production factors to a model based rather on increased productivity would seem necessary or even irrefutable. In this context, future development will inevitably depend on the major role played by the private sector.*

*It should also be recalled that in a context in which informal work proliferates, the dynamics of the private sector in Mediterranean countries face recurrent barriers and major obstacles related to the business climate. These barriers to investment and competitiveness range from regulations and administrative constraints, which can hinder entrepreneurship and the development and internationalization of firms, to problems of access to sources of finance, international attractiveness for foreign investment and companies and regulatory constraints related to capital markets, as well as delays due to the quality of institutions and governance.*

*Also, companies benefiting from foreign trade relations have difficulty gaining access to exchange and interest rate hedging, which forms a barrier to their development.*

*The purpose of this chapter is to show that central banks play a major role in private sector reform, and can contribute to improving the business climate and the attractiveness of foreign investment in Mediterranean countries.*

*The chapter will be structured as follows. First, there will be a focus on recent reform actions carried out by the Central Bank of Tunisia (BCT), as well as an analysis of the experiences of other central banks in Mediterranean countries (Egypt, Jordan, Morocco).*

*Six areas of intervention and major challenges will be Investigated based on this initial work:*

- (i) the modulation of the operational framework for the conduct of monetary policy to improve the banking sector's support for investment financing,*
- (ii) the pursuit of financial stability and the management of systemic crises,*
- (iii) a real commitment to the financial inclusion of V-SMEs,*
- (iv) an international commitment to the implementation of structural reform,*
- (v) exchange rate flexibility for greater private sector competitiveness and resilience to external shocks,*
- (vi) the relaxation of exchange rate regulations to optimise the attractiveness for foreign companies and international capital.*

## II. The role of central banks in private sector reforms: focus on the role of the Central Bank of Tunisia and comparative experiences from Mediterranean countries (Egypt, Jordan, Morocco)

### First challenge: Modifications of the operational framework for the conduct of monetary policy to improve the banking sector's support for investment financing

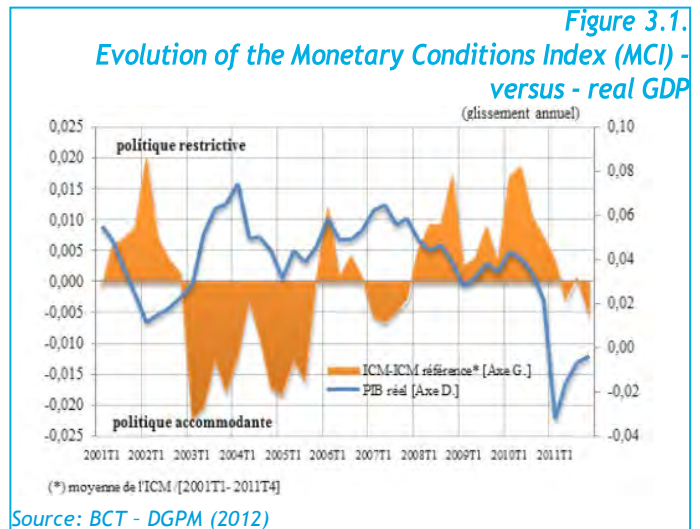
The optimisation of companies' access to funding sources first began by monitoring the structural liquidity of the banking system and better managing systemic liquidity risks. Indeed, at the beginning of the transition period, the banking system in Tunisia was confronted with proven risks of a systemic liquidity crisis, due to the unprecedented deceleration in autonomous factors (strong increase in banknotes and coins in circulation, driven by the hoarding behaviour of households, parallel to the decline in net assets abroad in line with the decline in net foreign currency assets), dropping from +827 MDT on average between 2006-2010 to -2040 MDT in 2011.

To manage this liquidity crisis, several reforms were undertaken, ranging from the implementation of unconventional monetary policy measures to the modernisation

Of its operational framework with a view to improving the banks' support of the economy, and other reforms affecting the interest rate structure.

### Non-conventional monetary policy measures

Non-conventional monetary policy measures were undertaken at the beginning of the transition period. Thus,



as a first step, the BCT initiated a Monetary Easing strategy throughout 2011. First, at the level of bank refinancing, with massive injections of liquidity into the money market (Quantitative

Easing) through weekly tendering mechanisms [1]. Then, at the level of unprecedented downgrading (Credit Easing) of the key rate of 100 basis points overall (in two steps of 50 basis points each) [2] and of minimum reserves of more than 10% (from 12.5% to 2% on deposits

**Tableau 3.1:**  
**Evolution des facteurs autonomes de la liquidité bancaire**

	Période d'avant-transition (2006-2010)						Période post- transition 2011
	2006	2007	2008	2009	2010	Moyenne	
Billets et monnaies en circulation	-3745	-4021	-4414	-4916	-5485	-4516	-6716
Solde net des Adm. Pub.	154	175	-22	-132	-240	-13	26
Dont :							
Solde du compte courant du trésor	-428	-421	-542	-660	-663	-542	-540
Actifs nets sur l'étranger	5334	6974	8124	9859	10344	8127	7772
dont :							
Avoirs nets en devises	6799	8924	10264	12550	12963	10300	11098
Autres facteurs nets	-1662	-2795	-2588	-3221	-3586	-2771	-3122
Facteurs autonomes de la liquidité	81	333	1100	1590	1033	827	-2040

Source : A partir des données de la BCT.



with an in-life of 3 months, from 1.5% to 0% on deposits with a life of between 3 and 24 months and from 1% to 0% on special savings accounts).

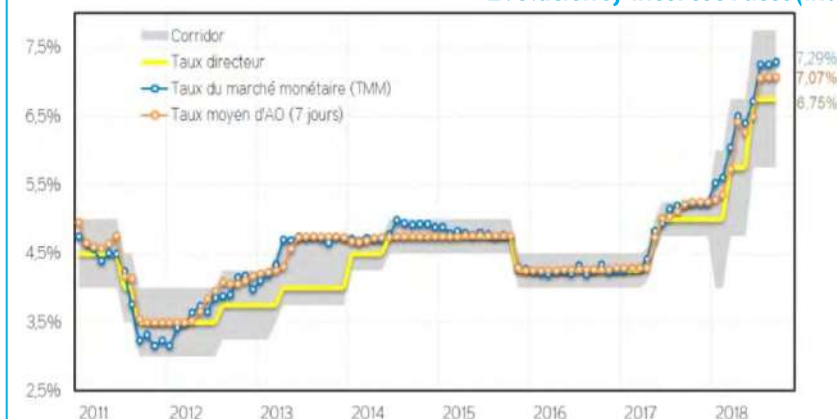
Although the easing strategy was timely for managing the overall liquidity risks of the banking system, it nevertheless proved to be inadequate in stimulating activity. The resurgence of inflationary pressures from the first half of 2012 onwards imposed a tightening of monetary policy, which was, however, implemented gradually.

### Prudent management of exit strategies from unconventional measures

A tightening of monetary policy (Monetary Tightening) to break the chronic inflationary pressures, which since August 2012 have been of a global and structural nature, was initiated with a series of gradual modulations.

First, with the BCT's decision to raise the key interest rate by 25 basis points to 3.75%. Then, with the gradual abandonment of the "full allotment" policy (which consists in refinancing all of the banks' liquidity needs), by recalibrating its refinancing operations on the basis of its own forecasts of the banks' liquidity needs. Another series of complementary monetary policy tightening measures was also initiated.

Figure 3.2.  
Evolution of interest rates (in %)

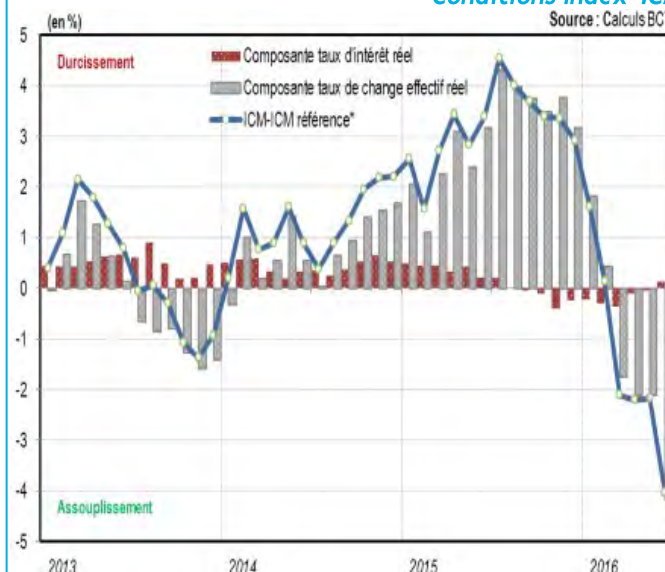


Source: BCT (2018)

Interest rates continued to rise gradually until reaching 6.75% in June 2018 [3].

Similarly, in its role as lender of last resort, the BCT set up an emergency liquidity facility intended solely for solvency banks but temporarily illiquid, accompanied by the introduction of a collateral discount facility for claims eligible for refinancing operations.

Figure 3.3.  
Exits from non-conventional measures (Monetary Conditions Index-ICM)



Source: BCT - DGPM (2016)

### Modernisation of monetary policy instruments to improve bank lending to the economy

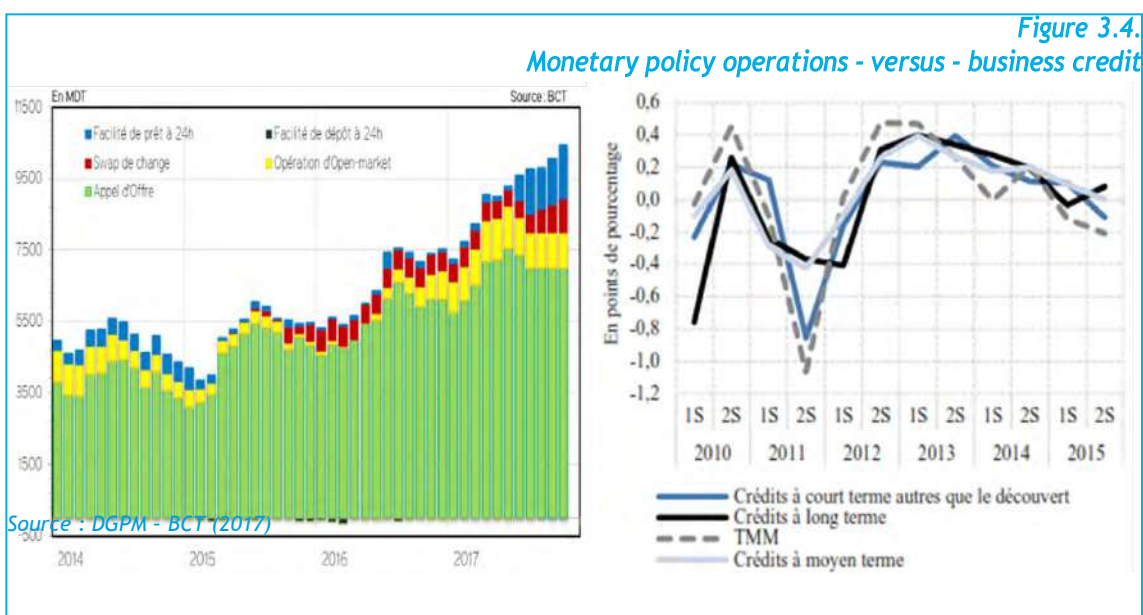
The regulation of bank financing was a source of exclusion for Small and Medium Enterprises (SMEs) in the granting of credit. Indeed, the BCT circular N°87-47 of 23 December 1987, which regulated the conditions for granting bank management loans as well as the ratings of commitments by signature within the framework of the current activity of SME clients (professionals and large companies), conditioned the maximum volume of operating loans granted to them to a ceiling of only 1 month's turnover (and 15 days for those operating in the trade and services sectors). To overcome these shortcomings, a redevelopment was introduced in August 2016 with Tunibor as the benchmark for money market transactions in dinars.

This new benchmark for the remuneration of bank deposits and loans, in addition to the average monthly money market rate (MMR), and which is a contribution to the development of the money market, has

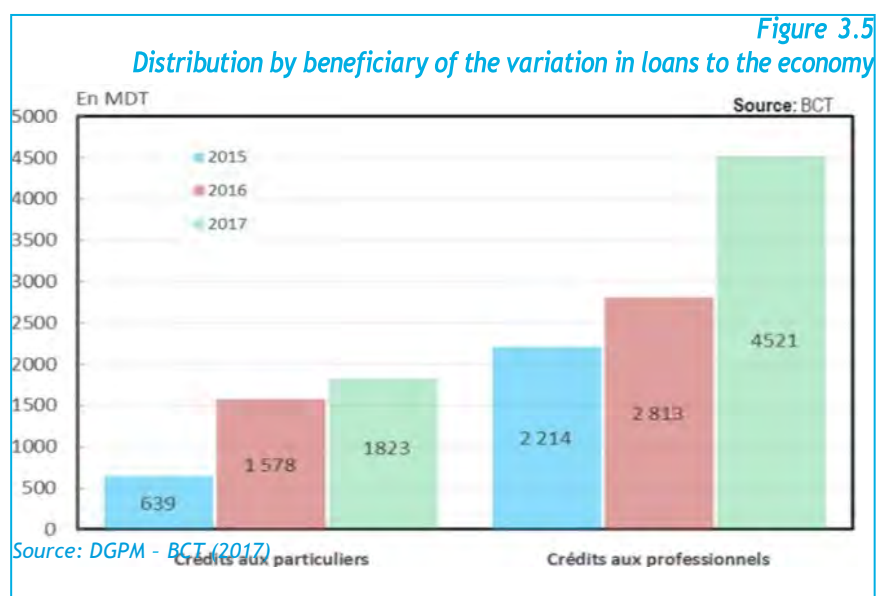
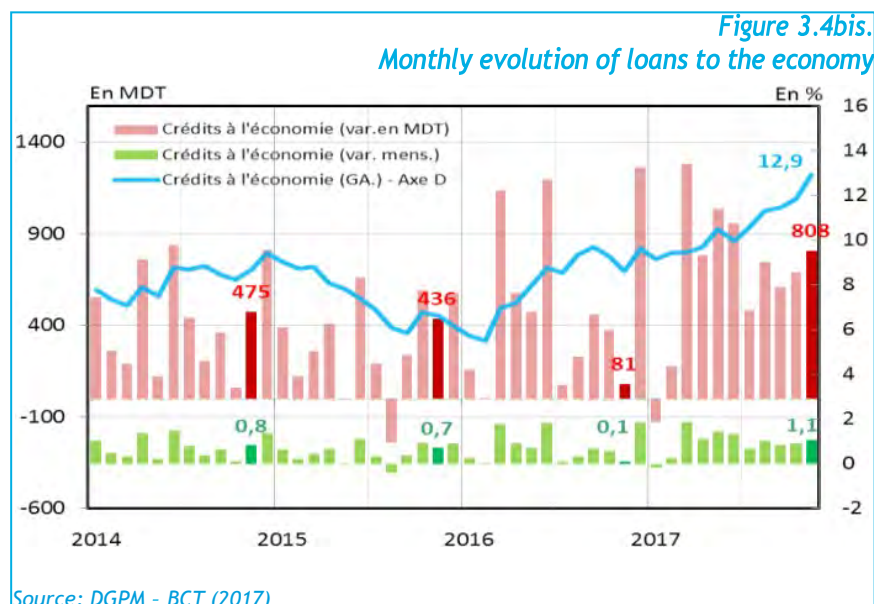
enabled the emergence of new short-term interest rate references that go beyond the overnight money markets, which will ultimately strengthen banking competition, and will encourage the relaxation of the conditions for granting bank loans to SMEs.

In the same vein, Bank Circular No. 2017-02, dated 10 March 2017, introduced a new manual of monetary policy operations to adapt to Act 2016-35 of April 2016 on the new statutes of the BCT [4]. In addition to tender operations, the diversification of other monetary policy operations has made it possible to reduce tensions on bank liquidity, improve the mechanism for transmitting monetary policy impulses through the interest rate channel and reallocate banks' resources to medium- to long-term loans to companies (Charts 3.4 and 3.4.bis).

Indeed, loans to professionals increased by 61% in the first ten months of 2017, compared with the same period in the previous year, driven mainly by a significant increase in short-term loans (Figure 3.5).



One of the latest innovations introduced in 2018 also concerns the operational modalities for strengthening the BCT's intervention on the money market through enhanced targeting of refinancing to further support investment and productive sectors. Hence, in November 2018, the BCT set up a new longer-term refinancing instrument with a maturity of six month in order to better direct bank credit towards financing investment in the real sector (and to increasingly regulate loans to individuals). This refinancing mechanism is intended for banks that grant medium- and long-term loans to finance investment projects in productive sectors.



The refinancing operations are carried out by means of an auction in the form of reverse transactions as provided for in Circular to Banks No. 2017-02 on the implementation of monetary policy. According to this circular, eligible collateral now includes medium- and long-term loans granted by banks to finance new and/or expansion investment projects that are no more than two years old from the date of release. Finally, a better dynamisation of interbank financing on the dinar money market was also boosted by the BCT circular N°2018-12 of 28 November 2018.

The reforms of the monetary policy framework and instruments in Tunisia, which were analysed earlier, were in fact juxtaposed with several actions to modernise micro-prudential supervision for the effective control of banking risks, for developments in terms of: (i) liquidity risk management, (ii) prudential capital requirements, (iii) risk concentration and division, (iv) classification and provisioning requirements for receivables,

and (v) liquidity risk management [5]

for all credit categories and for all institutions [8].

### Reform of the regulation on excessive interest rates

The rationing of loans to SMEs is due to the current restrictive regulation of excessive interest rates (or usurious rates) which is governed by law N°99-64 of 15 July 1999, as amended and supplemented by Act No. 2008-56 of 4 August 2008. This system for capping interest rates on loans granted by financial institutions and merchants stipulates that a loan granted at an excessive interest rate is a conventional loan granted at a total effective interest rate (TEG) that exceeds, at the time it is granted, by more than one-fifth[6] (more than one-third previously[7]) the average effective interest rate (AER) applied during the previous half-year by banks and financial institutions

It shows that the average effective rates (and their corresponding excessive rates) by type of credit are significantly higher for companies in the medium and long-term credit sector and for individuals in the consumer credit sector. The excessive nature of medium- and long-term borrowing costs explains why, despite the over-banking of the financing system in Tunisia, bank loans to productive sectors are limited to short-term loans..

Even though the threshold of the excessive interest rate (usury rate) in Tunisia is high, particularly for medium and long-term loans, with an average of (9.75%) during the second half of 2018, it remains nevertheless lower than that applied for example in Morocco (14.3%).

**Table 3.2.**  
**Average effective interest rates (AER)**  
(en %)

Catégorie des concours	2016		2017		2018
	1 <sup>er</sup> semestre	2 <sup>ème</sup> semestre	1 <sup>er</sup> semestre	2 <sup>ème</sup> semestre	1 <sup>ère</sup> semestre
1) Crédits à court terme, découverts non compris	6,56	6,61	6,64	7,20	7,76
2) Découverts matérialisés ou non par des effets	8,58	8,60	8,66	8,97	9,42
3) Crédits à la consommation	8,67	8,64	8,45	9,06	9,44
4) Crédits à moyen terme	7,00	7,14	7,15	7,56	8,16
5) Crédits à long terme	7,03	6,92	7,04	7,66	8,07
6) Crédits pour le financement de l'habitat *	7,74	7,63	7,64	8,20	8,46
7) Leasing mobiliers et immobiliers	10,16	10,03	9,75	9,89	10,19
8) Affacturage	8,17	8,26	8,19	8,64	9,49

Source: BCT and Ministry of Finance

**Table 3.3.**  
**Threshold of excessive interest rates corresponding to the AER**  
(en %)

Catégorie des concours	2016	2017		2018	
	2 <sup>ème</sup> semestre	1 <sup>er</sup> semestre	2 <sup>ème</sup> semestre	1 <sup>er</sup> semestre	2 <sup>er</sup> semestre
1) Crédits à court terme, découverts non compris	7,87	7,93	7,96	8,64	9,31
2) Découverts matérialisés ou non par des effets	10,29	10,32	10,39	10,76	11,30
3) Crédits à la consommation	10,40	10,36	10,14	10,87	11,32
4) Crédits à moyen terme	8,40	8,56	8,58	9,07	9,79
5) Crédits à long terme	8,43	8,30	8,44	9,19	9,68
6) Crédits pour le financement de l'habitat *	9,28	9,15	9,16	9,84	10,15
7) Leasing mobiliers et immobiliers	12,19	12,03	11,70	11,86	12,22
8) Affacturage	9,80	9,91	9,82	10,36	11,38

Source: BCT and Ministry of Finance



The mechanism in question was initially intended to protect bank borrowers against any excessive financing conditions, and against potential unfair competition between banks. Nevertheless, the imposed ceilings on usury rates have contributed to further restricting bank competition, have formed barriers to accessing sources of bank financing and, above all,

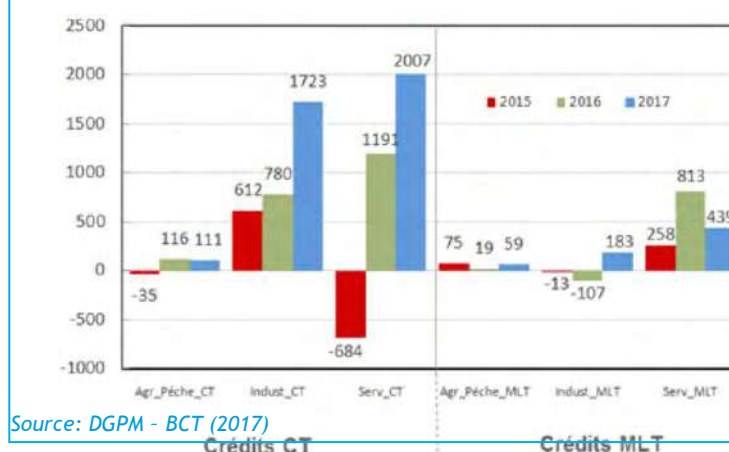
have not encouraged banks to charge better rates for their loans according to differentiated levels of risk (by type of borrower and maturity). As pointed out earlier, these ceilings have also favoured short-term loans at the expense of medium- and long-term loans..

Also, this regulation of excessive interest rates has become barrier to accessing sources of bank financing because it applies by credit category and not by type of borrower. The regulations have introduced inequity, in particular towards professionals (craftsmen, independent professions), traders or young graduates seeking to set up their own businesses who, by definition, are able to assess their risks but who, in the absence of the guarantees requested by the banks, cannot have access to financing because of the ceiling.

The regulation caps interest rates very uniformly (i) limiting access to certain "bankable" customers, (ii) without however ensuring that it fully meets the objective of protecting vulnerable populations.

For this reason, the BCT has engaged in a reform to relax the law on excessive rates accompanied by the creation of a private loan bureau, the modernisation of the central risk

Figure 3.6  
Breakdown by maturity of loans by sector



Source: DGPM - BCT (2017)

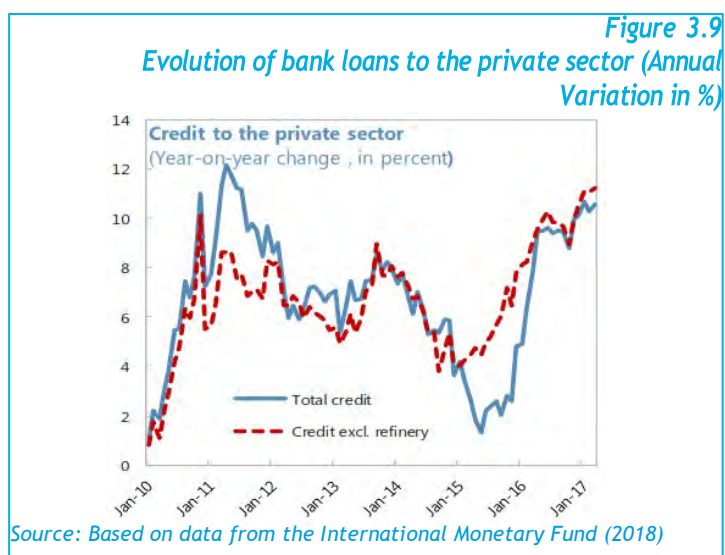
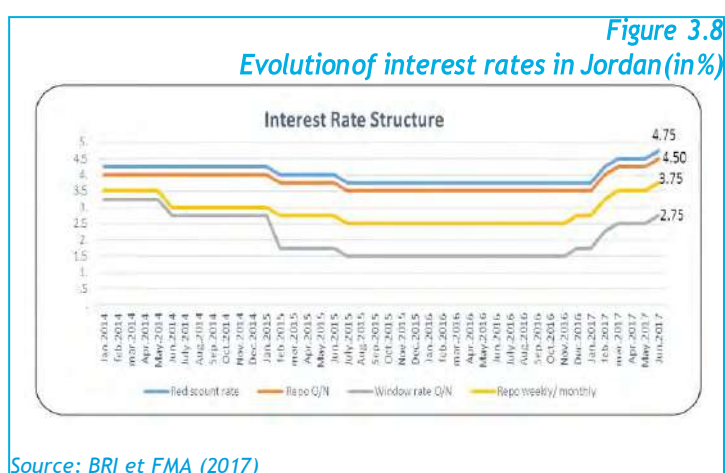
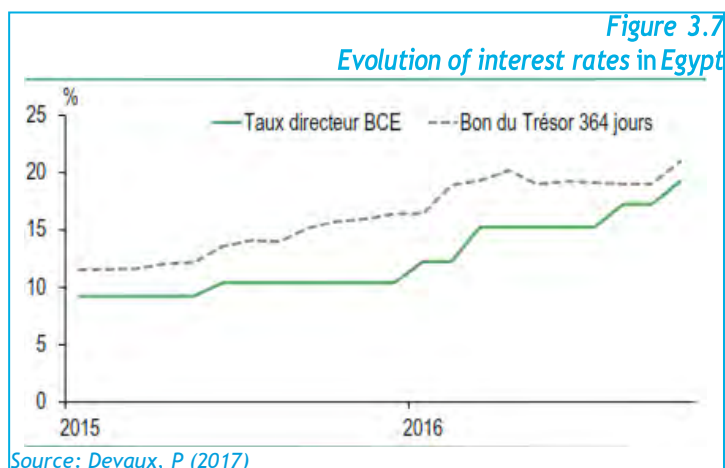
incentives to encourage banks to develop tools to measure and price their risks, through circular N°2016-06, for banks and institutions, relating to the system counterparty rating.

### Focus on comparator countries

As regards the conduct of monetary policy, only the Central Bank of Egypt (ECB) was able to opt for an accommodating monetary policy during the last period by adopting, as in Tunisia, a tightening of monetary conditions. Indeed, the reference interest rate has increased since September 2016 by 885 base points to 19.25%. This increase responds mainly to a twofold objective: to combat inflationary pressures and, above all, to continue to improve the liquidity of the banking system in foreign currencies by draining the currencies that remain outside the official banking system towards bank deposits, the remuneration of which is increasing [9].

In addition, and following the adoption by the ECB of a floating exchange rate regime [10], the interest rate instrument has become the main nominal anchor of monetary policy to serve price stability. A transition program towards an inflation-targeting regime was implemented in 2018 to limit the volatility of the economic cycle and to anchor inflation expectations.





The same monetary stimulus strategy was implemented by the Central Bank of Jordan (BCJ). Indeed, since August 2013, the Jordanian

economy has shown positive developments in its fundamentals and a sustainable level of expected inflation which has given rise to an increase in the attractiveness of the Jordanian dinar, a significant improvement in the current account and growth in foreign exchange reserves. Within this favourable context, the BCJ lowered interest rates on all its monetary policy instruments on four occasions : in 2013 and 2014 by 125 base points, then in 2015 by 50 base points, from 3.5% to 1.75%, with a final upward correction in May 2017 of 100 base points to reach 2.75%. Similarly, a revision of the operational framework for the conduct of monetary policy was adopted in February 2015, introducing the BCJ main rate as the main reference rate. These easing measures were motivated by the optimization of conditions for Jordanian SMEs access to bank financing, which also benefited from an additional preferential refinancing program with sectoral targeting (industry, tourism, agriculture, renewable energy and information technology), for an amount of 1.1 billion Jordanian dinars (5% of the direct facilities granted by banks). As a result, bank lending to the economy has increased.

With a deceleration of its reference rate, the Central Bank of Morocco (Bank El Maghrib - BAM) also maintained its accommodative monetary policy strategy in the face of controlled inflation. Average inflation for the last five months of 2018 was about 1% year-on-year, due to lower food prices. -

Since BAM lowered its reference interest rate to 2.25% in March 2016, lending rates have also fallen.

This led to a recovery in private sector credit growth in the second half of 2018, after a deceleration due to the contraction in the mobilization of bank deposits.

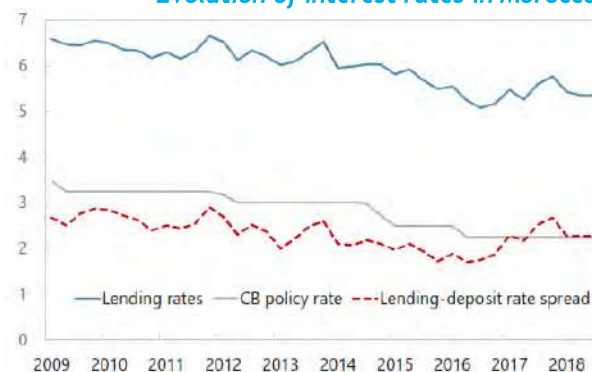
## II.1. Second challenge: Financial stability and systemic crisis management

### A new banking law aimed at the effective protection of depositors

Established by Act No. 2016-48 of July 2016, the new Banking Act introduced a bank deposit guarantee fund with the following objectives:

- (i) The introduction of a safety net to prevent the contagion effect of a bank in difficulty on the banking system by providing prompt compensation to depositors,
- (ii) The creation of the national bank deposit guarantee fund in the form of a public institution with a legal status and financial and administrative autonomy [11],
- (iii) The option for a bank deposit guarantee fund in the form of a "Pay Box plus" to compensate depositors in the event of unavailability of their deposits and to contribute to financial stability by providing a bank in difficulty with the necessary financing under a resolution plan,
- (iv) The definition of the method of intervention of the Bank Deposit Guarantee Fund in the resolution plan,
- (v) The definition of the Bank Deposit Guarantee Fund's investment policy based on rules that guarantee resources security.

Figure 3.10  
Evolution of interest rates in Morocco (in %)



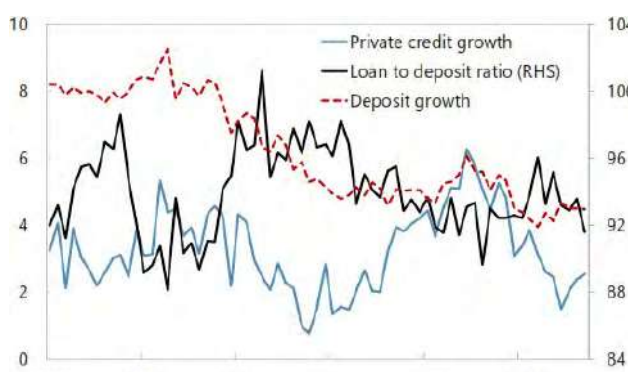
Source: Based on data from the International Monetary Fund (2018)

Figure 3.11  
Evolution in headline and core inflation in the Morocco (in %)



Source: Based on data from the International Monetary Fund (2018)

Figure 3.12  
Evolution of bank loans - VS - mobilization of deposits (in %)



Source: Based on data from the International Monetary Fund (2018)

- (vi) The definition of deposits eligible for compensation. These measures come in addition to the reformulation of the BCT's mission as a lender of last resort [12].

In addition, in June 2014, in preparation for the reorganisation of its mission as lender of last resort, the BCT set up a systemic liquidity management system, in the form of an emergency liquidity facility for solvent, but temporarily illiquid, banks only.

In the same vein, for systemic liquidity management, a system of guaranteed concession prices has been created for debt obligations that are eligible for refinancing operations, thus allowing the BCT to rationalize its massive liquidity injections for refinancing purposes.

### **A system for macroprudential management and regulation**

The purpose of implementing a macroprudential policy is to prevent the emergence of financial imbalances, in particular by (i) reducing the risk of contagion and mitigate systemic risks, and (ii) strengthening the shock absorption capacity of financial institutions. Systemic risks (and crises) are defined as risks (crises) of disruptions in the financial system that could have serious repercussions on the real economy.

Law 2016-35 on the new statutes of the BCT[13] introduced a new system of macroprudential management and regulation, which will now be based on the implementation of indicators of the soundness and robustness of the financial system and on the monitoring of early systemic risk factors. In order to preserve the stability of the financial system, this law allows the BCT to intervene with systemically important entities by extending monetary policy instruments to two complementary non-conventional modulations :

- (i) A new form of refinancing under the specific lending facility for financial

institutions whose exposure to systemic risk could affect financial stability (in particular banking institutions exposed to public company deficits);

- (ii) An extension of the beneficiaries of the BCT's lending facilities by the option of direct financing of non-financial companies, such as the national deposit guarantee fund, whose remit and organisational arrangements have been adopted by the new banking law [14].

### **Focus on comparator countries**

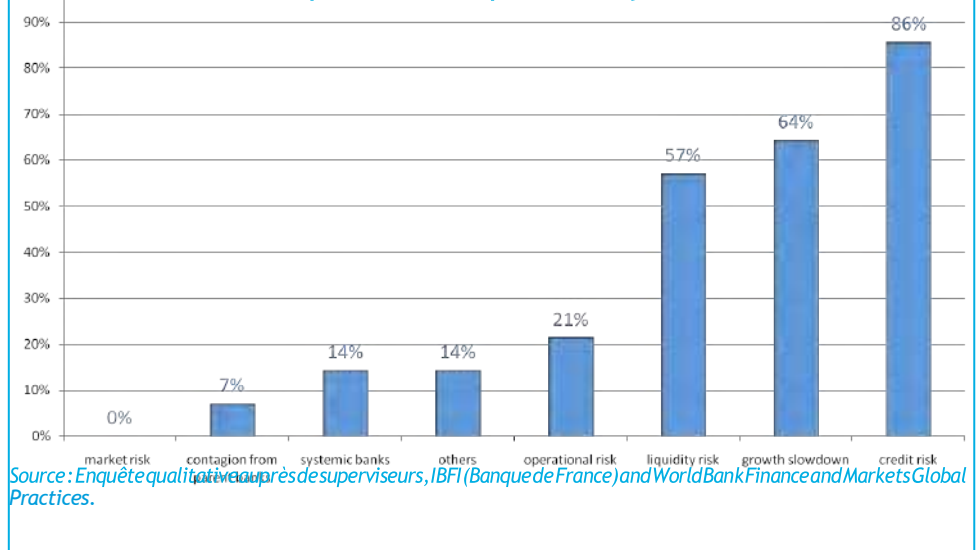
In other Mediterranean countries, central banks have also developed macroprudential supervisory arrangements to consolidate financial stability and manage the occurrence of systemic crises [15]. Morocco has the longest experience with the creation in 2006, during the revision of the law on credit institutions, of the coordination commission for financial sector supervisory bodies. This commission, chaired by the Governor of Bank Al-Maghrib, is responsible in particular for coordinating the actions of the supervisory bodies (Bank Al-Maghrib, the administration in charge of the supervision of insurance and reinsurance companies and the securities ethics council).

In January 2015, a new law on credit institutions was promulgated, which changed the name of the coordination committee into the coordination and supervision committee for systemic risk. This committee, which has been extended to the Ministry of Finance, is now responsible for macro-prudential supervision and systemic crisis management.

A recent survey on the operational frameworks of macro-prudential and financial stability arrangements set up by central banks in Mediterranean countries [16] shows,

that in terms of perceptions, 86% of central bank supervisors in the countries surveyed [17] believe that the implementation of macroprudential arrangements is motivated by credit risk management, and 21% by operational risk management [18], while other supervisors believe it is motivated by macroprudential risks related to cyclical hazards (64%), systemic liquidity risks (57%), risks of banks transforming into systemic entities (14%) [19] and other risks of systemic contagion (7%)

**Figure 3.13**  
**Comparative macroprudential systems in Euro med countries**



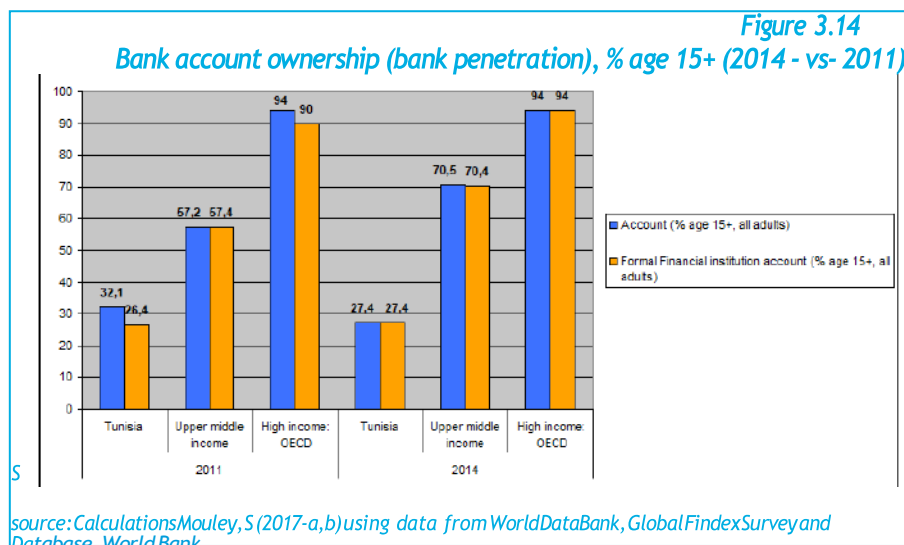
## II.2. Third challenge: A real commitment to the financial inclusion of SMEs

There are multiple barriers to Inclusive growth in Tunisia. Among others, access to finance is, major obstacle. The relaxation of this constraint by a financial inclusion policy is therefore crucial to combat economic exclusion, particularly in disadvantaged regions. Likewise, fighting against the weakness of financial inclusion in Tunisia and promoting more inclusive access to finance could also contribute to social inclusion. This is all the more important in a context marked by an unemployment rate of 15.3%, including 32% among young graduates.

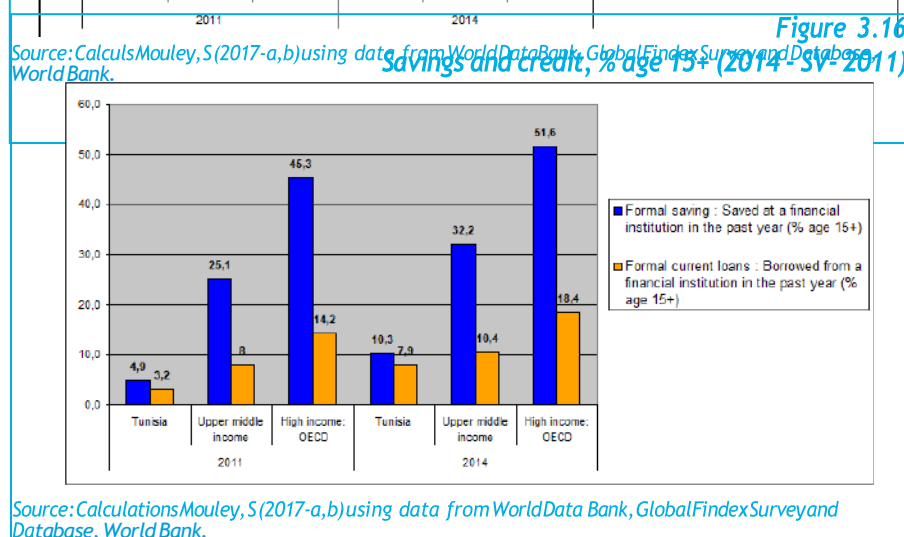
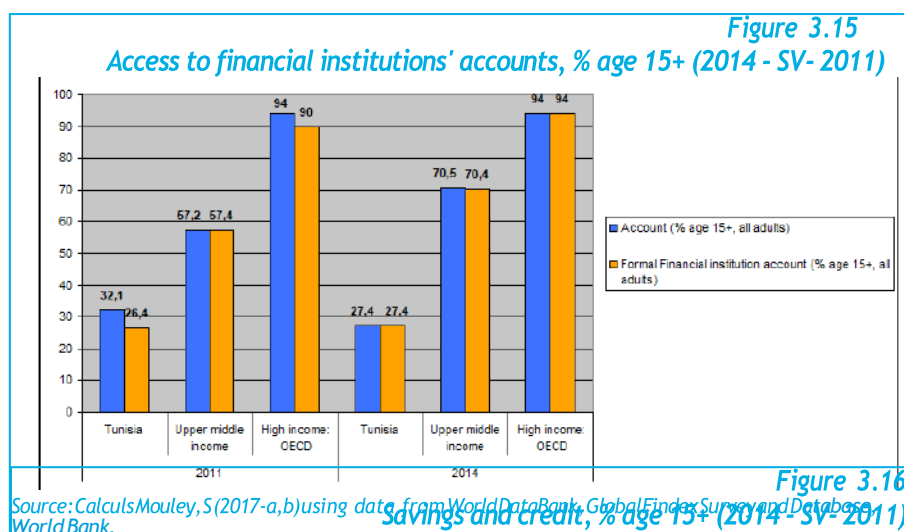
The comparative analysis of financial inclusion profiles is derived from the surveys of the World Bank's Global Findex platform.

The latest 2014 survey, published in 2015, refers jointly to the financial inclusion data book [20] and Global Financial Inclusion data (Findex) [21] which add to those of the previous 2011 survey [22]. It shows that in Tunisia, three quarters of the population over 15 years of age are suffer from financial exclusion. Indeed, in 2014, only 27.4% declared that they had an account in a formal institution (32.1% in the previous survey in 2011), compared to 70.5% in countries with the same income level (57.2% previously) and 94% in the advanced OECD economies. As a result, banking services fell by 4.7 points (Figure 3.14).

It is also important to note that the poorest 40% have the most trouble accessing formal financial services since only 17.2% have an account in a formal institution. Women, more than men, are also affected by this exclusion phenomenon since only 20.7% have an account in a formal institution compared to 34.3% for men. Difficulties in accessing savings products and loans are more acute in rural areas than in urban areas. In rural areas, only 22.4% of the population above the age of fifteen have an account in a



formal institution. Generally speaking, and in comparison with international standards, financial inclusion indicators for individuals in Tunisia are typically below international averages, in terms of penetration of bank accounts, access to financial institution accounts (Figure 3.15) and the holding of formal credit or savings accounts (Figure 3.16).



For this reason, Law N°2016-35 of 25 April 2016 approving the new statutes, prerogatives and organisation of the BCT, acted the creation of a financial inclusion observatory (OIF) to analyse, evaluate and monitor the conditions of access to sources of finance[23]. In particular, the OIF is responsible for:

“(i) the collection of data and information on access to and use of financial services and the establishment of a database for this purpose,



- (ii) monitoring the quality of services provided by institutions operating in the financial sector, particularly in terms of meeting customer needs,
- (iii) information and intelligence on financial services and products and their cost,
- (iv) the establishment of qualitative and quantitative indicators to measure the cost of financial services and their degree of customer satisfaction and financial inclusion,
- (v) the prescription of recommendations to institutions operating in the financial sector and to mediators,
- (vi) the review of the reports of banking mediators and the preparation of an annual report on banking mediation,
- (vii) the conduct of studies on financial services and their quality and the organization of sectoral consultations to this end,
- (viii) government assistance in the development of policies and programmes to promote the field of financial inclusion".

The creation of the observatory is part of a strategy to promote financial inclusion so that the financial sector can contribute to better economic and social inclusion of the population and promote the development of businesses that create value and employment.

Financial inclusion can be a major mechanism to promote economic growth and ensure a better future for the population, especially for low-income Tunisians. Tunisia offers opportunities for financial inclusion. Nevertheless, it still has to overcome structural and short-term obstacles

to increase the penetration of bank accounts, generalise retail access to banking and financial services, take advantage of and modernise the use of payment means and services and remove major obstacles to companies' access to sources of finance.

### Focus on comparator countries

Similarly to the BCT, the central banks of the Mediterranean comparator countries that were analysed are also aware of the significant scale of access to finance issues and, as such, have intensified their efforts to promote financial inclusion.

The last Findex survey in 2017 showed that Egypt and Morocco are still lagging behind in terms of financial inclusion (table 4) compared to the average of upper tier middle-income countries. The same is true for Jordan according to the 2014 surveys (Figure 3.17).

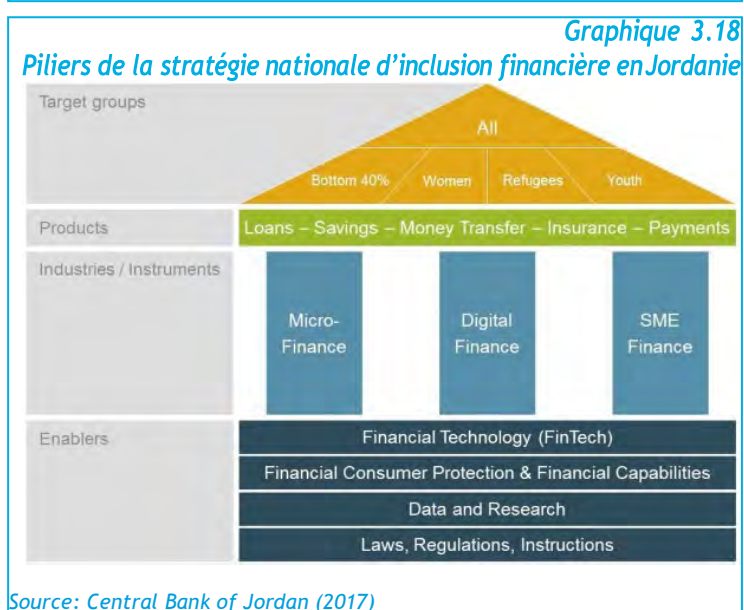
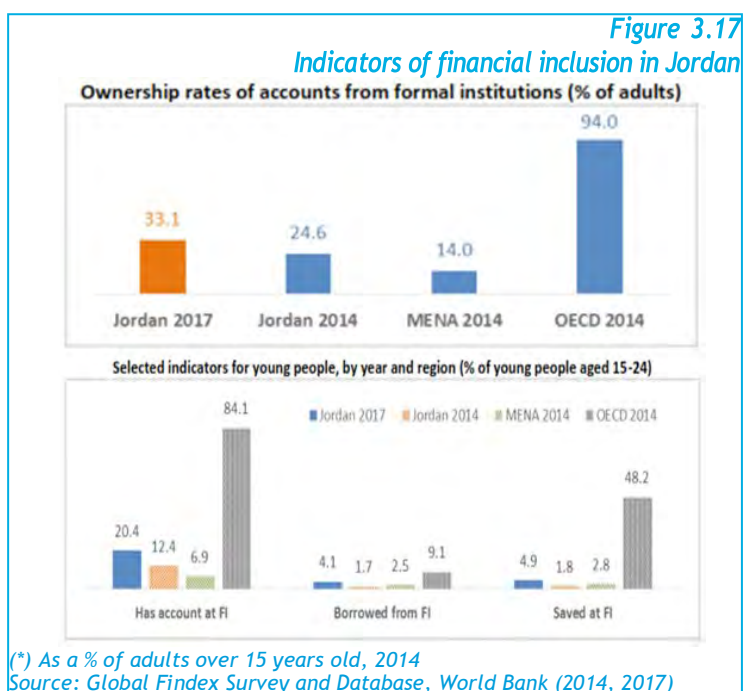
In this context, the Central Bank of Egypt (ECB) launched an initiative in early 2016 to encourage banks to reserve 20% of their loan portfolio for SMEs, with an interest rate that is not to exceed 5% per year. Egypt also launched a number of other initiatives

**Figure 3.4**

**Comparative financial inclusion indicators in Egypt and Morocco (\*)**

	Comparateurs pays		Comparateurs régionaux	
	Egypte	Maroc	Afrique du Nord	Tranche sup. des pays à revenus intermédiaires
Compte	32,8	28,6	34,7	73,1
Compte, femmes	27,0	16,8	26,0	69,3
Compte bancaire à accès numérique	1,3	1,2	3,8	30,0
Détention d'une carte de débit	24,8	21,1	25,4	58,8
Emprunt auprès d'une institution financière	6,3	2,6	5,4	9,9
Epargne auprès d'une institution financière	6,2	6,3	10,1	29,9

Source: Global Findex Survey and Database, World Bank (2017)



to promote financial inclusion, for example by improving the bankruptcy law.

In Morocco, a new mechanism for the inclusion of SMEs has been introduced by Bank El Maghrib to further support their access to bank financing. Thus, in 2012, it was decided to extend the collateral eligible for monetary policy operations to include private debt bills for V-SME through a new, longer-term refinancing instrument, "guaranteed loans". Due to

the persistence of a difficult economic situation and the continued deceleration of credit, a second support programme was set up at the end of 2013, which allows banks to have access, each year, to advances from Bank Al-Maghrib for an amount equal to the volume of loans (excluding real estate development and independent professions) they plan to grant to SMEs. They may also benefit from additional refinancing equivalent to the volume of credits granted to SMEs operating in the industrial sector or whose production is intended for export. These advances are granted quarterly for a period of one year. In the same vein, the Central Guarantee Fund (CGF) has facilitated access to financial services by guaranteeing VSEs, SMEs and low-income individuals.. The CGF guarantee thus benefited nearly 18,000 SMEs over the 2013-2018 period.

Finally, in Jordan, a new National Strategy for Financial Inclusion (SNIF) was put in place in 2018, whose pillars include: (i) microfinance, (ii) digital finance and access to finance for SMEs.

## **II.2. Fourth challenge: An international commitment to the implementation of structural reforms**

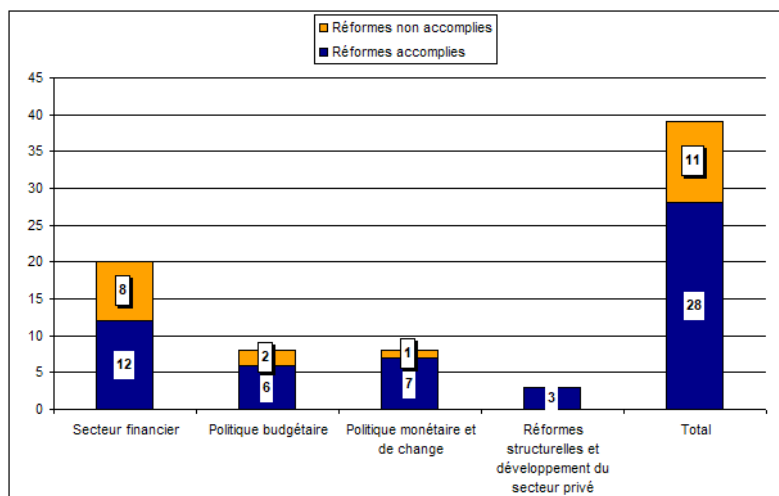
In June 2013, the BCT concluded a first Stand By Arrangement (SBA) with the International Monetary Fund (IMF) worth 2.7 billion dinars (\$1.75 billion), supported by a two-year program

for the implementation of structural reforms and the preservation of macroeconomic stability. The releases by tranche of this precautionary credit line were conditioned by the implementation of a reform package established according to a structural bench-mark agenda. The stand by agreement (SBA) covers 39 structural benchmarks for reform actions, spread over four strategic areas, 28 of which were generally achieved over the 2013-2014 period[24].

The BCT subsequently requested IMF support in May 2016 for an Extended Fund Facility (EFF) that plans to mobilise \$2.9 billion., backed by a four-year programme (2016-2020) whose main objective is to boost growth in order to create more jobs and reduce unemployment, pursue sound macroeconomic policies, further reduce the vulnerability of the economy to exogenous shocks and promote more inclusive development, especially since the regional security context remains fragile. This new extended credit facility program, along with the 2016-2020 five-year plan, forms a tool for tool for defining and prioritizing the reforms to be adopted for effective and efficient implementation. The MEC covers 18 structural benchmarks for reform actions, spread over four strategic areas, 7 of which were completed at the time of writing this chapter [25].

Figure 3.19

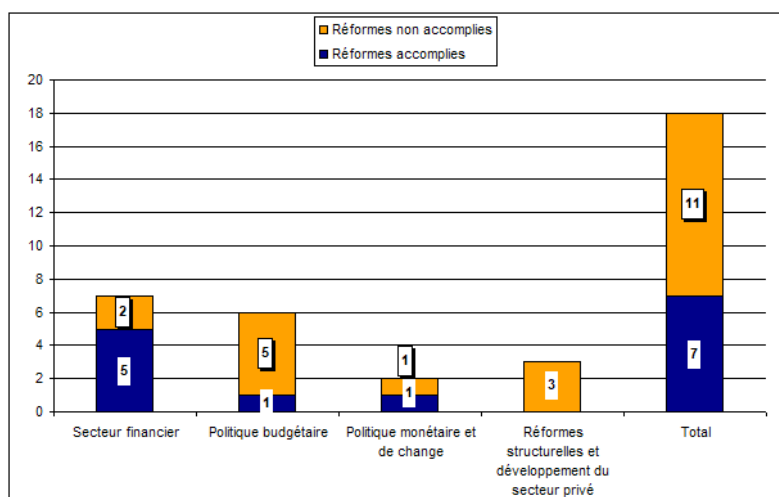
Performance of structural benchmarks within the SBA



Source: Compilation of the study

Figure 3.20

Performance of structural benchmarks within the MEC framework



Source: Compilation of the study

### Focus on comparator countries

The analysis of comparative cases from other Mediterranean countries shows that their central banks (Egypt, Jordan, Morocco) have also implemented similar structural reforms with the support of the IMF.

Thus, in the grip of a steep fall in its foreign exchange reserves and an abyssal budget deficit, Egypt benefited from support from multilateral institutions in the form of a three-year, \$21 billion loan. This was in the form of a package, which includes a loan of \$12 billion from the IMF, \$3 billion from the World Bank, \$1.5 billion from the African Development Bank (AfDB), and \$4.5 billion in the form of bond issues and bilateral agreements. The first tranche of the World Bank loan, amounting to US\$1 billion, was released in early September 2016 in the light of prerequisites met by the Egyptian government[26], while the conclusion with the IMF in November 2016 of an Extended Fund Facility (EFF) of US\$12 billion over three years was backed by a reform programme to:

(i) restore macroeconomic stability, (ii) support inclusive growth and job creation, (iii) modernise the functioning of the foreign exchange market[27], (iv) improve public finances and debt sustainability, (v) correct external imbalances and restore competitiveness, and (vi) strengthen social safety nets to protect the most vulnerable groups during the adjustment process.

Jordan concluded a three-year Stand-By Arrangement (SBA) in 2012, completed in 2015, of \$2.06 billion over three years, focusing on reducing external vulnerabilities and maintaining macroeconomic stability. This was followed in August 2016 by a

second three-year programme under the Extended Credit Facility (EFF) for an amount of \$723 million to implement an economic and financial reform programme focused on fiscal and public debt consolidation and improving the attractiveness of external capital.

In 2012, Morocco used an IMF Precautionary and Liquidity Line (PLL)[28] of \$6.21 billion over two years, which has been extended twice. A first time in 2014 for \$5 billion over two years, and a second time in July 2016 for \$3.47 billion backed by an additional two-year program to strengthen macroeconomic resilience and inclusion through growth.

### II.3. Fifth challenge : Exchange rate flexibility for greater private sector competitiveness and resilience to external shocks

In 2012, the BCT reformulated the operational framework for the Tunisian dinar exchange rate determination policy, with more flexible active exchange rate management, by calibrating the reference exchange rate on the basis of the average exchange rate on the interbank market and not on the basis of a fixed basket of currencies. In other words, the BCT would only intervene on the foreign exchange market through bilateral transactions when market quotations deviated substantially from the daily fixing, which led to a concrete reduction in the bid/ask margin from 1% to 0.2%.

This system has recently been abandoned, as it is conditional on the BCT disposing of sufficient foreign currency resources, which it did not have, to intervene regularly on the foreign exchange market in order to defend parity in the event of differences between interbank quotations and the fixed daily rate. Indeed, and in accordance with the agreements concluded with the IMF, whether under the previous stand-by programme or under the present extended credit facility agreement, a new exchange rate mechanism has been introduced. Since May 2013, it has consisted in depreciating the dinar in effective terms (euro-dollar basket) according to a mobile parity regime in a band of 2% on average per year,



as long as the national currency remains overvalued in real terms. This exchange rate flexibility was essentially motivated by the search for better price competitiveness of the exporting sectors and above all to ensure adaptability and strong resilience to external shocks.

According to updated estimates from the CGER (Consultative Group on Exchange Rate Issues)[29], used for international harmonisation purposes by the IMF, a real depreciation of the dinar was necessary to correct a relatively overvalued (or overestimated) real effective exchange rate compared to its various normal standard balances. Indeed, on the basis of these estimates, the real effective exchange rate of the dinar was overvalued:

(i) by 6.4% in 2016 (compared to 7% at the end of 2015)[30] compared to its standard fundamental balance (ii) by 9.1% in 2016 (compared to 5.2% in 2015) using the macroeconomic balance method on the data projected until 2021, (iii) by 13.1% in 2016 (compared to 13.2% in 2015) using the adjusted macroeconomic balance approach, and (iv) by 9.1% in 2016 (compared to 5% in 2015) using the external balance sustainability method based on the rebalancing or restoration to 2010 levels of the net external assets ratio to 14.4% of GDP

Nevertheless, the size of the current account

Figure 3.21  
Evolution of the current account deficit and other balance of payments balances

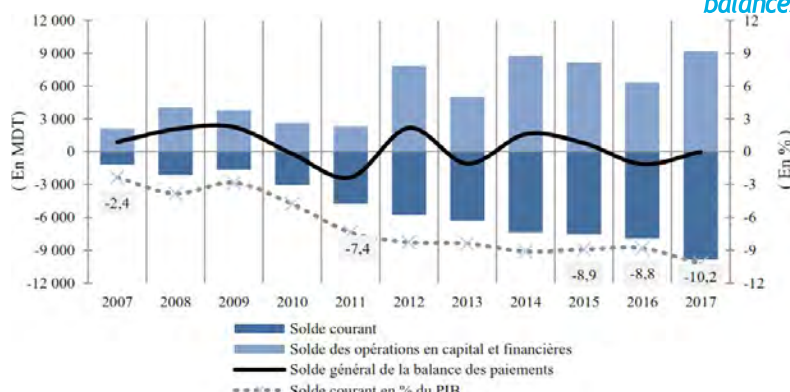
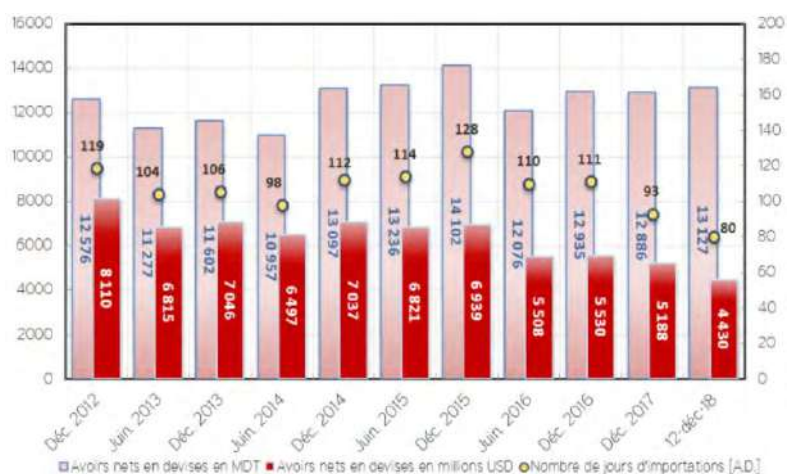


Figure 3.22  
Evolution of net foreign currency assets



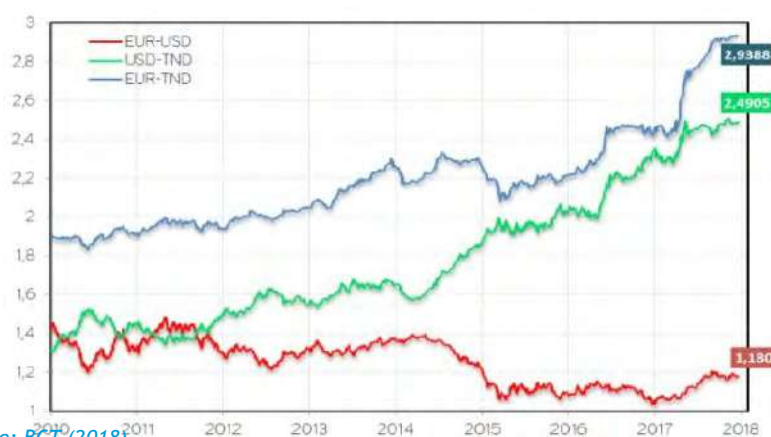
Source: BCT (2018)

deficit [31] and the persistence of external imbalances (Figure 3.21) have weighed heavily on foreign exchange reserves in Tunisia. Pressure on the foreign exchange market, due to a structural shortage of foreign exchange resources, has led to increased pressure on foreign exchange reserves (Chart 3.22), with a decline in the level of net foreign exchange assets to only \$4,430 million in December 2018 (80 import days) from \$8,110 million in December 2012 (119 import days).

This led to a rapid depreciation of the dinar and its decline against the euro and the dollar (Graph 3.23). In 2017 alone,



Figure 3.23  
Evolution of the exchange rate of the dinar



Source: BCT (2018)

the dinar exchange rate thus lost 17.3% and 6.1% of its value against the euro and the US dollar, respectively, movements that exacerbated the exchange risk for economic operators. The gradual depreciation of the exchange rate initially expected was unable to support the economy's price competitiveness, as the business of the main exporters was blocked due to the deterioration in security and to social and labour instability, and it actually led simply to a larger trade deficit as a result of higher prices for imported products.

It is for this reason, and in order to better equip operators with appropriate currency hedging instruments, that a new BCT circular for approved intermediaries N°2016-01 introduced reforms on hedging instruments and instituted a market-making mechanism (TDM) allowing certain banks to participate in currency auctions with the BCT and consequently hedge the operators' foreign currency exchange risks. These reforms came in addition to the range of instruments already in place, introduced between 2001 and 2007.

Indeed, as part of the strengthening of the liberalisation of foreign exchange market operations, approved intermediaries and

Tunisian economic operators were equipped with tools to manage exchange rate risks. With this aim, the BCT

Circular N°2001-11 of 4 May 2001, extended the possibility of using forward exchange rate hedging (forward contracts) for financial operations, to financial transactions, to authorise currency/dinar foreign exchange swap transactions and to allow banks and companies to hedge interest rate risks on currencies through Forward Rate Agreements (FRAs).

Since then, approved intermediaries have been allowed to act as counterparties in forward exchange transactions on behalf of their clients for foreign currency loans and borrowings, in addition to current transactions. To this end, they may forward quote currencies against the dinar for financial transactions with a maximum term of 12 months.

Consequently, in order to hedge against the exchange rate risk related to the repayment of their foreign currency borrowings, resident companies may forward purchase foreign currencies against dinars from resident or non-resident approved intermediaries for a maximum period of 12 months. In the same context, and to hedge against interest rate risk on foreign currencies, authorised intermediary residents may conclude FRA agreements with foreign correspondents for a maximum period of 12 months.

Nevertheless, international operators note that the forward currency purchase instrument only hedges the exchange risk relative to current purchases since the maturity cannot exceed 12 months; however, for capital

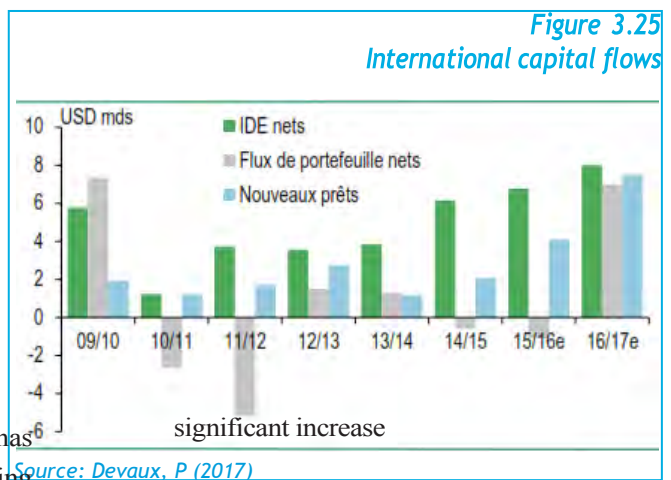
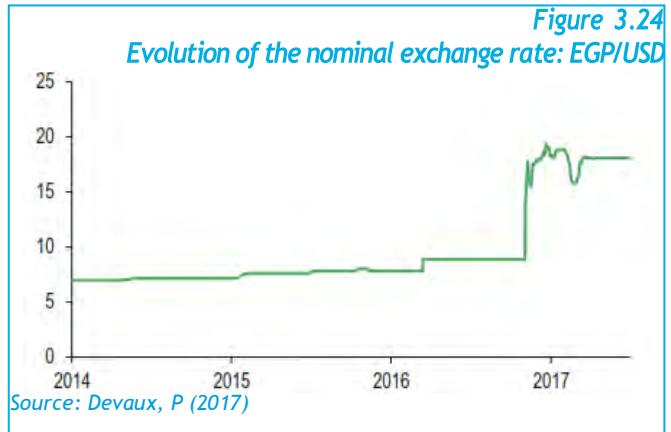
goods requirements and to hedge the exchange rate risk relating to repayments of loans denominated in foreign currencies, the only possible hedging is that offered by the Exchange Equalization Fund, managed by Tunis Ré.

It is for this purpose that the Circular to approved intermediaries No. 2001-11 of 4 May 2001 was amended by Circular BCT N°2007-27 of 18 December 2007 which extended currency hedging techniques to introduce currency/dinar exchange options on both commercial and financial transactions. The authorised currency options are similar to those in Europe, with maturities covered until the settlement date of the underlying commercial or financial transaction, without exceeding a maximum term of 3 years in any case.

#### Focus on comparator countries

Except in Jordan, where the central bank has consolidated the exchange rate fixing mechanism, Egypt and Morocco have begun the same experience as Tunisia in terms of exchange rate flexibility, with, however, different implementation conditions and consequences. While in Tunisia, the trend towards flexibility has been accompanied by certain distortions, in the form of a galloping depreciation of the dinar's exchange rates due to a lack of sufficient foreign exchange reserves to defend its parity, the floating of the Egyptian pound, which began in November 2016, ended several months of tension on the foreign exchange market, namely multiple restrictions on commercial (import freeze) and financial transactions (constraints on international banking transactions) and the development of a parallel foreign exchange market.

Although the immediate effect of the floating was a 50% depreciation of the Egyptian currency, it was carried out in conjunction with a



in interest rates and, especially, the financial support of the International Monetary Fund (IMF) following the conclusion, in November 2016, of a programme under the Extended Fund Facility (EFF)[32]. In addition to the funds disbursed by the IMF, there has been support from other multilateral donors (notably the World Bank) for about \$3 billion, as well as two bond issues on the international financial markets for an amount of 7 billion dollars.

The acceleration of the public finance reform programme subsequently restored confidence in economic policy and allowed a massive inflow of foreign exchange into the banking system. External capital flows have also been substantial: they are estimated at about \$27 billion over the last period. In addition, the high interest rates offered by the government on treasury bills and the renewe

confidence in the foreign exchange market attracted about \$10 billion in portfolio investments. Given the much more comfortable liquidity situation in foreign currencies, restrictions on foreign currency transactions were gradually lifted.

In Morocco, since 2015, the authorities have been transitioning from a managed floating exchange rate regime (linking the dirham to a basket of currencies reflecting the structure of foreign trade), a de facto intermediate exchange rate regime of fixed parity (limited to a euro-dollar basket), increasing the weightings of the euro to 80% and the dollar to 20%. The exchange rate fluctuation margins were  $\pm 0.3\%$  on either side of a central rate, calculated using the fixed historical reference rates of the euro and the dollar against the dirham. From 2017, Bank El Maghrib (BAM) began a project to move towards a more flexible exchange rate regime. The target exchange rate regime, where exchange rates against the dirham fluctuated within a narrow band of 0.6%, has been replaced by a new exchange rate regime where, in its early phases, the fluctuation band of the dirham was extended to  $(\pm 2.5\%)$  compared to the central rate fixed on the basis of a basket composed of 60% of the euro and 40% of the dollar.

This flexibility of the Dirham has been accompanied by risk hedging instruments against currency risks, with major changes introduced by the Office des Changes through the General Instruction on Foreign Exchange Operations (IGOC) in 2017 [33]:

(i) Thus, forward transactions in foreign currencies against dirhams or in foreign currencies against foreign currencies, carried out by authorised intermediaries, now cover terms freely negotiated between the parties, (ii) the characteristics of currency

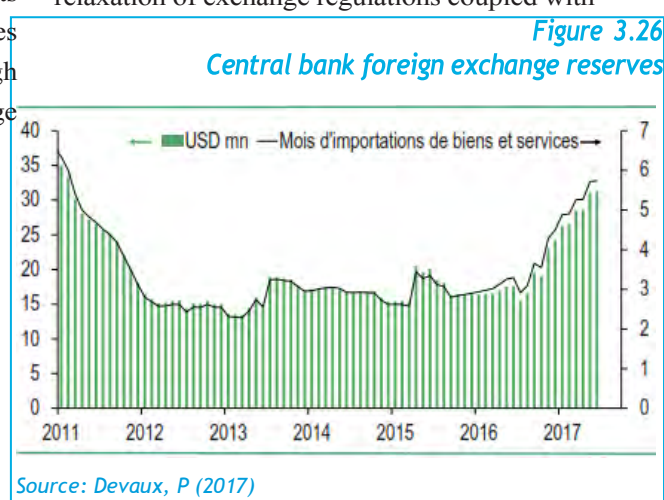
(ii) swap contracts against dirhams or currencies against currencies entered into by authorised intermediaries are also freely negotiated between the parties and must comply with the provisions laid down by the ISDA (International Swap and Derivatives Association),

(iii) the authorised currency options are the standard European vanilla options, the maximum maturity of which cannot exceed one year.

For greater ease and flexibility of hedging instruments, another IGOC was recently established in 2019, and introduced: (i) the possibility of offsetting receivables, (ii) the possibility of covering the depreciation of inventories and all types of risks (credit risk, risk inherent in any type of asset, insurance risk, etc).

#### II.4. Sixth challenge: The relaxation of exchange rate regulations to make foreign companies and international capital more attractive

Despite the measures already undertaken in the field of foreign exchange regulation in Tunisia, be this the loosening of exchange controls, the liberalisation of certain current transactions or several other measures inherent to capital account and financial transactions, initiated in particular since 1993 by the BCT, economic and financial operators, Tunisian and foreign, consider that the current regulations remain a major barrier within the business and investment environment. The relaxation of exchange regulations coupled with



the progressive liberalisation of capital movements, should contribute to the transformation and increased efficiency of the financial system. For Tunisia, in the current post-transition context, characterized by a shortage of national savings, a new gradual level of capital flow liberalisation might also be effective in mobilising external resources. Indeed, stable sources of financing for the current account deficit have declined, as foreign direct investment (FDI) now represents only 22.1% of total external financing, and more than half of this is concentrated in the energy sector alone [34].

Similarly, at the level of the balance of capital and financial transactions, portfolio investment income is significantly lower than that for FDI commitments. And this applies equally to share transactions for subscription by non-residents (Tunisian and foreigners) to capital increase operations of listed companies (or in the process of admission to the Tunisian Stock Exchange)), as well as those relative to subscriptions to private or public bonds (assimilable or transferable Treasury bills) and debt securitisation funds (FCC).

Nevertheless, despite the above findings, the monetary authorities, aware of the risks inherent to a disorderly liberalisation of capital flows, especially within the context of a difficult economic transition in Tunisia since 2011, have rightly adopted the same gradual and sequential approach to progressive liberalisation that had been followed previously.

#### **a. Regulatory stringency related to capital markets in Tunisia**

Capital markets in Tunisia play a marginal role. The government securities market remains

underdeveloped and illiquid while the primary market for corporate shares and bonds remains modest with listed companies that do not reflect the structure of the economy [35]. Regarding portfolio investment, the contribution of the stock exchange (BVMT) to the financing of the economy and investment remains marginal, compared to countries with the same level of development [36]. The Tunisian stock market is small and is not representative of the national economy. Similarly, the market's financial contribution to the economy is weak (an average of only 5% of GDP). In terms of market capitalisation, the position of the Tunisian stock exchange, relative to other emerging markets, shows a lack of depth.

At the same time, the financial market is not very attractive to foreign investment in equity and bond portfolios, due to exchange control for foreign investors that remains excessive in the main and alternative markets for equity securities on the stock exchange listing. Indeed, the current exchange regulations on the main and alternative markets for equity securities on the stock exchange list only provide for measures to loosen exchange control for foreign investors. Since 1997, portfolio investments in shares with voting rights are no longer subject to approval by the former Higher Investment Commission, but have only been liberalised by up to 50% for listed companies.

In Morocco or Egypt, however, foreign investors may hold up to 100% of the capital of listed companies with no other restrictions on sectoral choices. [37]. Since 2005, the following measures have been implemented: (i) freedom of acquisition between foreigners of shares in Tunisian companies, (ii) full convertibility

the Tunisian dinar for capital transactions carried out regularly by non-residents, provided that they make investments in Tunisia by importing foreign currency [38] and (iii) the full liberalisation of underlying transactions (including SICAVs) and portfolio investments in the form of equity investments in non-financial sectors. However, these measures have, so far, been insufficient to boost the market due to the restrictions on access rights, which are still considered to be insufficient by 50% compared to other emerging markets, which also explains the low foreign participation in market capitalisation, which has averaged 21.7% in recent years compared to that of the comparator and emerging countries [39].

#### **b. Economic operators' views on the major obstacles to foreign exchange regulation**

The perception of economic operators regarding major obstacles to foreign exchange regulation have revealed the following provisions to be the most problematic, detailed below according to main categories [40].

#### **Financial operations backed by current transactions with foreign countries**

Many measures have been put forward that could complete the full liberalisation of current transactions with foreign countries, and these can be used as the foundation of a roadmap towards a broader liberalisation plan:

- A consolidation of foreign currency accounts due to the highly heterogeneous, and sometimes ambiguous, nature of the accumulation of different accounts (AVA, tourist allowance, professional account, service provider account and all other accounts);
- Simplify and popularize the procedure for granting Business Travel Allowances (BTAs) for new promoters;
- The possibility of having foreign currency

accounts for individuals receiving dividends, in proportion to their export earnings;

- The possibility of using these funds for financial operations or investment abroad;
- The derogation process relative to the validity of F1 authorisations issued by the BCT would benefit from a more flexible revision;
- Facilitation of the use of BCT F2 forms, especially in the context of foreign markets;
- Review the corresponding circular to support foreign currency accounts if payments are made in another currency;
- Facilitate the establishment abroad of Tunisian SMEs that wish to develop their markets as well as the financing of offshore companies (through specific credit lines) ;
- Easing of the regulations on the financing of offshore companies in Tunisia and foreign investments in order to optimize the attractiveness of FDI.

#### **Financial or capital transactions with foreign countries: in terms of foreign investment**

In addition to the reform of the investment code to remove the restriction on the acquisition by foreigners of majority shares in existing companies, a relaxation of exchange rate regulations is also likely to remove other major obstacles to foreign investment:

- Even though offshore companies enjoy freedom of repatriation, this requires the authorisation of the BCT, with more or less long delays;
- Despite a certain amount of easing, the conditions for access to SME capital by non-residents are still very restricted. However, since 2005, exchange regulations have provided for the freedom of foreigners to acquire shares in Tunisian companies. ;

Financial or capital transactions with



foreign countries: regarding the attractiveness of the stock exchange and the bond market

It would appear that it is increasingly counterproductive to maintain restrictions on foreign capital. Acting upon foreign demand would provide significant financial leverage. To increase Tunisia's attractiveness to foreign investors, the following options could be implemented as a matter of priority:

- Further liberalisation of equity portfolio flows, from 50% currently to 70%, for foreign institutional investors;
- Development of the bond market by increasing the authorised limits on subscriptions by foreign investors (non-resident natural or legal persons of foreign nationality) in bond portfolio flows; the aim here, for the outstanding amounts relating to each issue line, would be to extend beyond the current 20% [41], the basis for the rate at which non-resident foreigners are allowed to subscribe to public debt securities (fungible Treasury Bonds (BTAs) issued by the State, Treasury bonds or bonds issued by resident companies listed on the stock exchange or with a rating ;
- Gradual liberalisation (extension of maximums) of trade and financial credits contracted abroad by credit institutions and other resident companies.

#### **The role of foreign investment funds and the depth of capital markets**

Exchange regulations are not very favourable to the registration of venture capital funds offshore. Therefore, a gradual liberalisation plan in this area could include the following two steps [42] :

- The short-term objective would be to establish a specific framework for offshore venture capital funds. This framework could include flexible conditions for how they operate

and, in particular, in terms of flexibility in the use of resources and the return of capital. Especially since the implementation of the texts relating to the code of provision of financial services to non-residents (provided for by Law No. 2009-64 of 12 August 2009) will open up the venture insurance, investment and management activities of investment funds and venture capital (private equity) non-resident investment service providers operating as legal persons.

- The medium-term objective would then be to authorise portfolio investments in Tunisia, limited, in a transitional stage, to foreign institutional investors, in accordance with the terms of the Code for the Provision of Financial Services to Non-Residents and, also, to make the terms of portfolio investment by non-residents in Tunisian debt securities more flexible. In the long term, the objective would be, within the framework of full convertibility of the dinar, to provide for the liberalisation of portfolio investments abroad as well as bank loans to non-residents.

It is for this reason that the BCT has proposed a series of measures to ease exchange rate regulation [43], in terms of capital and financial transactions, whether they involve:

(i) investments made in Tunisia by non-resident foreigners, (ii) investments made abroad by residents, (iii) subscriptions for debt securities issued on the domestic market, (iv) external borrowing, (v) the organisation of the money market in foreign currencies and local credits [44].

### **III. Conclusion**

Central banks in Mediterranean countries play a major role in private sector reforms and can effectively contribute to improving the business climate and

attractiveness to foreign investment. The focus in this chapter on recent actions carried out by the Central Bank of Tunisia (BCT), in comparison with the central banks of other Mediterranean countries (Egypt, Jordan, Morocco), has highlighted six main converging reform channels, the effects of which can be rapid and controllable (quick wins) :

- (i) the first channel is inherent to the modulations of operational frameworks for the conduct of monetary policies to ensure better support from the banking sector for the financing of private sector investments,
- (ii) the second channel is part of the pursuit of financial stability to ensure that the private sector has an environment that is conducive to doing business,
- (iii) the third channel concerns the monetary authorities' real commitment to the financial inclusion of SMEs,
- (iv) the fourth channel also concerns the international commitment of central banks to the implementation of structural reforms,
- (v) the fifth channel concerns exchange rate flexibility for better private sector competitiveness and resilience to external shocks. The mixed effects of this channel for the central banks analysed are essentially due to the varying degrees of success achieved for certain prerequisites, such as the robustness of financial systems, the sustainability of macroeconomic fundamentals, the sustainability of foreign exchange reserves and, above all, the international support of the main donors. All these are preconditions that must precede the use of currency floating,
- (vi) Finally, the sixth channel concerns the relaxation of exchange rate regulations to optimise attractiveness to foreign companies and international capital. On this last point, converging findings emerge from the strategies pursued by central banks. Aware of the risks inherent to a disorderly liberalisation of capital

movements, the latter have quite rightly adopted a sequential approach to the progressive liberalisation of capital and financial operations, which can be effective in mobilising the external resources needed to finance the reforms to be undertaken. But the expected benefits of this external financial liberalisation will not be automatic. They will be determined by the level of financial development, the stability and resilience of the macroeconomic framework and the quality of institutions. This requires a pragmatic and gradual approach to relaxing exchange rate regulations.

## Notes

1. Cumulative monetary policy operations reached more than 6% of GDP from January 2011 to July 2012.
2. First in June 2011 from 4.5% to 4%, then again in September 2011 bringing it down to 3.5%..
3. It should be noted that at the time of finalising this chapter, the BCT raised its key interest rate by 100 basis points again in February 2019 to 7.75%.
4. cf. *Infra*;
5. cf. *Appendice.1*.
6. From the second half of 2008 until now.
7. From the first half of 2000 to the first half of 2008.
8. The methods for calculating the TEG and TEM are set by Decree No. 2000-462 of 21 February 2000. For each category of loans granted, a half-yearly TEG is actuarially determined by the BCT, taking into account, in addition to interest, fees, commissions or remunerations of any kind, direct or indirect, involved in the granting of loans. The half-yearly TEM is determined by the simple arithmetic average of the TEGs observed during the same half-year and used during the following half-year to determine the excessive interest rate.
9. cf. Devaux, P(2017)

10. cf. *Infra*.

11. In particular, with the creation of the national deposit guarantee fund, monetary authorities will have an institutionalised security mechanism, in the form of a deposit guarantee and insurance scheme in the event of a systemic crisis, in order to limit the effects of moral hazard. The purpose of this fund is to strengthen depositor protection and preserve public confidence in the banking system. In particular, it makes it possible to avoid massive withdrawals by depositors (bank runs) in the event of proven or unproven difficulties for certain banking institutions. But the deposit guarantee scheme is not an effective instrument for preventing banking crises in countries that may experience both banking difficulties and a public debt crisis because the countries in difficulty cannot, therefore, mobilise sufficient funds (recent cases of Greece and Spain).

12. In addition to the resolution mechanism, there was also talk of creating an asset management company (AMC), which is a form of "bad bank" or public debt buyback vehicle. The mission of this company would be to examine the various methods of restructuring non-performing loans, to which so-called non-performing loans from the banking sector would be transferred, in order to ensure the restructuring of the balance sheets of banks, in particular public banks, and to ensure the restructuring of struggling but viable economic entities. For example, there was talk of absorbing the debts of the tourism sector in exchange for government-guaranteed bonds. The tourism sector has seen a particular increase in the share of unpaid or disputed loans. For the banking system as a whole, the share of unpaid (and disputed) debts in the sector's commitments has risen from 18.8% in 2010 to more than 27.3% currently, within the total unproductive debts of the banking system. In addition, non-performing loans in the

tourism sector alone represent 40% of the loan portfolio.

13. Repealing Act No. 2006-26 of 15 May 2006 and Act No. 2007-69 of 27 December 2007.

14. Amending the former Banking Act No. 2001-65 of 10 July 2001 on credit institutions, and all subsequent texts that amended or supplemented it.

15. cf. Prasad. A, Abdel Monem. H and Garia Martinez. P (2016), *Macroprudential Policy and Financial Stability in the Arab Region*, IMF Working Paper WP-16/98, IMF, May.

16. cf. Quemard, J.L (2015), *Articulation between micro and macro prudential frameworks in the euro-Mediterranean jurisdiction*, IBFI (Banque de France) and World Bank - Finance and Markets Global Practices.

17. The survey covered the following 15 Mediterranean countries: Albania, Algeria, Croatia, Egypt, France, Greece, Italy, Jordan, Lebanon, Montenegro, Morocco, Malta, Palestine, Slovenia, Tunisia.

18. This also reflects the importance of managing banks' conventional micro-prudential risks and compliance requirements with the Basel rules. III.

19. cf. Mouley, S (2016).

20. cf. World Bank (2015), *The little data book on financial inclusion: From global financial inclusion database*.

21. cf. Demircuc-Kunt, Asli, Leora Klapper, Dorothée Singer, and Peter Van Oudheusden (2015), *The Global Findex Database 2014: Measuring Financial Inclusion around the World*, Policy Research Working Paper 7255, World Bank, Washington, DC.

22. cf. Asli Demircuc-Kunt and Leora Klapper (2013), *Global Findex data: Measuring Financial Inclusion - Explaining Variation in Use of Financial Services across and within Countries*, Brookings Papers on Economic Activity, Spring.

23. The Observatory of Banking Services (OSB), previously created within the BCT pursuant to Decree No. 2006-1879 dated July 10, 2006, has been replaced by a Financial Inclusion Observatory (OIF).

24. cf. Appendice.2.
25. cf. Appendice.3.
26. These correspond to future measures to reduce the public sector wage bill from 8.2% to 7.3% of GDP between 2015 and 2019, a reduction in energy subsidies beyond 3.3% of GDP by 2019, (via the five-year "energy price reform" plan), a decrease in the State's participation in the electricity sector from 92% to 85% between 2016 and 2019 and a total liberalisation of the gas sector, with the end of the monopoly on electricity and gas infrastructure, the introduction of anti-trust legislation, the strengthening of investor rights, the licensing of new competitors in the energy sector, and finally an income tax reform. But the main condition is the introduction of VAT.
27. The liberalisation of the exchange rate regime and the devaluation of the Egyptian pound were crucial steps in restoring confidence in the economy and eliminating currency shortages. The new exchange rate regime has been supported by a cautiously restrictive monetary policy aimed at anchoring inflationary expectations, at containing domestic and external demand pressures and allowing the accumulation of foreign exchange reserves.
28. The global financial crisis has highlighted the need for effective global financial security arrangements to help countries overcome the shocks they face. One of the main objectives of the recent reform of IMF lending instruments was thus to ensure that the institution, which has a traditional crisis resolution role, also has more effective tools to prevent crises. The Precautionary and Liquidity Line (PLL) is designed to provide a flexible response to the liquidity needs of member countries with fundamentally strong economies that remain exposed to external vulnerabilities and shocks preventing them from using the flexible credit line (FCL). To date, two countries, the former Yugoslav Republic of Macedonia and Morocco, have used the PLL.
29. Or methodology of the GCTC (Consultative Group on Exchange Rates) applied to a panel of advanced but also emerging economies. Tunisia has been included in the sample used by the GCTC since 2007.
30. As a result of the concomitant deterioration in productivity and other fundamentals (inflation, net foreign assets and terms of trade, in particular).
31. The current account balance deteriorated further (-10.2% of GDP in 2017 against only -2.4% in 2007 (see Mouley, S 2017).
32. cf. Supra.
33. This is in comparison with the most recent reforms of 2007, and particularly the most recent IGOC of 2013 on spot and forward exchange markets and financial risk hedging operations.
34. FDI currently contributes only 12.4% to GFCF.
35. cf. Mouley, S (2014-a, 2014-b)
36. cf. Mouley, S (2013).
37. In Tunisia, some sectors remain closed to foreign participation such as: distribution, real estate and the financial sector (unless authorised by the BCT).). Foreign participation in the automotive sector, for example, is capped at 30%.
38. In this context, these operators enjoy the freedom to transfer the real net proceeds of the sale or liquidation of the invested capital even if this proceeds is higher than the capital initially invested.
39. Although low compared to other emerging financial markets, foreign participation in market capitalisation is only 2.5% on average, which has protected the BVMT from destabilising risks related to the volatility of foreign capital flows..
40. cf. Mouley, S (2016-b).

41. BCT Circular to approved intermediaries No. 2007-10 of 17 April 2007.
  42. cf. Mouley (2015).
  43. These measures are based on a matrix proposed by the BCT (cf. Mouley, S (2016-b)).
  44. cf. Appendice.4.
  45. As defined by Circular to Credit Institutions No. 91-24 of 17 December 1991 on the division, hedging of risks and monitoring of commitments, which stipulates that banks are required to report monthly to the BCT a ratio between realisable assets and liabilities payable that must be at least 100% and must be respected at all times.
  46. As provided for in the former Circular to Credit Institutions No. 1991-24 of 17 December 1991 on standards for division, risk coverage and monitoring of commitments.
  47. It should be noted that the assets of public banks may include commitments from public companies in financial difficulty, and not covered by the implicit guarantee of the State.
  48. In particular, the circular laid down the standards to be adopted by banks for the classification of receivables according to the risks incurred and the minimum rules for setting up the related provisions..
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## **Appendices**

### **Appendix 1 : Tunisia - Modernisation of micro-prudential supervision for effective banking risk control**

#### **Developments in terms of liquidity risk management**

A BCT circular No. 2014-14 introduced a new Liquidity Coverage Ratio (LCR) based on the Basel 3 criteria. The former liquidity ratio[45] was abandoned in November 2014 and replaced by the new ratio mentioned above, as from January 2015. This new ratio is defined as the coverage rate of net cash outflows by the outstanding amount of high quality liquid assets over a 30-day period in a situation of liquidity stress (i.e. excluding the refinancing of the BCT). It must be at least 60%. A stress test conducted by the BCT shows that the new liquidity ratio, despite its new requirements and constraints, has been respected by 18 banks out of 22. Similarly, a new long-term structural liquidity ratio (NSFR: Net Stable Funding Ratio) is being studied for future implementation in order to better control the transformation activity (short-term loans to finance long-term positions), while guaranteeing financing based on a minimum amount of stable liabilities.

#### **Developments regarding prudential capital requirements**

Shareholders' equity consists of core shareholders' equity (Tiers 1) and additional shareholders' equity, the amount of which is limited to half of the core shareholders' equity. Credit institutions are required to comply at all times with a solvency ratio, which has been increased to a minimum of 10% from the end of 2014, compared to 9% from the end of 2013 and 8% previously. In addition, net core capital may not be permanently less than 7% of the risks incurred from the end of 2014, compared with 6% previously. But, apart from these notions of regulatory capital, banks do not yet have any control over the concept of economic capital, i.e. the additional part of equity used to cover abnormal, exogenous and exceptional risks.

To address this deficiency, in June 2018 the BCT introduced a new circular N°2018-06 to banks and financial institutions on the reform of capital adequacy standards, which requires reporting institutions to have clear, effective and comprehensive strategies and processes in place to assess and maintain on an ongoing basis the level and quality of internal capital that they consider appropriate to cover the risks to which they are or could be exposed. Under this circular, the solvency ratio has introduced operational and market risks in addition to credit risk.

#### **Developments in terms of risk concentration and division**

A BCT circular N°2013-21 of 30 December 2013 introduced more tighter conditions for concentration and risk division [46]. Thus, from the end of 2013, the total amount of risks incurred must not exceed: (i) 3 times the credit institution's net equity, for beneficiaries whose risks amount, individually, to 5% or more of the said net equity (compared with 5 times the net equity previously) and, (ii) 1.5 times the credit institution's net equity, for beneficiaries whose

risks amount, individually, to 15% or more of the said net equity (compared to twice the net equity previously).

In addition, the total amount of risks incurred on persons related to the credit institution (related parties) according to the definition of Article 23 of Banking Act No 2001-65 of 10 July 2001 on credit institutions, may not exceed one time the credit institution's net equity. The risks incurred for the same beneficiary may not exceed 25% of the bank's net equity. Circular No. 2013- also required the implementation of a rule, at the end of 2013, according to which any excess in relation to one of the risk concentration and division standards must be added with a weighting of 300% to the total risks incurred used to calculate the solvency ratio. This implementation has led to a decrease in the solvency ratio for some public banks. Most of the overruns concern commitments of more than 25% for certain public companies[47] or for certain business sectors.

### **Developments in terms of classification and provisioning requirements for receivables**

Circular No. 2012-02 of 11 January 2012, amending circular No. 1991-24 of 17 December 1991[48], introduced new collective provisioning rules to cover latent risks on current liabilities (asset class 0) and liabilities requiring special monitoring (asset class 1). Note 2012-08 of 2 March 2012 to credit institutions recommended a specific methodology for assessing the liabilities to be provisioned based on an estimate of a possible migration risk rate from classes 0 and 1 to class 2. These collective provisions are only determined for commitments exceeding 50,000 TD in classes 0 and 1 at the closing date of the financial year.

In order to restructure the banking sector through the strengthening of equity capital and better risk coverage, the latest circular No. 2013-21 of 30 December 2013 amending circular 91-24 introduced new additional provisioning rules with a view to achieving a better balance between financial performance and adequate risk coverage. Two new articles have been added to Circular No. 91-24 of 17 December 1991, obliging credit institutions to make additional provisions precisely for asset class 4, which is more than three years old. Indeed, credit institutions must set up, as from the closing of the accounts on 31/12/2013, additional provisions on assets with a maturity in class 4 of 3 years or more to cover the net risk, in accordance with the following minimum percentages:

- 40% for assets with a maturity in class 4 of 3 to 5 years;
- 70% for assets with a maturity in class of 6 and 7 ans ;
- 100% for assets with a maturity in class 4 above or equal to 8 years.

The latest circular No. 2013-21 of 30 December 2013 introduced new rules for additional provisioning by adding two new articles to circular No. 1991-24 of 17 December 1991, requiring credit institutions to make additional provisioning at the level of asset class 4 whose maturity exceeds 3 years. This measure, which aims to restructure the banking sector through the strengthening of equity capital and better risk coverage, would allow a better balance between financial performance and adequate risk coverage.

Appendix 2 : Matrix of structural reform benchmarks of the Stand-By agreement (Tunisia)		
Areas and reform initiatives	Objectives	Reform actions; SBA structural benchmarks (2013-2015)
1. Financial sector	1.1. Stability of the financial sector	1.1.1. New architecture of the bank reporting system, for accounting, financial and institutional functions
		1.1.2. Adoption by the Council of Ministers of a strategic vision of State intervention in the financial sector based on the results of the full audit of banks public
		1.1.3. Generalization of on-site inspection for one bank and credit risk inspection of four other banks
		1.1.4. Completion of the joint IMF-WB financial system stability assessment programme for the detailed assessment of compliance with the Basel Core Principles for Effective Banking Supervision
		1.1.5. Review by the Board of Directors of the Central Bank of Tunisia (BCT) of the results of an impact study on banks of changes in the ratios of liquidity in line with changes in international standards
		1.1.6 Drafting of a new law on the statutes of the BCT in line with international best practices
		1.1.7. Development and implementation of a new reporting and classification system for bank receivables
		1.1.8. Full audit of public banks (BH, BNA and STB)
		1.1.9. Adoption of the restructuring plan for BH
		1.1.10. Adoption of the restructuring plan for BNA
		1.1.11. Adoption of the restructuring plan for STB
		Adoption of recapitalisation plans for public banks (BH and STB)
		1.1.13. Adoption of the BNA recapitalisation plan
		1.1.14. Mechanism for the separate resolution of unproductive receivables and creation of an asset management company (APG): Asset Management Company (AMC)
		1.1.15. Doubling the number of supervisors at DGSB - BCT
		1.1.16. Compliance of banks (including public banks) with a minimum solvency ratio (10%)
		1.1.17 New procedure for appointing directors representing the State and public participants in the boards of directors of public banks (BH, BNA and STB)
		1.1.18. Approval by the boards of directors of the three public banks (BH, BNA, STB) of performance contracts (programme contracts) in accordance with their restructuring plans
	1.2. Systemic crisis management	1.2.1. Adoption by the ARP of a new banking law (including a banking resolution mechanism) in line with international best practices
		1.2.2. Development by the BCT of the regulatory framework for a lender of last resort facility (PDR)

2. Budgetary policy	2.1. Simplification and reduction of tax distortions	Adoption by the Council of Ministers of a corporate tax reform for the convergence of tax scales and rates between the on-shore and off-shore sectors: reduction of on-shore corporate tax from 30% to 25% and taxation of offshore companies at the rate of 10% income tax
		2.1.2. Adoption of an agenda (schedule) for full convergence of the taxation regimes of the on-shore and off-shore sectors
		2.1.3. Elaboration of a new tax code covering a reform of direct and indirect taxes
	2.2. Reduction of energy subsidies	2.2.1. Approval of an automatic fuel price adjustment formula as part of a reform to abolish the generalisation of energy subsidies
	2.3. Tax equity and protection of the most vulnerable segments of the population	2.3.1. Reform of grant targeting procedures
	2.4. Better management of public finances	2.4.1. Tax Administration Modernization Plan
		2.4.2. Unification of the treasury's current accounts into a single account
	2.5. Better monitoring of budgetary risks	2.5.1. Preparation of a consolidated balance sheet of the 20 main public companies



3. Monetary and exchange rate policy	3.1. Strengthening monetary policy transmission mechanism	3.1.1. Publication of a circular by the BCT concerning the guarantee discount on loans used as collateral eligible for refinancing operations
		3.1.2. Approval of a minimum threshold of 25% of the guarantee discount on loans used as collateral eligible for refinancing operations
		3.1.3. A minimum proportion of treasury securities of 10% of the refinancing volume due as collateral
		3.1.4. A minimum proportion of treasury securities of 20% of the refinancing volume due as collateral
		3.1.5. Review of the results of an impact study on the capping of excessive interest rates
		3.1.6. A minimum proportion of treasury securities of 40% of the refinancing volume due as collateral (2015)
	3.2. Exchange rate flexibility	3.2.1. Establishment of an electronic interbank platform for foreign exchange transactions and approval of an agreement for market makers
		3.2.2. Weekly foreign exchange auction system
4. Structural reforms and private sector development	4.1. Promoting inclusive growth and job creation	4.1.1. Adoption of a new investment code (protection of market access conditions, reduction of investment restrictions, rationalisation of incentives and review of tax and financial benefits)
	4.2. Promoting good governance	4.2.1. Adoption of a competition law
		4.2.2. Adoption of a law on public-private partnership (PPPs)
Source: IMF and Tunisian authorities (2017)		

Appendix 3: Structural reform benchmarks for the extended credit facility (Tunisia)		
Areas and reform initiatives	Objectives	Reform actions: Prerequisites and structural benchmarks MEC (2016- 2016-) 2020)
1. Financial sector	Prerequisites	
	1.1. Stability of the financial sector	1.1.1. Approval by the boards of directors of the three public banks (BH, BNA, STB) of their updated business plans
		1.1.2. Approval by the boards of directors of the three public banks (BH, BNA, STB) of their performance contracts (programme contracts) in accordance with their new restructuring plans
		1.1.3. Adoption by the ARP of the BCT Act, the Banking Act and the Bankruptcy (Bankruptcy) Act in accordance with standards and good practices international practices (best practices)
	1.2. Modernisation of the monetary and exchange rate regime	1.2.1. Approval of the secondary legislation of the Banking Act, with regard to the banking resolution system, through: (i) the adoption of a decree on the implementation of the National Guarantee Fund (NGF) for bank deposits based on the principle of the lowest cost of resolutions, with an exception for systemic cases, and (ii) the adoption of a resolution by the regulation council providing for a short deadline for determining resolution measures for banks and systemic entities
		1.2.2. Operational implementation by the BCT of a lender of last resort facility (PDR)
	Structural benchmarks	
	1.3. Stability of the financial sector	1.3.1. Systematic implementation by the BCT of the risk-based banking supervision manual
		1.3.2. Inspection of the seven largest private banks to the highest standards
2. Monetary and exchange rate policy	2.1. Strengthening monetary policy transmission mechanisms	2.1.1. Excessive interest rate raised from 20% to at least its 2009 level (33%)
	2.2. Flexibility of exchange rates	2.2.1. Measures to ease exchange regulations
3. Fiscal policy and public institutions	3.1. Fiscal equity	Adoption by the Council of Ministers of the tax reform strategy, in line with the principles of equity and efficiency established with IMF staff
		3.1.2. Adoption of the Budget Organization Act based on objective-based management (GPO - GBPO)
		3.1.3. Establishment of the Large Companies Department including formal responsibility for the main tax law enforcement functions (management, service, and control).
	3.2. Improved monitoring of budgetary risks	3.2.1. Signing of performance contracts with the five largest public companies

	3.3. Fiscal sustainability and quality of public services	3.3.1. Completion of the functional review of four ministries (Health, Education, Finance and Equipment)
	3.4. Sustainability of public debt and the development of capital markets	3.4.1. Adoption of a medium-term public debt strategy
4. Structural reforms and private sector development	4.1. Promotion of inclusive growth and job creation	4.1.1. Adoption of decrees implementing the new Competition Act, the PPP Act and the new Investment Code
	4.2. Promotion of good governance	4.2.1. Establishment of an independent high level body for good governance and the fight against corruption and malpractice
	4.3. Social protection and security fund reforms	4.3.1. Completion of the establishment of a database on needy and low-income families
Source: IMF and Tunisian authorities (2017)		

## **Appendix 4: Synopsis of the measures taken by the BCT to ease foreign exchange regulations**

### **Investments made in Tunisia by non-resident foreigners**

- Lifting of the regulatory ambiguity regarding the liberalisation of transfers of proceeds from the sale of non-resident investments in accordance with Article 1 of the Foreign Exchange Code, which was not followed by a circular.
- Abandon of its intervention in the granting of authorizations for investments made by foreigners in the capital of companies carrying out activities not governed by investment codes (holding companies, retail trade, transport).
- Consolidation of the investment file as the exclusive document to justify the import of foreign currency, with a redesign of its form and transmission methods to the BCT.
- Authorised intermediaries allowed to regularise investments and financing of non-residents financed in foreign currency and supported by any bank document (other than an investment file) and carried out before the date of publication of these reforms (with a time limit).).

### **Investments made abroad by residents**

- The right of transfer as a foreign investment must be the prerogative of companies benefiting from an exchange discharge, relative to a situation and not to a document, and that will be defined in reference to criteria relating to: (i) prior exercise for a certain number of years in Tunisia (3 years, like Morocco), (ii) transparency, soundness and financial performance, compliance with the tax authorities and exchange regulations in force (certified accounts, commitments not classified as CI, activity related to that of the resident company, tax clearance, acknowledgement of receipt of documents submitted to the BCT under the obligation to provide information, certificate of repatriation of export products - IAT then BCT)
    - Revision of the regulatory framework for companies insofar as the transfers to be made will be set in relation to net equity and therefore to a reference other than turnover as is currently the case. They may represent a fraction of 30% of net equity, for example, with a ceiling to be established. Investments that do not meet this condition will be subject to approval by the BCT,
- (iii) the provision of information to the BCT must be respected. At this level, the text should clearly highlight a system of dissuasive sanctions in the event of non-compliance with the provisions of the said circular and, in particular, in the event of a lack of information (which may include a ban on the foreign exchange market following the example of certain countries such as Argentina)
- (iv)

### **Purchases of debt securities issued on the domestic market**

- Removal of the cap on foreigners' subscriptions to debt securities issued by the State or by resident companies for new issues (in consultation with the services of the Ministry of Finance). It should be noted that such a measure has a positive signal effect, particularly for holders of long-term savings (pension funds) who are looking for profitable investments. It does not present any major risks in the current situation (high country risk, absence of a secondary market for debt securities issued on the domestic market, size of the stock already constituted in these securities, etc.). In any event, this measure could be reviewed in the light of changes in the behaviour of foreign investors.

#### External borrowing

- Maintainance of the current framework with the following necessary adjustments: (i) remove the ceilings for credit institutions, (ii) remove the ceilings for fully exporting companies, and (iii) raise the ceilings to 10 billion dinars per calendar year for companies other than fully exporting ones.

#### **Money market in foreign currencies and local credits**

According to its reform plan, the BCT plans to allow non-resident industrial companies based in Tunisia to gain free access to foreign currency money market resources to finance expansion investments, with initial investments to be financed by importing foreign currency. Non-resident companies established in Tunisia, exclusively industrial, legally incorporated and in a sound financial situation, may benefit from financing in dinars. The financing must relate to the acquisition of rolling stock or equipment necessary for the operations only; the repayment must be made in foreign currency (leasing credits). This is a move towards the convergence of the two off-shore and onshore regimes, and aims to boost leasing credits.





## CHAPTER 4

# How can social entrepreneurship contribute to the development of the private sector and support growth and employment in Mediterranean countries?

by Constantin TSAKAS and Karine MOUKADDEM

### Introduction.

#### Why and how is social entrepreneurship important for Mediterranean countries (MC) ?

The previous chapters highlight the need to find innovative tools to support the private sector in the Mediterranean countries to boost economic activity that generates sustainable and viable wealth. However, in order to ensure the sustainability of a new model, we believe it must include both a social impact and inclusive growth.

We believe that, in its different forms and designations, Social Entrepreneurship (SE) provides a relevant response, as it meets certain major challenges faced by the Mediterranean, among which:

- when supported by appropriate public policy it can **contribute to the economic security of all segments of the population**. The British study State of Social Enterprise Report 2015 shows that social enterprises are economically efficient while strengthening equity, diversity, equality and respect for the environment. In addition, several fields of SE and the Social and Solidarity Economy (SSE) propose solutions to the challenge of informal work, such as micro-credit and small cooperatives.
- It can form **a solution to the lack of economic diversity**. A number of forms of SE can be found in all sectors. The same British report underlines that 59% of social enterprises introduced a new product or service in 2015, as compared to only 38% of traditional SMEs. In addition, its limited-profit business model and principles mean low exposure to financial market transactions.
- It is **based on territorial development and proximity**,

*promoting community participation and prioritizing local social impacts. It promotes local agriculture and allows a different approach to the individual's relationship to food. The creation of sustainable and non-relocatable jobs is also at the top of the SE agenda.*

- Finally, **it is a school of participatory values**, through participation in organised civic expression and thus in the appropriation of the corresponding institutional rules.

*SE places human problems at the centre of the development process. It could therefore become a tool for economic, financial and social innovation adapted to the MCs.*

*The long-awaited development of entrepreneurship in the Mediterranean must therefore include **companies with a social, societal or environmental purpose, which will generate profits, not as an end in itself, but rather as a means designed to meet the needs of the territory and to create local jobs**. This seems all the more feasible as MCs abound in potential to meet the challenges of inclusive economic development. SE in MC is an integral part of traditional solidarity structures and collective and community enterprises. Overall, the number of jobs created by SE is significant, estimated at 4% of the population in direct jobs in the MC and much more if we count the jobs created indirectly (Graph 1).*

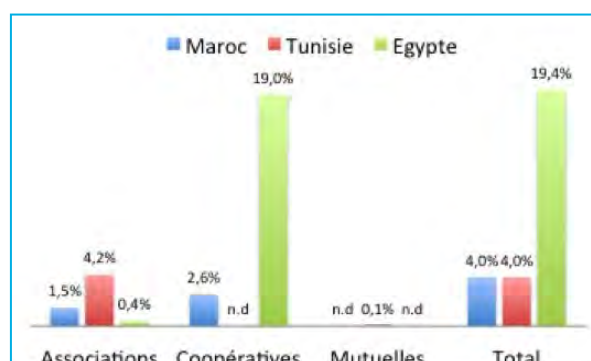
*Following the wave of revolutions, new organisations and actions have been promoted in the MC, in particular by groups of citizens proposing initiatives for the provision of economic and social services to disadvantaged groups. However, despite this momentum, the economic*

performance of SE is still falling short of the expectations raised by the economic and social context. For this reason, the chapter is divided into three parts.

In the first, we address **the situation of the MC in terms of SE and the obstacles to its development**. In the second, we focus on **the range of tools (particularly financial)** to support and develop SE in MC. Finally, in the third part, we present **areas for reflection** which could feed into future actions and programmes to promote SE **within the framework of the EuroMed partnership**.

It should be noted that since there is no consensus on the definition of SE, we review, in the box below, how this concept is defined in the economic literature. We also provide more details on SE schools of thought in the appendice (Box A1). **With regard to this report, we will consider SE in its broadest possible terms. For FEMISE, indeed, social entrepreneurship is defined by a practice that combines innovation, dynamism and the ability to meet social and environmental challenges. The social entrepreneur creates a social enterprise, which may be for-profit or non-profit, but which always seeks to solve societal problems (poverty, marginalization, environmental deterioration, etc.) through innovative solutions or not.**

**Figure 1.**  
**Jobs (direct and indirect) generated by SSE structures, as a % of total employment**



Source: FEMISE-BEI (2014)

## I. SE its place in MC and the obstacles to its development

### I.1 An analysis of the development of SE on MC

One of the main characteristics of SE is its **ambition to find innovative solutions to socio-economic questions neglected by the commercial sector** due to their lack of profitability, as well as by the public sector in a context of fiscal austerity. As shown in Table B in the Appendice, in most MC there is a real culture of solidarity and collective work at the heart of the SE process.

**Social entrepreneurs in the MC mostly invest in sectors such as personal services, professional integration, fair trade, agriculture, culture, social housing, waste recycling and tourism** (Box 3 focuses on specific examples of structures that have emerged in the MC in sectors such as agriculture and tourism). In MC, SE companies contribute on average to 10% of national GDP (OECD, 2010). These companies would also appear to out-perform traditional companies in the longer term. Moreover,

**Box 1. How can social entrepreneurship be defined?**

Since its inception, social entrepreneurship has been considered as an innovative and attractive approach to more effectively meet complex social needs. By focusing on problem solving and social innovation, social entrepreneurship activities blur the traditional boundaries between the public, private and non-profit sectors, with an emphasis on hybrid models of activities that can be both for-profit and non-profit.

In the United States and Europe, since the 1980s, there has been a gradual scaling-up of debates on social entrepreneurship. The first social enterprise model was created in Italy in 1991, in a legal form specific to social cooperatives. Then, France, Greece, Poland, Portugal, and Spain followed (Defourny and Nyssens, 2010). In 2004, it was the United Kingdom's turn to engage in this momentum by announcing the establishment of a second form of social enterprise, the Community Interest Company. From the 2000s onwards, publications on this subject have become more frequent, while social entrepreneurs are increasingly recognized.

Thus, social entrepreneurship is not a new concept. **However, there is still no consensus on the definition of the criteria to define social enterprise.** Providing a definition, with its conceptual boundaries, is a complex task, partly because the term encompasses a wide range of activities and initiatives.

Social entrepreneurship was globally recognized as a new type of entrepreneurship with the main objective of creating social wealth rather than producing economic wealth. (Dees, 2001 ; Drayton,

2002 ; Leadbeater, 1997). This type of entrepreneurship has also been identified as having significant economic effects on growth, poverty reduction and large-scale social development (Yunus and Weber, 2008; Zahra, Gedajlovic, Neubaum and Shulman, 2009). In the public sector, it has been associated with a new shift in the social policies that have been put in place by the EU since the 1980s (Dees 2001). In addition, it has been associated with forms of corporate social responsibility (CSR) and corporate social innovation (CSI).

Social entrepreneurship is thus linked to for-profit but also non-profit activities. In the case of non-profit enterprises, it refers to the strict dimension of social entrepreneurship (SESD), where the sole purpose is to solve social problems (Certo et Miller 2008). In the case of for-profit enterprises located in the sphere of social entrepreneurship, the resolution of social problems becomes a fundamental objective of the activity carried out, beyond the traditional concerns of profitability (Peris-Ortiz 2015). Social entrepreneurship takes on a broader dimension here (SEBD). It is not surprising that the different definitions of social entrepreneurship are often challenged across economic sectors, among academics, as well as across regions, countries and even sub-national spaces. (Kerlin, 2006 and Kerlin, 2015).

If we were to synthesize the different understandings of what social entrepreneurship is, we would distinguish two **groups of perception, American (where legal form is of little importance) and European (with a strong focus on governance)**, each having their own sub-categories. Overall, we can identify four analytical approaches to social entrepreneurship. They are described in more detail in the appendix to this chapter (Box A1).

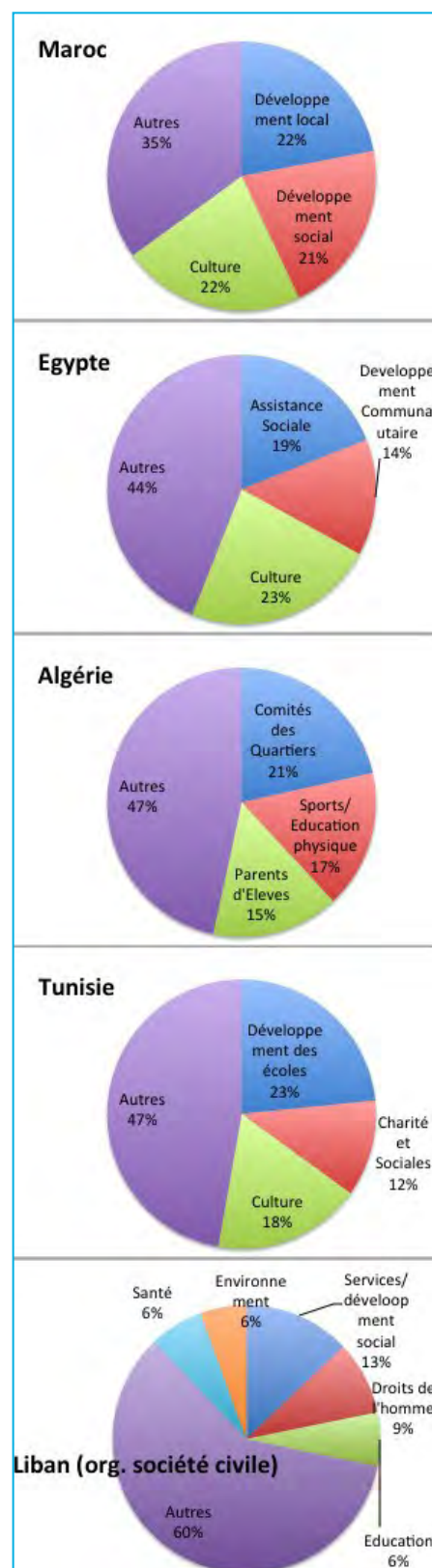
mechanisms have been developed in recent years to support the development of SE initiatives.

**The SE landscape is complex due to the multiplicity of stakeholders.** SE is structured, with great legal diversity, around the associative fabric, NGOs, the above-mentioned initiatives, the cooperative fabric and the microfinance sector.. In all the MC, the preferred fields of activity of the associative sector are education, culture, agriculture and charitable and social work (Figure 2). In addition, the sectoral distribution of cooperatives shows the prevalence of the agricultural sector (Figure 3).

The MC analysis below reveals certain national specificities:

**Jordan** seems to follow the American "Social Enterprise School" approach with the recent emergence of "organic civic initiatives" (OCI). This is a new form of social enterprise created as a non-profit corporation under a law adopted in 2010. Under this legal form, Jordanians can form a company to work in areas related to four specific social objectives (education, health, capacity building and microfinance). OCI do not pay taxes as long as their profits are reinvested in the social objective they seek to achieve. The registration procedures for an OCI are simple and local actors claim that it only takes 45 minutes to register as a non-profit OCI with the Jordanian Ministry of Industry and Trade (AlNasser, 2016). According to AlNasser (2016), there were 100 social enterprises in Jordan in 2016 in the form of OCIs and 400 non-profit organisations, including private schools and hospitals, recently registered after the declaration of the new law. These OCIs offer a redefinition of the social impact of SE as they focus more on

Figure 2. Priority fields of activity of associative structures in MC



Source: FEMISE-BEI (2014)



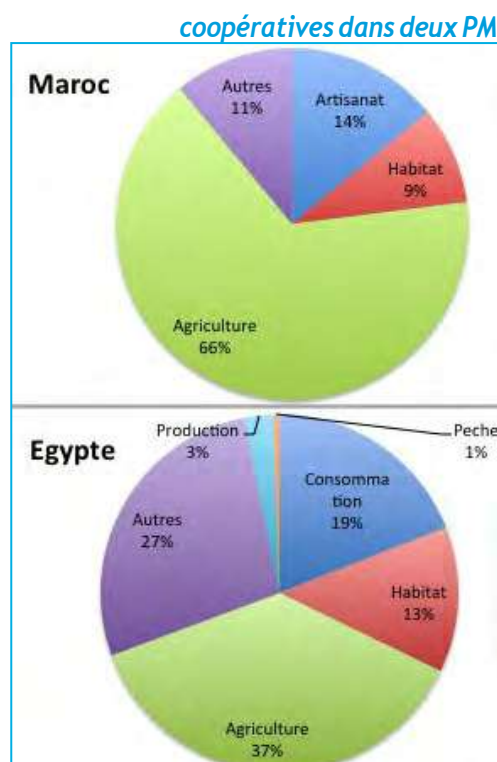
Community needs. It would seem, however, that "traditional" forms of SE are becoming less popular. The Jordanian Cooperative Corporation (JCC) reports that only 1.55% of the Jordanian population was a member of a cooperative in 2016.

Regarding other MC, we may note that **Tunisia and Morocco** have opened a national dialogue on social entrepreneurship, within the more general framework of social and solidarity economy policy. The organisations in these two countries are closer to the EMES model of Social Entrepreneurship (described in Box 1).

**Tunisia** has nearly 20,000 associations with more than 12 million members, half of which were created over the last five years under the impetus of post-revolution civil society. The agriculture and fisheries sector is particularly involved in SE, especially since the sector has more than 3,000 development cooperations, 284 agricultural service cooperatives, 18 agricultural production cooperatives and several companies in charge of these structures at national and regional level. At the institutional level, various structures ensure compliance with legal standards in the sector, including the National Union of Mutuals (UNAM), the Tunisian Social Economy Network (RTES), PLATESS (SSE Platform), RADES (Network of Development Associations).

**In Morocco**, dynamic initiatives have been created under the sponsorship of companies or associations. It should be noted that since its launch in 2005, the National Human Development Initiative (NHDI) has given a quantitative and qualitative boost to traditional SSE structures, including cooperatives and associations. In quantitative terms, the number of creations has increased considerably (the number of cooperatives has risen from 5,749 to 9,046 between 2007

*Graphique 3. Champs d'activités prioritaires des structures*



*Source: FEMISE-BEI (2014)*

and 2011 and was then multiplied by three between 2011 and 2015). In qualitative terms, the second phase of the NHDI, which requires beneficiaries to contribute 30% of the funding for their activities, has led to the empowerment of these beneficiaries, and has given rise to more viable economic entities (REMESS). The HCP notes that three quarters of the associations have a local impact, favouring local actions. Their field of intervention tends to focus on "Development and housing" (35.2% of associations), "Culture, Sport and Leisure" (27.1%) and activities related to education, social and health (HCP data, 2011) (See Table C, Appendice). The cooperative form benefits from the greatest support from the authorities with a contractual partnership with the State. Support includes training in participatory governance and material and financial assistance for the marketing of cooperative products in supermarkets..

SE value chains in Morocco are composed of private sector companies, as production cooperatives in the agricultural, craft and/or fishing sectors market their production in the private sector (local, regional, small and large distribution markets, etc.). Nevertheless, the latter enjoys a significant profit margin offered by a low-paid, poorly or undeclared workforce. The suppliers of the vast majority of cooperatives are also composed of private companies and producers. Although SE in Morocco is more developed than in some MC, it would seem that its contribution is not always that of quality production, but often cheap production using an untrained workforce that is ill-informed as to its rights (testimony Quartiers du Monde).

**In Lebanon**, the social entrepreneurship ecosystem develops through a bottom-up approach. The legal framework is under construction, with entrepreneurs, incubators, financial institutions and NGOs all participating in the legal design of social enterprise. Beyond reform and development (a Lebanese actor with an undisputable social impact described in the appendix), in collaboration with COSV, is leading the initiatives to introduce the notion of social entrepreneurship into the national SE law (see Box 2).

**Box 2. Lebanon: Innovative partnership between Civil Society and International NGOs to define the national legal framework for SE**

Beyond reform and development and the Italian NGO COSV joined forces and created a platform for SE in 2017, in order to facilitate the action of social enterprises and to gather their needs to translate them into policies. This platform aims to enable the growth of social entrepreneurship, to multiply opportunities for job creation and to improve the transparency and efficiency of government

*decision-making in the affairs of private and public organisations.*

*For the time being, the platform's initiatives have essentially been inspired by the reform of the tertiary sector and the new law on SE in Europe, while adapting it to the local Lebanese context. The existing legal possibilities at the moment are: NGOs, cooperatives, civil societies and commercial entities (SEL, SARL). The social enterprise qualification is granted if the organisation complies with a certain set of conditions on which there is a consensus: the social impact of the organisation's activities, the type of governance and financial model, as well as the principles of intentionality, measurability, sustainability and adaptability. In addition, the platform is trying to reform labour law to include more transparency, in particular with regard to the publication of financial and social reports. Thus, both organisations are doing a considerable amount of work on the potential conditions and policies that could be implemented in an ad-hoc law on SE. To prove the compatibility of these principles and identify the final rules, an implementation phase is led by a group of selected Lebanese social enterprises in order to propose optimal law amendments to the relevant ministries and government institutions.*

*Thus, Lebanon will have benefited from Italian, European and international experiences and from the debates already concluded, making it possible to avoid costly and sometimes ineffective choices and decisions. The Lebanese example could also serve as a model for other countries in the region regarding definitions, conditions, incentives, standards and impact measures, thus creating a category of autonomous legal persons for social enterprises: organisations qualified as social enterprises for their sector of activity, their social utility and their non-profit purpose.*

**Egypt** is a special case with many structures that have a social and solidarity vocation. Private initiatives have emerged to address the inability of governments and formal activities of the private sector to meet the diverse needs of poor households. As a result, new and diversified forms of collective organisations or actions have been developed to meet the multiple needs of citizen groups. These institutions for collective action are grouped under different names, including NGOs, cooperatives or unilateral initiatives of limited duration. Membership levels in cooperatives is the highest as compared to all other organisational structures, whether in the public, private or non-profit sector. Membership was estimated at 14 million people in 2016, or about 16% of the total population. Data on Egypt indicates that SE contributes to between 7 and 8% of GDP, a share that could increase if obstacles to the sector's development were removed.

While in the other MC, SE developed in the 1980s, partly in response to structural adjustment plans, **in Algeria** SE only appeared in the 1990s. The Association Act of 4 December 1990 contributed to the emergence of an associative movement, with autonomy from the State. Act No. 12-06 of 12 January 2012 marked a new step forward and today, the range of actions of more than 100,000 associations is relatively wide (consumer, environmental, sports and neighbourhood associations, etc.). It should also be noted that there are mutuals, acting in addition to social security and recognised as being of social utility. The question is currently being raised as to better supervision of the latter, which could go hand-in-hand with their development.

**In Palestine**, even though the political dialogue has not yet started, certain initiatives

carried by civil society and international partners deserve to be highlighted. Social inclusion is one of the main initiatives of the Leaders Organisation, and therefore one of the programmes undertaken by the organisation is the Social Enterprise Accelerator (SEA) programme. Particular emphasis has been placed on the most vulnerable groups such as women and youth, with the aim of creating sustainable social enterprises that would have an impact on communities that benefit from extensive support programmes. The SEA programme has provided training for more than 150 entrepreneurs aged 22 to 30, and has hosted and supported 7 start-ups, with a female participation rate of 42%..

The Palestinian social entrepreneurship sector also benefits from the participation of entrepreneurs in forums such as AMWAJ, ("waves" in Arabic), an international forum on sustainability and entrepreneurship focusing on the MENA region, organised by PepsiCo in Amman, Jordan. This type of event allows young social entrepreneurs to connect with incubators and accelerators but also allows them to explore technical and financial resources. An example of a social impact project that participated in this forum is BuildPalestine, a crowdfunding platform for social enterprises.

## **I2 Obstacles to the functioning and development of SE**

For social entrepreneurs to succeed, they need an **ecosystem of social innovation** that is as developed and promising as that of traditional businesses. However, such an ecosystem is generally lacking in MC.

More specifically, we may note that :

**i. In all South Mediterranean countries, with the exception of Jordan,**

### **Box 3. Agriculture: a growth sector for SE**

**In Morocco**, "SOS Maroc Terroir", affiliated to the Moroccan Alliance for Climate and Sustainable Development (AMCDD) has become a key player in the debate on the Moroccan agricultural sector as a key element of the economic and social development strategy. This social enterprise works to contribute to safeguarding national food security and creating added value in the region while defending the environment and fighting poverty. It promotes the need to support rural organisations in order to facilitate the marketing of their products and creates an online space for the exchange of experiences and networking to promote local products.

**In Jordan**, Sakhrat Women's Cooperative is a participative cooperative for agriculture and traditional crafts. Its members are involved in packaging cereal, manufacturing everyday products, working in textiles and in handicrafts. In order to promote culture and eco-agriculture in Jordan, the cooperative facilitates its members access to loans to launch their own initiatives and the funds obtained are invested in the various projects whose benefits are then distributed fairly among the members. The major challenges addressed by the projects launched are the exploitation of women in agricultural work, the lack of a national agricultural strategy and the high level of poverty and unemployment in rural communities. Thus, an association of women farmers has been created with 450 members to protect and raise awareness among women in rural areas, in particular, on their rights.

**In Algeria**, the agricultural sector therefore has a lot of potential and areas of activity where SE is developing to compensate for the lack of economic diversification. Certified organic areas represent a small proportion of the crops in Algeria (700 hectares of the 9 million hectares of agricultural land). Considered unprofitable given

organic certification, social entrepreneurship in agriculture is stagnating. This is why Torba, an AMAP\*[Association pour le maintien d'une agriculture paysanne; editor's note] created in 2016 and based in Cheraga, is working on citizen awareness. This association brings together nearly 300 members and supports small farmers who farm without pesticides. In addition, Bionoor is an Algerian company, also present in France, which has developed a production and sales chain for organic and fair-trade dates in the city of Ouargla. The company works with local farmers, connecting them to new traders in France and elsewhere. As a result, the establishment of effective public services is necessary.

**In Tunisia**, in 2016, the State granted 50 million dinars in the form of bonuses to agricultural investors. This commitment was reinforced in March 2018 by the launch of the Agripreneur 2.0 program by the Ministry of Agriculture, Water Resources and Fisheries. Agricultural entrepreneurship, especially in rural areas, is recognized as a key means to overcome challenges. The priority of this initiative is therefore to raise public awareness of effective and sustainable agricultural practices. An example would be Tazart, a social enterprise founded by Ali Karkour who started his fig business at the age of 17 in 2015. Tazart promotes figs and dates from the Tataouine and Kébili regions and works to improve the working conditions and techniques of farmers in these regions. Tazart products are available in fine grocery stores and promote environmentally friendly cultivation techniques.

**In Egypt**, Agrimatic Farms, Bustan Aquaponics et Schaduf, are all startups in the hydropower and agricultural sector, affirming the ability to use new technologies to achieve 90% water savings compared to traditional agricultural methods. The social enterprise Farminal, that created early warning system software, is trying to provide high-tech solutions to the problems of the dairy sector, while BioGas



**There is no specific legislation to govern social enterprises.** Social entrepreneurs may choose to register as a non-profit organisation, or as a private commercial enterprise, cooperative, civil society or a mix of different forms..

ii. **The lack of access to funding, linked to the legislative barrier, is one of the most important obstacles.** Indeed, as there is no specific legal framework, social entrepreneurs are either bound by their non-profit business model, which penalises their sustainability, or they are forced to develop profit-making activities with a social impact but without any incentives (legal, fiscal or technical) and are no longer eligible for donations and subsidies. Moreover, the nature and activities of social enterprises **limit the attractiveness of this model for investors.** Structures sometimes have access to funding, but this remains limited or costly. In addition, SE may become dependent on specific funding sources, which could condition their orientation according to the donor's policy.

iii. The development of SE goes hand-in-hand with entrepreneurial spirit. We must also mention the obstacles related to the creation of companies in the MC, **in particular public**

**administrative barriers.** Although SE initiatives maybe undertaken anywhere throughout the territory, the administrative process remains centralised, which is an obstacle.

iv. As enthusiastic as SE may be, there is often a lack of knowledge, a **qualitative (and quantitative) weakness of their human resources**, which is reflected in their skills in management, planning, project design and evaluation, market development, training, etc.. In addition, there is sometimes a lack of clarity about their scope of action, difficulties in mobilising volunteers or convincing those already committed to continuing to work in these associations.

v. Finally, **in general, the State does not provide sufficient support for SE and social innovation.** Limited public financial support is only one side of the problem. Indeed, unlike countries in which SE is experiencing a real boom, the MC States have not been able to support the emergence of local mechanisms that support SE structures, thus depriving them of access to the necessary professional advice, know-how and support.

With regard to each of the countries specifically, the following facts should be highlighted:

#### **Box 4. Tourism, another SE “growth” sector**

*Social tourism presents many opportunities to enhance the value of cultural and environmental heritage in the MC where the development of poorly regulated tourism would harm economic prosperity, especially in view of the lack of diversification and collaboration between the various local actors. However, sustainable and ecological tourism currently represents only 1% of Mediterranean tourism.*

*The idea of alternative tourism has been particularly popular in **Morocco**. The beginnings of social tourism in the Kingdom are mainly due to the importance of tourism in terms of job creation (15.99% of job creation over the period 2000-2015) and in the economy in general (about 20% of GDP). In 2015, a Partnership Agreement for the development of sustainable tourism in natural areas was signed by the Minister of Tourism, and the High Commissioner for Water and Forests and the Fight against Desertification. This aims to develop an integrated tourism offer for all the*



<p>Moroccan natural spaces according to a development plan, vision 2020, identifying all the fragile sites to be conserved and the areas that can both accommodate tourist activities and respect the specificities and constraints of the sites where they are located. For the promotion of ecotourism, we may note the "Terres d'Amanar", a project initiated by Jean-Martin Herbecq in 2007 and located on more than 100 hectares near Marrakech. This ambitious project consists of a recreational centre to facilitate the economic development of this rural region, while helping residents to preserve their culture and environment. Since 2007, the park has been offering leisure facilities to the general public and in compliance with European safety standards.</p> <p><b>In Tunisia</b>, the absence of a national policy for marketing and promoting ecotourism is an obstacle to its development. Alternative tourism faces a major challenge: the non-recognition of a specific status is preventing the development of ecotourism, as it does not come under the responsibility of the Ministry of Tourism and is difficult to include in administrative procedures. While tourism represents between 15 and 20% of Tunisia's GDP and counts for 15.70% of national employment (annual average 2000-2015, World Travel Council, 2016), ecotourism remains highly underdeveloped.</p> <p>Within this context, the European Commission has set up the SwitchMed project to support the creation of the Ten-Year Action Plan 2016-2025 on tourism in Tunisia, managed by the Ministry of the Environment. This project has resulted in the allocation of subsidies to certain social enterprises working in sustainable tourism, in particular Tunisia Ecotourism. This eco-tourism agency received support between 2016 and 2018 to integrate the green economy concept in its services to local and foreign tourists.</p> <p><b>In Lebanon</b>, there is considerable potential for this new alternative. There is still no definition of</p>	<p>Eco-tourism at the national level, but a multitude of decentralized initiatives are emerging.</p> <p>The number of actors in ecotourism has increased significantly in recent years. The number of tour operators organising hikes and treks has increased from 10 in 2008 to more than 30 to date. Other local actors such as guest houses, NGOs, municipalities and donors (such as USAID and the European Community) are multiplying their initiatives. Souk al-Tayeb, for example, is a farmers' market that is opening restaurants all over Lebanon and their income is used to finance the restoration and rehabilitation of houses, in Lebanese villages, to be used as guest houses.</p> <p>Dunia Baroud-El-Khoury's Women's Association of Deir El Ahmar is another example of a social enterprise working to promote alternative tourism. This association aims to bring together Lebanese women from the rural region of the Bekaa to work in rural ecotourism and agro-tourism. The company's actions were rewarded with the Dubai International Award for Best Practices to improve the environment, in 2002.</p> <p><b>In Jordan</b>, platforms such as the "Voyageons-Autrement: Jordan 2018" and blogs on ecotourism in Jordan have been created to promote the different forms of sustainable activities or accommodation offered either by individuals or innovative social enterprises.</p> <p><b>In Algeria</b>, the project "Djebba heritage, a tourist destination" was founded by a group of young Kabyles, headed by Ahmed Farid. The aim of this project is to promote local initiatives within the framework of solidarity tourism, such as the restoration of dilapidated Kabyle houses. They organise spring festivals, for which 2018 marked the 5<sup>th</sup> edition, with the objective of transforming the village into an eco-tourism centre.</p>
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**In Morocco, the development of the draft SSE framework law offers some hope, but the process is lengthy.** In addition, SE actors in Morocco are exposed to great precarity.

The High Commission for Planning (HCP) published, in 2011, the results of a national survey of non-profit institutions highlighting the difficulties encountered in the associative sector, which prevents the different structures from working successfully and ensuring the proper monitoring of their operations. More than half of the associations have no premises and nearly 30% are hosted free of charge. Only 11% are tenants and 9% owners of their premises. The majority of associations are poorly equipped (computers, internet connection, accounting, etc.) and lack qualified human resources. Women, who constitute the vast majority of SE workers in the country, must also deal with the multiple problems specific to rural Morocco (high illiteracy rate in rural areas of 41.9% among women), remote territories that are far from marketing zones...) more those due to the inequalities and discrimination experienced by women in Morocco, which are even more pronounced in rural areas: lack of mobility, market access, income management, and decision-making (Quartiers du Monde). Women's work is seen as an extension of their domestic activities and remains undervalued. They are victims of early employment, before the age of 15 (73.2% of rural working women compared to 59.8% of rural men), and unpaid work.

**In the case of Egypt,** since the mid-1980s and after the introduction of the Cooperatives Act, many voices have called for its improvement as it was inadequate in introducing the required changes in the cooperative sector. The same might be said of the NGO law. The second recurring problem is the lack of sufficient funding for cooperatives and for a large number of small NGOs, despite the fact that they serve a large community

of beneficiaries throughout the country (Abdou and El Ebrashi, 2015).

**In Tunisia,** within the framework of the legislative initiative of the Tunisian General Labour Union (UGTT), work on a draft law has now been under way for some time, to create a specific institutional mechanism and structure in charge of promotion and a statistical system specific to the sector. This would allow the monitoring of the main indicators and the evaluation of the real contribution of SE to local development, social promotion and employment. The bill was then the subject of a public consultation. Some experts pointed out shortcomings in the current version of the draft: ethical values and the notion of "decentralization" are absent, certain categories that are the supposed targets of SE are absent (rural women and people with disabilities), administrative procedures also seem complicated. The possibility of creating a "mutual bank" to finance the social and solidarity economy sector also seems to have been excluded (AfricanManager, 2018).

In addition, the poor performance of the social and solidarity economy in Tunisia is also due to the deficit of mobilised financial resources and the ability to raise funds, particularly from the various international donors. At this level, support has so far been reserved for human rights associations or the promotion of categorical rights.

**In Algeria, the development of SE remains rather limited.** The State does not provide sufficient recognition of its general interest, which is an obstacle to its organisation. It should also be noted that the sources of funding for associations are essentially limited to government subsidies, as the internationalisation of associations is not viewed favourably, as it is considered to

Challenge the State's "effective control" over community associations. Thus, the jurisdiction limits the possibilities for local associations to establish links with international organisations (IPEMED, 2013). The National Youth Employment Support Agency (ANSEJ), which is responsible for providing microcredits and other forms of support for small projects, is trying to reorganize its priorities in order to focus funding on strategic sectors such as agriculture, industry, construction and new information technologies and to intensify its support for unemployed young graduates. Nevertheless, this institution depends mainly on the availability of public funds. Thus, when the austerity measures were put in place by the Algerian State in 2016, 64 ANSEJ activities were suspended, in particular those concerning the agriculture, plumbing and electricity sectors, the latter being key sectors for employment.

**In Lebanon**, social entrepreneurs have so far been working without incentives or support from public actors in their social impact activities. Some social enterprises manage to overcome the obstacles imposed by the lack of legal recognition but acknowledge that this prevents them from broadening the impact of their interventions.

**In Israel**, political dialogue has been initiated, but only pilot initiatives have been carried out. Although there are already a number of social venture capital funds that invest in social enterprises created with the support of the government, current legislation does not formally recognise social enterprises. Israeli law allows the creation of a non-profit organisation (called in Hebrew an "amutah" or "amutot" in the plural form) or a public interest company (PIC).

Neither can distribute profits, but they are entitled to receive a certificate recognising the company as a public institution under the Israeli Income Tax Ordinance. A draft law has recently been proposed to amend the Israeli Companies Act, with the aim of creating a single legal structure called the "Social Enterprise Company" (SEC) adapted to the needs of social entrepreneurs. According to the draft law, SEC will be allowed to distribute dividends (capped at 50% of their profits) and the profits can be reinvested in social projects (Asaf Shalev and Daniel Kleinman, 2018). Israel therefore seems to be moving towards the American "Social Enterprise School" approach.

However, the Israeli political discourse on inclusiveness and the social impact of SE in society remains to be clarified. Despite the continued growth of the Israeli economy over the past 15 years, social cohesion remains incomplete in the local market and in the socio-economic sphere in general. The OECD report published in March 2018 shows that despite the decline in unemployment in the Israeli economy, socially marginalized groups are largely forced into poverty and discriminated against in access to the financial resources required for entrepreneurial activities.

**In Palestine**, SE and its model remain embryonic (Akella and Eid, 2018). Profit remains the primary goal of social entrepreneurs who are willing to sacrifice their social mission to generate profits. Akella and Eid explain this model of social entrepreneurship, which they describe as "insincere", by the country's institutional structure, the unstable political framework and the lack of a clear legal framework for social, cultural and economic entrepreneurial activities in Palestine. The economic

Agendas of social entrepreneurs are thus hidden behind external social welfare and community development objectives.

The lack of public interest in the issue of social entrepreneurship is a major obstacle to defining an appropriate framework. Palestine depends on external aid and projects from international organizations, which are very often ad hoc. However, social enterprise models can be developed with local actors through strategic facilitation based on the experiences of other countries in the region. Committees specializing in Palestinian entrepreneurial activity would examine immediate priorities to address key issues of food security, lack of safe drinking water and sanitation, construction, health and energy (Abdelnour, 2010).

**In conclusion, the lack of financial resources, the low skills of the social enterprise workforce, the lack of support structures, the ineffective legal framework and the lack of spaces for exchange and coordination between actors are all obstacles that prevent the SE from reaching its full potential in the MC.**

If SE is to become a key element of economic and social development policy in the MC, it is necessary to develop, or even reinvent, social innovation ecosystem. We believe that in order to make SE more attractive and to allow a first step towards the emergence of a real ecosystem in MC, **it is essential to :**

- **Develop adapted tools, designed specifically for social enterprises.** These can take the form of financial, technical or insitutional support. Section II lists certain tools

which, we think, deserve to be developed more generally throughout MC. Some are already present, have proven their effectiveness and could easily be replicated..

- **capitalise on EuroMed cooperation (North-South and South-South) to promote this type of tool.** The structure of SE ecosystems, the networking of different organisations, the State, international financial institutions (IFIs), NGOs and other organisations can only be effective within a framework of cooperation, exchange of knowledge and good practice. Ways forward within the framework of EuroMed cooperation towards sustainable social entrepreneurship eco- systems are thus discussed in Section III.

## **II. Which tools to support and develop SE in MC ?**

### **II.1 Development of funding: A range of ready-to-go tools and others to be created**

At the heart of the dynamics of SE is the question of project financing and the mobilisation of resources. The financing of social enterprises must be at the heart of the concerns of local, national and Euro-Mediterranean authorities. "Social funding" allowing access to liquidity and credit linked to shared coordinated objectives is necessary.

Social entrepreneurs are often unable to finance their projects because the system is poorly (or not at all) adapted to the different types of entrepreneurship. This raises the question of the financial tools and specific mechanisms to be developed to support social enterprises. Solutions to secure the development of ES structures in the Mediterranean are sometimes available, but the lack of visibility in financing circuits is a major obstacle.

Thus, we propose possible tools to address the obstacles identified and that can be supported by all local, national and international actors.

### 1. Financial institutions for the management of “social funding”

Local and international, public, private and institutional actors are all called upon to contribute to a sustainable economic model. Financial institutions are increasingly moving towards more socially and environmentally responsible lending policies. Some focus almost exclusively on SE projects. These "social", "participative" or "ethical" banks **hold the objective of having a positive economic, social and environmental impact in the collection and use of money (FEBEA, 2012)**. They invest in innovative activities and meet the needs of those excluded from the traditional banking system. Before the loan agreement, these banks use, in addition to their economic criteria of project viability, a set of "ethical criteria".

The main advantage of these banks is that they are characterised by a greater commitment to the real economy. In addition, they can play a triple role by acting as (i) an intermediary between the State and social enterprises, ii) as a mediator between social enterprises and local institutions (such as Islamic banks, microfinance institutions described below etc.), iii) as an intermediary between social enterprises and international financial institutions.

**Morocco** has clearly understood the usefulness of these structures and hence, in 2016, prepared all the legislative, regulatory and fiscal instruments necessary

#### Box5. Ethical Banking VS Ordinary Banking

*An ethical bank differs from an ordinary bank in:*

- ***Its role**, which is to work for the common good and ensure the right to credit through the raising and reallocation of funds, in the form of loans, to cultural, social and environmental projects.*
- ***social and environmental impact values** that are fundamental and inseparable from the economic impact value. In an ethical bank, at least 90% of the financing distributed meets both economic and socio-environmental criteria. In addition, an ethical bank systematically measures the social and environmental impact of its activities and the projects/institutions financed.*
- ***its particular attention to supporting employment and/or self-employment initiatives for women and young people, in particular through microcredit and micro-finance interventions.***

*Source: FEBEA (2012), FEMISE-BEI (2014)*

to launch participative banks. Morocco also leaves the way open for innovation, allowing the emergence of new financial tools and unconventional projects, and the integration of people who do not adhere to the principles of conventional finance. In January 2017, five applications for approval to set up participative banks were accepted. The banks authorised by Bank Al-Maghrib to start their participative activity were Umnia Bank, the first participative bank in the kingdom, Bank Assafa, the first 100% Moroccan participative bank, Al Akhdar Bank, the result of a partnership between Crédit Agricole du Maroc and the Société islamique pour le développement du secteur privé (ICD), Bank Al Yousr, an autonomous and universal participatory bank of the Banque centrale populaire Group



and Dar Al Amane, a participatory window within the Société Générale Group presenting an innovative hybrid model in Islamic finance.

We believe it appropriate that each of the MC should support, in particular by establishing a favourable regulatory framework, the emergence of such structures to direct funds towards useful, sustainable and inclusive projects.

## 2. Islamic Finance to Support Social Entrepreneurship

Islamic finance is an alternative to the conventional financial system. It differs from the traditional banking system by opposing certain practices such as "the use of interest rates, speculation, debt assignment, lack of transparency and opportunistic behaviour of managers». The purpose of Islamic financial activity is to promote an ethical, social and moral balance.

According to Amzil (2013), the Islamic banks' financial tools would be perfectly adapted to the expectations and needs of social entrepreneurs. Firstly, Islamic banks would give them access to participatory financing methods. This type of operation consists in the establishment of partnerships whose products are often similar to private equity venture capital operations. In line with the Profit or Loss Sharing principle (3P principle), investment account holders share risks with shareholders of the Islamic bank. Two types of contracts exist to give concrete expression to this principle in the transactions undertaken: **Mudaraba and Mousharaka**.

Islamic finance also offers credit-type financing methods. The **Morahaba**

### **Box 6. Mudaraba and Mousharaka : participatory financing of entrepreneurial activity**

*Mudaraba consists of an association contract between financial capital and labour. According to the Islamic Development Bank, Mudaraba is defined as "a form of partnership where one party provides the funds and the other (mudarib) the experience and management. The profit made is shared between the two partners on a pre-agreed basis, but capital losses are borne by the sole lender. The developer fully manages the business but, while the profits are shared between the two parties in the proportions stipulated in the contract, capital losses are entirely borne capital contributor. This product would allow social entrepreneurs to draw upstream from considerable financial resources in order to meet the funds necessary to undertake their activities without renouncing the ethical and/or religious principles of the capital contributor.*

*Musharaka consists of the participation of at least two parties in the financing the capital of the same business. In this case, each partner is able to intervene directly in the management of the business and this also implies that losses are borne in proportion to each partner's contributions to the capital. This tool seems ideal to facilitate SE as it represents a guarantee of risk sharing. Social entrepreneurs are thus able to mobilize funds for the creation, management or expansion of their businesses while allowing profits and losses to be shared between the developer and the financier.*

*Other types of Mousharaka exist and multiple products are available depending on the needs of entrepreneurs, their preferences, their risk aversion and the type of financiers and partners they have.*

is an example of this. It consists of "a contract of sale at cost price plus a known profit margin agreed between buyer and seller". The borrower reimburses an amount agreed in advance over a fixed period of time in several instalments or in a single payment. Accountability here means that the seller bears the risks concerning the goods until they are delivered to the buyer.

Finally, there are financing methods based on donations and charity. **Zakat** is a religious duty of solidarity with a social scope that can take several forms such as the Sadaqa, al-Hibat or donations, Qard hassan or interest-free loans, al-Maniha or donations and the Waqf (Elkettani, 1997 and Kahf, 1997). The social dimension of Zakat is obvious since it represents an act of solidarity and a form of redistribution of the national product to reduce economic disparities (Elkettani, 1997).

Tunisia has therefore acquired its first Islamic banks. After El Baraka and Zitouna, Wifack Leasing obtained an agreement from the central bank to become a full-fledged Islamic bank, the Wifack Islamic Bank, with a capital of 150 million Tunisian dinars. Morocco also recognises that Islamic finance can be an important source of financing for the development of SE. The current law allows participating banks to market four main products of Islamic finance.

### **3. Encourage the financing of SSE through microfinance**

We also think it is also appropriate to **encourage the financing of SE by microfinance institutions (MFI)**. The latter have a developed territorial network and are close to micro-entrepreneurs and their needs. MFI can facilitate the growth of SE in the Mediterranean.

Among the examples, we may note, **in Tunisia** Taysir Microfinance, a Tunisian microfinance institution launched in 2011 as a project, and which gained official approval in 2014, following the publication of the new microfinance law. With the support of the French association Adie, Taysir has developed microcredit products that support craftsmen, small farmers, shopkeepers and entrepreneurs. The amount of the microcredit varies from TND 500 (production campaign for farmers) to TND 7000 (investment for young entrepreneurs) and for periods ranging from 2 to 36 months. The EU was the first international donor to support Taysir, followed by the Principality of Monaco, the Ile de France Region, Total, Danone Ecosystem, the Institut Français de Tunisie and the Qatar Friendship Fund. Taysir thus became the first accredited microfinance institution in Tunisia and opened 6 branches in the country. Participating banks can also integrate their own microfinance activity, as did the social bank Amen Bank, which finances operations, housing and individuals in Tunisia. **In Morocco**, microfinance is also diversified with 13 Microcredit Associations (MCAs) (4 large national MCAs, 3 MCAs with regional coverage and 5 MCAs that are local associations).

### **4. Association contribution agreements to strengthen equity capital**

The purpose of association contribution contracts is to financially strengthen social enterprises. The purpose of such a contract is to strengthen the equity capital of associations of social utility. Here, the property or the amount of money contributed is part of the association's assets. The associative contribution agreement does not include any interest. The contribution is returned either in one instalment

at the end of the term of the contract, or in several years, at the end of a grace period of at least 1 year.

In France, the France Active model (a French network of associations that works to put finance at the service of people, employment and territories) uses this type of tool. The process is simple. First, an application is submitted to a Territorial Fund of the France Active network. Next, the expertise and financial support from the Territorial Fund comes into play. Then, a decision is taken by a commitment committee of the Territorial Fund or France Active. If the decision is positive, the financing (amount between €5,000 and €30,000 with a right to claw back for a period between 2 and 5 years) and the follow-up of the beneficiary association is organised.

These contracts therefore require the presence of structures dedicated to entrepreneurs that offer them the means to work within their territory, which is not necessarily the case in the MC. The significant support of the State is also a major factor in the success of France Active. In MC, **alternative and/or complementary solutions could be devised to replace and/or use jointly with public resources**, for example through the resources of international donors, if national legislation allows it.

## 5. The development of Social Impact Bonds

Innovation would be another option with **social impact funding contracts (Social Impact Bonds – SIB)** with or without public intervention. SIBs are very popular securities in the Anglo-Saxon world, making it possible to fund social programmes (fair trade, social tourism, access to culture, etc.) through private investors (foundations, companies, etc.) remunerated according to the social result. The implementation

The implementation of the social impact project is entrusted to an association and public finances are only granted afterwards according to the result obtained. Public intervention traditionally serves to guarantee the lender's remuneration in the event of failure, but one can imagine a modulation of the interest/return on capital according to the success or failure, assumed by the stakeholders without a public guarantee.

While Mediterranean countries have recently made progress in terms of supporting entrepreneurship at the strategic level, **SIBs remain a considerable untapped opportunity**, except for in Israel. In Israel, SIBs are already being used to alleviate unemployment in the Arab and Ultra-Orthodox communities by providing vocational training and sustainable career programmes. We may also note the existence of Green Bonds, used for low-carbon or clean energy investments, in Morocco. The Moroccan Solar Energy Agency (Masen) issued the first Moroccan Green Bond in 2016 to help finance the development of solar energy in three projects (Laayoune, Boujdour and Ouarzazate) that are part of the NOOR PV 1 solar energy project. However, beyond these initiatives, SIBs remain very underdeveloped in the region. The report by JP Morgan and the Global Impact Investment Network, "Perspectives on Progress", already highlighted this delay in 2013. This survey of ninety-nine impact investment groups around the world shows that despite the extremely optimistic outlook for SIBs, the MENA region attracts the smallest share of investment. Two factors justify this gap: on the one hand, the lack of awareness of the hybrid concept of SIB, both among entrepreneurs and investors, and on the other hand, the absence of a favourable legal and regulatory environment.

**Box 7. Kafalat, a Lebanese initiative, a tool to support traditional and SSE entrepreneurship**

*Access to finance must be possible for all types of structures, whether for profit or social purposes, in urban or rural areas and whatever their sector of activity. This is made possible by the Kafalat initiative, a Lebanese financial company which, since its creation in 2000 in Beirut, has supported 16,500 projects led by Lebanese SMEs for which it has provided guarantees. These guarantees reassure bankers, allowing SMEs, start-ups, but also ES companies (cooperatives, NGOs) to secure bank loans for their development and to create wealth and ultimately jobs..*

*In the early 2000s, the main loan beneficiaries in Lebanon had their headquarters in Beirut or its immediate vicinity. Only the trading and service sectors were able to access credit. SSE structures were practically excluded from access to bank financing. In the interest of inclusiveness, Kafalat wanted to help all the country's SMEs. Since its creation, Kafalat has defined priority sectors: industry, agriculture, tourism, crafts and new technologies. Also, 42.5% of loans go to the agricultural sector and 15.1% to tourism. In addition, only 5.3% of the loans are for companies based in Beirut. We may note that :*

*The loans guaranteed by Kafalat benefit from a interest rate subsidy established to mitigate the crowding-out effect of high interest rates resulting from public sector borrowing. The subsidy is financed by the Lebanese Treasury and managed by the Banque du Liban.*

*• The Kafalat loan guarantee is issued on the basis of the viability of the project that is the object of the request for funding.*

*Loans guaranteed in Lebanese pounds are exempt from the need to ensure minimum reserves defined by the Banque du Liban, which considerably reduces the lending bank's cost of capital and allows it to grant loans at lower interest rates.*

Thus, it seems to us that SIBs could be further developed in MC, using associative seed funds that mobilise local and/or diaspora savings or even solidarity NGOs. However, **it should once again be a complementary measure, not an argument for reducing the share of public expenditure devoted to the social field.** To achieve this, the first requirement is the legal integration of social enterprises and investment funds. Secondly, there must be more promotion of SE successes and contributing factors. Knowledge of potential and effective strategies to overcome the major challenges of the sector would encourage both investors in terms of potential attractive returns and society in general. It would also encourage government actors to consider SIBs as potential sustainable solutions.

In recent years, Kafalat has adapted its programmes to the partnerships established with the European Union and the World Bank and has also designed new innovation support programmes.

In our view, the inclusive concept of Kafalat could be a model to be followed by the countries of the region. It is a tool that can be combined with both the traditional sector and social enterprises, making it possible to finance projects of modest size (see graph D in Appendix). Before the war, Syria showed great interest in the guarantee mechanism.

## **6. The role of crowdfunding platforms and participative financing**

Participatory finance allows the saver to choose the project or structure that will receive his/her money. In the past,

associations that raised funds according to the participatory principle engaged in "fundraising", favouring social ties and addressing funders directly. Today, whether in the form of grants, loans or capital, specialized Internet platforms make it possible to broaden the scope of the relationship and ensure that each project can be financed by "the crowd" (hence the Anglo-Saxon term "crowdfunding").

The financing process is transparent and there is no intermediary financial institution but **only via the platform**. In concrete terms, projects that register on the crowdfunding platform have a space in which they present their project, propose a clear target to be reached and provide the details of matching donation formulas (e. g. a product, a subscription...). The project bearer must then send the link to their page to their network and relaunch calls for support so that the movement does not run out of steam. If the target is met or exceeded, the platform generally receives a percentage of the overall amount as a facilitator. In the opposite case, the donations are returned to the sender. Finally, the platforms can be general or specialised (culture, women's entrepreneurship, renewable energies, etc.) national or regional.

The concept spread very quickly in developed countries. In France, the amounts collected on crowdfunding and alternative finance platforms (grants, online loans to SMEs) reached €628.8 million in 2016. Crowdfunding allows more inclusiveness for young entrepreneurs, the typical profile of the contributor or investor on a crowdfunding platform being predominantly made up of people under 34 years of age. For donors, their donations may be tax deductible if certain conditions are met. Crowdfunding also allows them to closely monitor the

the progress made by the project bearer, but also to promote their image as contributors to a project with a social impact.

**Crowdfunding is unfortunately not very developed in MC.** In Tunisia, platform projects have been initiated but they have not really been able to launch due to regulatory constraints. A draft crowdfunding bill was to be presented to a Council of Ministers and submitted to the ARP for adoption before the end of the current year. However, Tunisian project leaders have already raised funds from foreign platforms (France, USA, Lebanon) despite the absence of a legal framework. In April 2015, 32 projects managed to raise a total of around €200k, an increase of more than 120% compared to 2014. The main platforms operating in Tunisia are KissKiss-BankBank (grants, based in France), Zoomaal (grants, based in Lebanon), CoFundy (grants, based in Tunisia and France) and Afrikwity (investment, based in Tunisia and France). In Morocco, the legislative framework is not very secure either and the result is the same, platforms are set up abroad. Thus, Smala & Co was the first crowdfunding platform dedicated to Morocco and based in France to be created. The projects financed are exclusively dedicated to Morocco, with priority given to three sectors of activity: SE, green entrepreneurship and the cultural sector. In addition, Smala & Co engages in educational work to raise awareness among project leaders and create a crowdfunding ecosystem in Morocco and North Africa.

Overall, there is a strong demand for crowdfunding in the MC that remains unsatisfied (e. g. in Tunisia less than 5% of the financing needs were satisfied in 2014). The Mediterranean Diaspora would like to target local projects with a strong social impact and direct donations towards "favourite" projects



MC therefore need to set up their own platforms to ensure proximity with project leaders and make the link with funding. We believe it to be desirable, in the medium term, that the MC authorities facilitate financing via this model by proposing a bill that promotes the development of crowdfunding.

### **Crowdfunding can also be a way to finance women's entrepreneurship (Sidlo, 2018).**

Women in the South Mediterranean often do not work outside their homes, have less disposable income to start their businesses and external financing is limited by the small number of women-friendly investors. This problem can, to some extent, be mitigated by the presence of crowdfunding platforms. The results of a recent study show that women's fundraising campaigns are 32% more likely to achieve their fundraising goals than men's. (PwC, 2017). It would seem that women entrepreneurs in the region have begun to seize this opportunity. Beehive, one of the popular platforms for participatory financing in the MENA region, reported that between 2014 and 2018, 20% of the 516 start-ups funded by the platforms had at least one female founder. Its competitor, Zoomaal, specified in 2015 that 60% of the projects seeking funding via the platform were initiated by women. On another local crowdfunding site, Eureeca.com, one fifth of all projects and 60% of those that received funding were created by women.

### **II.2. Develop appropriate support mechanisms to create a SE ecosystem**

Public actors are essential in facilitating cooperation between structures and allowing the emergence of a SE ecosystem. They can

### **Box 8. INTER-MADE : incubator of social and solidarity enterprises**

*Inter-Made is a social business incubator based in Marseille that seeks to promote SE as a sustainable solution to the major challenges of the PACA region. Inter-Made supports young social entrepreneurs in the elaboration and development of their projects. A team of professionals accompanies the projects through the various stages of their development:*

*From the Starter to incubator and to post-creation follow-up. Upstream, supported by the incubator, the "Initiative Factory" relies on all the resources of the region and the skills available to implement viable and sustainable SE projects. The different stages of the process consist firstly, in identifying the socio-economic needs and opportunities of the territory, secondly, in validating the relevance of a SE solution, thirdly, in identifying, recruiting and qualifying a project leader, fourthly, in accompanying the leader until the creation of the social enterprise.*

*The Starter consists of a 3-month training course and personalised support for the needs and expectations of each social enterprise in line with its objectives and structure. The Starter's objective is to raise social entrepreneurs' awareness of the various main questions around SE through adapted training modules. These training courses, given in groups of a dozen people, are mainly intended for entrepreneurs under 35 years of age and are conducted in the form of practical workshops.*

*The Inter-Made Incubator is responsible for testing the social enterprise's activity in an area of mutualisation and cooperation, while providing individual support, legal advice and collective training (9 to 18 months). After the incubator, Inter-Made supports social entrepreneurs as part of a post-creation follow-up-*

*consolidation for 12 months. The purpose of this step is to ensure a transition to business development and to limit risks by providing Inter-Made's consulting and training services.*

***Resultss:** Environ 518 projets et 450 entrepreneurs sont passés par le starter depuis 2002 ; Plus de 300 études de faisabilité réalisées grâce au programme ; 135 projets ont été couvés depuis 2002 ; 85% des projets qui sont passés par la Couveuse sont toujours rentables 5 ans après leurs lancements à travers l'incubateur.*

***Partenaires principaux :** Région PACA, Conseil Général- Bouche du Rhône, L'Acsè, l'Europe s'engage en France, Avise, Caisse des dépôts, Vitrolles, CCFD TerreSolidaire*

***Territoire(s) impliqué(s) :** la région PACA (Marseille, Toulon, Avignon, Vitrolles et Arles)*

***Impact régional :** Jusqu'à présent, plus de 300 entreprises sociales ont été créées et/ou accompagnées ce qui correspond à près de 1000 emplois créés et 800 personnes formées.*

help to support the economic diversity of solidarity entrepreneurship and the sustainable development of territories through appropriate policies, tools and legislation.

## 1. Towards a generalisation of support and assistance mechanisms for SE and Social Innovation

We believe that it would be appropriate to develop tools to support the sector and collective territorial poles of social development, which would make it possible to standardise the links between the economic and social spheres. Among the replicable experiments that have already proven effective are **local support systems (DLA)**, public schemes created in 2002 by the French State and Caisse des Dépôts and with the support of

the European Social Fund, which target social entrepreneurship structures that wish to benefit from support in their efforts to create, consolidate and develop employment. Since 2003, these schemes have supported nearly 51,000 structures in France, representing 660,000 jobs. This type of mechanism makes it possible to provide advice, technical support and training and to contribute to the mobilisation of networks and territorial resources.

Another form of support mechanism is the **regional incubator dedicated to social innovation**, co-financed by the European Regional Development Fund and able to support project bearers in the implementation of their projects. The objective is to support social utility in an innovative manner to meet societal needs; this is an economic choice just as technological innovation is.

One example is Alter'Incub, a social innovation incubator that provides tailored support for socially innovative projects. With the objective of sustainable entrepreneurship and job creation, Alter'Incub facilitates cooperation and the exchange of good practices between social project leaders, territories and research in the human and social sciences to meet needs of public interest.

It should be noted that Tunisia supports SE in a form that is multi-partner by nature, as shown by the Social and Economic Economy Laboratory project (Lab'ESS). This laboratory, developed in collaboration with, among others, the SOS Group and the Comptoir de l'Innovation, includes the activities of the Bureau Associations Conseil (BAC) and a social business incubator. Two types of support are proposed: i. the first is specific and responds to the targeted and specific needs of an association and ii. The second is

general and aims to strengthen the association's internal skills.

The support is provided by a team of project managers (Tunisian and French), accompanied by project managers specialised in fundraising, associative law, and graphic design. We can therefore see that the impetus of civil society sometimes makes it possible to develop tools that make up for the lack of public support. **A real discussion on the generalisation of such structures with the support of public authorities deserves to be launched in each of the MC.**

## **2. Administrative simplification and facilitation of cooperation between structures**

The public authorities of MC need to simplify the procedures for creating and managing social enterprises and facilitate their cooperation. We believe this the State should support this process:

- **To adapt legal frameworks in favour of social economy enterprises.** To achieve effective progress, we believe it is important to strengthen the advocacy of organisations that represent the social economy to propose legislative reforms and create working spaces between SE representatives and the heads of public administrations of each MC. For the time being, the process is moving forwards very gradually. In Morocco, the ministry in charge of the SSE sector submitted the draft framework law to the General Secretariat of the government in July 2016. In Tunisia, the draft law on the social and solidarity economy is being discussed in the internal structures of the UGTT (Tunisian General Labour Union).
- **To set up a Consultation Committee in each MC** composed of the different competent departments (Crafts industry, Finance and Economy, Women...), agencies

(Social Development, National Council of Local Authorities, Microcredit Associations etc.) and existing SSE networks to discuss how to simplify administrative procedures.

- **To network SE structures** at national (and regional) level to pool resources and strengthen the capacities of SE initiatives (example of the success story of Divers' Etik in PACA in the Annex, box A5).

## **III. EuroMed cooperation can play a role in providing opportunities to unlock the potential of SE and create sustainable social entrepreneurship ecosystems to promote growth and inclusion**

In countries where they contribute to growth and employment, social enterprises are well structured with dedicated institutional, financial and support tools. Considering their proven effectiveness in countries/territories with similar social needs, we believe in their ability to boost social impact in the MC.

In Europe, **SE is widely supported through a multitude of tools and initiatives, contributing to sustainable growth and job creation.** In addition, the call for action of the European Commission's Expert Group on Social Entrepreneurship (October 2016) presented 13 recommendations to strengthen SE throughout the EU, which can be grouped into four categories: i. the first aims to **increase the visibility and recognition of SE**, ii. the second focuses on **improving access to funding** for social entrepreneurs, iii. The third concerns **the improvement of the legal environment** which governs and surrounds the SE and iv. the fourth recommendation has a more international perspective, namely to **stimulate international development and growth by supporting SE.**

Consequently, the group of experts has suggested that the European Commission should play a leading role in promoting global cooperation to support SSE and social enterprises. The EU should **act as a connector** to facilitate the exchange of knowledge and the dissemination of good practice.

To date, on the EuroMed level, the officially defined mechanisms (particularly institutional) for supporting and promoting SE exist but are not sufficiently developed.

Nevertheless, in the Mediterranean, there are quite a few general support mechanisms for entrepreneurship, whether national or regional, financed by the public or private sector, with domestic or foreign resources. This is why it seems to us that SE does not always have to be dealt with in parallel circuits. Of course, we do believe that it is necessary to structure the Mediterranean SE ecosystem through a long-term process. However, to we persist in considering SE as a separate sector, we accept that the rest of the economy is not bound by the values and responsibilities promoted by SE. It is also possible to consider entrepreneurs of all kinds as social actors and to encourage and reward those who really engage in maximizing their social and societal impact, so as to encourage other entrepreneurs to emulate them. FEMISE holds the view that all of the different models can contribute to the emergence of SE ecosystems in MC.

The first three recommendations of the EU expert group seem to us to be perfectly adaptable in the context of south Mediterranean countries (i.e. recognition, financing and improvement of the legal environment). The fourth recommendation of the expert group (stimulate

#### **Box 9. EU mechanisms and initiatives for SE**

*In 2015, the social economy in the European Union represented 10% of the European economy (GDP) and more than 11 million workers, equivalent to 4.5% of the EU's active population. Having understood the importance of SE as a tool for economic and social development in European countries, the European Commission (EC) launched the SE initiative in 2011.*

*The initiative is based on three main axes aimed at promoting SE in the field, first by **improving access to public and private financing for social enterprises**. On the public funding side, the Employment and Social Innovation Programme has been opened to social enterprises with the aim of supporting the growth of the social investment market to the tune of €85 million., as well as to facilitate social enterprises' access to capital through instruments such as loans, from 2014 to 2020. In the same way, States have allocated part of their budgets to the financing of social enterprises during the reform of their Structural Funds.*

*With regard to private sector investment, Europe has created the European Social Entrepreneurship Fund, an instrument used to improve social enterprises' access to financial resources while helping investors to select the most promising projects. The EC has created a new label in the Venture Capital Funds Regulation, entitled "European Venture Capital Funds". This will allow investors to market and extend these funds across the EU. In addition, the EC has monitored the development of social exchanges in order to create a European platform for the trading of shares in social enterprises.*

*In addition, the EC seeks to **improve the visibility of social enterprises**. To this end, it has set up the electronic platform Social Innovation Europe highlighting social enterprises*



That are considered to be innovative and whose potential is recognized. This platform also serves as a communication hub for social entrepreneurs and for sharing expertise and information on the latest developments in SE. In addition, EU-funded education-related programmes, such as Youth in Action, highlight the potential of SE, by including, training programmes, among others. In addition, the SME Forum, the first edition of which dates back to 2010, seeks to find collaborative and complementary solutions over the long term. This platform aims to improve dialogue and understanding between the traditional private sector, social enterprises and financial institutions.

National authorities are yet to understand the stakes and needs of the sector. The EC is thus seeking to clarify the characteristics of the sector in order to optimise national support for local and national ecosystems of social enterprises. This has led to the development of a "Guide to Social Innovation" to help national authorities improve their support mechanisms for SE, accompanied by technical assistance provided by the EC between 2014 and 2020. The EC is also working on the elaboration of a precise mapping of the SE, taking stock of the sector's situation. This project also collects reliable data on European SE to identify possible areas of intervention at the EU level to strengthen SE.

Finally, a major aspect of the initiative is **the optimisation of the legal environment surrounding SE**. In seeking to promote SE at national level, it is necessary to determine how authorities can legally take into account the specificities of social enterprises. In 2014, a series of measures relating to the reform of public procurement were adopted to encourage and empower public authorities to take into account the entire life cycle of products and services offered by social enterprises in their procurement decisions, while taking into account social criteria involved in the production process. The same logic

gave rise to the implementation of measures for services of general economic interest in 2011. They allow local authorities to gain flexibility and proportionality in the granting of State aid to social enterprises, "by raising the derogation threshold for the obligation to notify public service compensation in the EU to €500,000 per company over a three-year period". In addition, the EC has worked on the range of legal forms available to cater for the specific needs of social enterprises. It thus adopted a proposal on the European Foundation Statute with a view to facilitating cross-border activities of social enterprises and non-profit foundations. In addition to this project, which is currently being negotiated between the Member States, there is already another legal form available, entitled the European Cooperative Society. The project therefore aims to simplify its current form and to facilitate its use through public consultation..

To assess the impact of this initiative, the EC organised the event "Social Entrepreneurs - Take the floor" in Strasbourg on 16 and 17 January 2014. This event made it possible to define the actions to be implemented for the following years. One of these was a possible action at EU level, if research showed significant added value, to regulate Internet fundraising across Europe.. The EC also understood the need to research and update existing lists of SE structures to help them work together more effectively.

In addition, the EC encourages partnerships between social enterprises in Europe, in particular with social enterprises in the Mediterranean. This would make it possible to share the expertise of certain companies that are more technically advanced or have developed innovative and reproducible forms of management, to be adapted to the different local contexts. The Commission is therefore funding projects seeking to build bridges of collaboration between regions, including the MedUp project led by 4 European organisations, in particular OXFAM (Diesis, Impact



*Hub International, Réseau Euclid) and composed of 5 South Mediterranean co-applicants (Sekem Development Foundation, Tunisian Centre for Social Entrepreneurship, Enactus, Jordanian Hashemite Fund for Human Development, Agricultural Development Association) and 4 associated partners (Tuscany Region, Autonomous Region of Sardinia, Banca Etica, Association Imprenditrici and Donne Dirigés d'Azienda). The consortium operates in 6 countries in the MENA region (Morocco, Tunisia, Egypt, Lebanon, Jordan and Palestine) with the aim of promoting SE in the southern neighbourhood by providing complementary expertise in the field of social innovation. MedUP! Project, and seeks to increase economic inclusion and employment through appropriate SE policies, public-private dialogue and exchange of practices.*

*The EU also funds several projects led by regional or international NGOs to promote SE in Europe and within Euro-Med cooperation, sharing EU expertise in this field.*

international development and growth by supporting SE) is the one in which the Euromed partnership could be of great use to the countries of the South in supporting the development of SE.

Considering the reality encountered by social enterprises in the MPs and presented in the previous sections, in this part we propose **tools and recommendations that could be supported by all actors in the EuroMed partnership and that would help to overcome the obstacles identified:**

- i) at the macro level, **by contributing to the emergence of an SE policy environment**, raising awareness among public authorities of the existence of private actors providing support (financial and technical) for social impact,
- ii) at the meso level, **by improving the capacities of support and training structures**

**social entrepreneurship**, thanks to a complete MED mapping for the emergence of ecosystems with social and environmental impacts and

- iii) at the micro level, **by providing a sustainable business model and performance monitoring for SE** with high potential for competitiveness, job creation and social innovation.

#### **1. Macro level: Raise awareness, share experiences and develop strategies for a policy and regulatory environment favourable to SE**

The public authorities of MC can play an important role as facilitators of SE. They can provide a legal framework that specifies the financing to which companies are entitled and removes regulatory barriers to stimulate private investment with a social impact. They may also introduce tax incentive schemes.

The actions to be taken at the macro level must therefore:

- i. **raise awareness** and create a national dialogue between the main stakeholders of the social economy,
- ii. **define social impact performance indicators** that could be adapted within a national framework according to the strategic priorities of each country (youth employment, women's employment, etc.).
- iii. **connect SE stakeholders** from both shores and promote regional convergence in the political direction for social entrepreneurship.

#### **Proposal 1. Provide a National Framework and Social Impact Assessment Tools**

We believe that **a rating methodology to assess a company's social performance in terms of local impacts**

is necessary. A dialogue between social entrepreneurs, public authorities and support organisations could be launched in each country to define social impact performance indicators that could be adapted in a national framework according to the country's strategic priorities (youth employment, women's employment, etc.).

This framework/tool could then be transferred to the ministries and support agencies in charge of SE through technical assistance and training. It would enable public (and private) actors to better evaluate investment projects and contribute to the implementation of socially responsible and inclusive projects. In addition, it would allow

i. companies to know how to truly engage to improve the impact of their activities and ii. citizens and public or private organisations, to identify and promote the achievements of companies present in their territories

## **Proposal 2. Create National Advocacy Panels for Social Impact**

In each of the MC, the panel could include representatives of all the actors concerned by the SE, namely:

- public authorities, which will have a facilitating role by providing a legal framework for the sector, introducing tax incentives, etc.
- the banking and financial sector, which will be able to communicate on the tools made available to SE.

social Entrepreneurs who will have to proactively assess their social and environmental impact, allowing a real "reporting" of social impact and more visibility and transparency. They will also be able to communicate on the needs and obstacles they encounter.

- Impact Investment institutions that could set up a generalised system of social and environmental impact assessment.
- networks of economic and social science institutes, capable of presenting new tools from economic research, proposing new practices from social sciences, making the link between reflection and policy application by confronting researchers with the realities of social entrepreneurship.

Discussions could be based on presentations of best practices and Advocacy Panels could provide:

- First, the design of national "Social Impact RoadMap" roadmaps in close collaboration with the local authorities and
- Secondly, in collaboration with members of the GECES (Commission Expert Group on Social Entrepreneurship) to contribute to **the emergence of a real SE ecosystem in EuroMed**, coordinated without necessarily being closely regulated.

## **2. Meso level: map and empower the actors of the South Mediterranean social entrepreneurship ecosystem and connect them to the EU-MED scene**

The proposed actions to put SE in contact with intermediate support actors (meso level) are as follows:

## **Proposal 3. Carry out a mapping of social enterprises in the Mediterranean**

The potential of SE in the Mediterranean is still relatively unknown and needs to be quantified and inventoried. The activities of SE companies are not disaggregated in the National Accounts. To give a real boost

to social entrepreneurship we need, among other things, to **identify ES trends by activity, sub-region, identify jobs created and opportunities for inclusiveness**, through the preparation of satellite accounts. There is therefore an urgent need to build databases on SE in the Mediterranean to increase its visibility, better communicate around "social returns" and effectively orient support and funding to the right structures.

It is in the context of this objective that the EU launched, in 2009, a programme of satellite accounts for cooperatives and mutuals, in order to develop reliable statistics on this type of structure at national and European level. This approach has the advantage of offering a complete overview of the situation and economic potential of the structures (Production, Intermediate consumption, Value added creation, Compensation of employees, Gross operating surplus, Gross fixed capital formation, Borrowings, etc.) and it would be extremely useful if it could be extended, within the framework of EuroMed, for each of the MC.

This work could be done in two stages:

- i. the Mediterranean Statistical Offices would work on a harmonised statistical basis, to produce a regular (annual or bi-annual) publication of SE satellite accounts,
- ii. Satellite accounts would provide **a real SE EuroMed observatory** to maximize dissemination to stakeholders (private sector, public, academic research, social innovators, IFIs etc.))

#### **Proposal 4. Link the demand of social enterprises to the supply offered by financial instruments with a social impact**

The mapping could then feed a real **Platform of EuroMed SE Actors**.

This could include i. the overview obtained from SE structures in the previous step and ii. a map with all EuroMed structures supporting or financing SE, public or private (local support actors, international networks and financial institutions ready to invest in the region) as well as any other actor working for the development of the SE in EuroMed (e. g. academic research networks, etc.).

Social enterprises will need to rely more and more on private funding for their development. **We therefore believe that the development of a mechanism to match social impact investments with the needs of social entrepreneurship is appropriate.**

The system could be in the form of **a regional online platform** which would be adjacent to the EU's Social Challenges Innovation Platform presented in the box below. This online platform would use the mapping of intermediate support structures for SE in order to connect them with social entrepreneurs. The platform would be created in two stages, with a first registration phase **for intermediate social finance structures** followed by a second phase of registration for Mediterranean **social entrepreneurs**. When registering online, they could specify the characteristics of their social enterprise (size, sector, etc.), their clients, their objectives in terms of social impact, the challenges encountered, their traditional sources of financing, etc. The responses obtained could then be visualized in a digital map of the ecosystem. This map would allow match-making between social entrepreneurs and social impact financial structures. It would also provide a means for financial structures to better define

prioritize and support social challenges.

All this work could be carried out with the impetus of the EU on the basis of European co-financing (grant or call for tenders), and with a share to be borne by the national/local authorities concerned.

**Box 10. Social Challenges Innovation Platform: Platform for the Emergence of a SE Ecosystem**

*The "Social Challenge Innovation Platform" is a new platform set up by the EU in 2017. It aims to design, create and support an online ecosystem, encouraging interaction between social innovators and SMEs. It seeks to contribute to the development and adoption of sustainable and marketable innovations with a clear social impact. For example, the Social Challenge Innovation Platform:*

- supports European actors in defining and prioritising social and societal challenges*
- encourages the widest possible participation of social innovators, social entrepreneurs, start-ups and SMEs in identifying, developing and testing concrete solutions tailored to needs*
- provides grants, for actions that translate challenges into practical and marketable solutions*

*Social Challenges.eu is therefore a dual tool for social innovation, responding to both demand and supply and facilitating their collaboration in the development and implementation of projects adapted to different social needs. As one of the objectives of this platform is to define and prioritise social and societal challenges, collaboration between different stakeholders becomes a major asset to test concrete and collaborative solutions. The initiative thus aims to effectively exploit the potential of European start-ups and SMEs to generate both economic and social impact.*

**Proposal 5. Direct "traditional" business support mechanisms towards SE**

Moreover, there are already European tools to provide SMEs with financial support which could, it seems to us, also include the countries of the South Mediterranean and address social enterprises. For example, the Programme for the Competitiveness of Enterprises and SMEs (COSME) was set up to provide better access to finance for European SMEs through two dedicated financial instruments (available since August 2014). These instruments are managed by the European Investment Fund (EIF) in cooperation with financial intermediaries in EU countries. They have a budget of more than €1.3 billion and will be able to facilitate access to loans and equity financing for SMEs and produce leverage effects.

- **The Loan Guarantee Facility (LGF):** Part of the COSME budget is dedicated to the financing of guarantees and counter-guarantees for financial intermediaries (e. g. guarantee institutions, banks etc.) in order to help them provide more loans to SMEs. Due to the leverage effect, each euro invested in a loan guarantee is expected to release up to 30 euros of financing for SMEs. These guarantees help many SMEs that could not obtain financing because of their higher risk or lack of sufficient guarantees. Up to 330,000 SMEs are expected to receive loans supported by COSME guarantees, for a total loan value of up to €21 billion.

- **The Equity for Growth Facility (EFG):** Another part of the COSME budget is devoted to investments in venture capital funds. Fund managers working on a commercial basis ensure that investments are directed towards SMEs with the greatest growth potential.

One could imagine that an extended version of the COSME would target SMEs with a social aim/utility and SE. In particular, social enterprises in the MC could have access to the LGF loan guarantee. A new COSME mechanism with a social impact could therefore support Mediterranean financial intermediaries, provided that a specific percentage of the structures financed by the intermediaries are for social purposes.

### 3. Micro level: empower and monitor the performance of social entrepreneurs and contribute to their growth and inclusion potential

**With an appropriate social impact framework, public authorities in the MC would be able to select innovative and job-creating social enterprises to provide them with technical and financial support.** This could be done in partnership with the EU and also involving private sector actors. The proposed actions to be undertaken are:

#### Proposal 6. Create an ERASMUS for social entrepreneurship

In the MC, emerging social enterprises are often in shortage of know-how and good management practices. We believe that the creation of a specific ERASMUS for SE would be a measure to **cultivate entrepreneurial skills with a social impact in the Mediterranean.** It should be noted that a European exchange programme for entrepreneurs already exists, namely the Erasmus for Young Entrepreneurs programme, which enables future European entrepreneurs to acquire the skills required to create and/or manage a small business in Europe. A "tailor-made" version for the SE, which would include the MC and social enterprises, would allow new social entrepreneurs

from the South Mediterranean to acquire or exchange socially innovative entrepreneurial knowledge and ideas with an experienced entrepreneur from the North or another South country, where they could stay for a few months. The stay could be co-financed by the European Commission and the authorities of the Southern countries. It would be facilitated by local contact points (e.g. chambers of commerce, incubators, DLAs, etc.) and by networking, which could also be done via the Social Challenge Innovation Platform.

In addition to knowledge transfer, this would be a **mutually beneficial collaboration**, allowing, on either side the discovery of new markets and partners, new commercial practices and the development of a EuroMed relational network. The systematisation of this system could also go hand-in-hand with the creation of centres for the training of managers in SE, or the beneficiaries of ERASMUS SE could help to multiply training of future actors in sustainable development.

#### Proposal 7. Propose an EU- Med Mentoring Scheme for Social Entrepreneurship

Entrepreneurial Mentoring makes it possible to accelerate and secure the growth of companies with high development potential by transferring experience between entrepreneurs (see the example of Mowgli Mentoring in the Appendix, box A7). There are various such initiatives dedicated to companies with high development potential that operate "downstream" of business creation assistance schemes. These initiatives connect the future leader (mentee) with experienced entrepreneurs (mentors) and contribute to entrepreneurial success.



This process could also be applied to SE. The generalisation of training and mentoring workshops would empower a generation of social entrepreneurs with high potential for job creation and inclusive growth. A Euro-Mediterranean programme, which would bring together technical and financial support actors for social entrepreneurs with structures specialised in mentoring programmes, would allow training and mentoring for entrepreneurs to empower them for social impact. As with the Erasmus of Social Entrepreneurship described above, the relationship between mentee and mentor could be established via the Social Challenge Innovation Platform. Thus:

- New entrepreneurs from the MC would meet the selection criteria required by the programme (age, legal form of the company, having created its company in the South, having the objective of creating jobs and developing the local territory, etc.) and would apply to the Platform.
- The selected files would go before a Selection Committee that would validate the entrepreneurs. Then, the Platform would ensure the connection between the mentor and the young mentee entrepreneur.
- The mentoring would last 1 year, with at least one meeting per month between the young person and his or her mentor. Mentee entrepreneurs would also have access to a network of third-party experts.
- Mentee entrepreneurs would themselves become mentors at the end of the internship and could be connected via the platform with future mentees.

## Conclusion

For FEMISE, this work is part of an evolving and continuous process. Given the evolution of certain legislative frameworks, the emergence of new tools and structures and the appearance -

of new "success stories" that deserve to be known, this work would benefit from being updated on a regular basis.

However, this first analysis already provides a general overview and feeds into the reflection on future actions and programmes in the Mediterranean. In this sense, the box below completes the analysis and gives the floor to key FEMISE partners who offer their views on priority actions to be undertaken to better develop social entrepreneurship in the Mediterranean.

### **Box11. Which actions are priorities for the development of social entrepreneurship?**

*FEMISE interviewed some of its partners to elicit their proposals on actions they consider to be priorities for enhanced cooperation between social entrepreneurship structures, to better understand international good practices that could be transposable in the South Mediterranean context and to obtain an overview of the initiatives of their respective structures in promoting inclusiveness and social utility. Here are some excerpts from interviews with key actors in EU-MED social entrepreneurship.*

**Thomas Vailleux (French social entrepreneur based between Paris, Lyon and Beirut, co-founder of Friends of the Middle East):** *Not all South Mediterranean countries are equal in terms of the will of their political leaders and the development of social entrepreneurship. Nevertheless, it seems to me essential to adopt the sharing of regional good practices, feedback from the experience of*

networks and knowledge a *modus operandi*, a collaborative work methodology that reflects the values of the sector. The aim would be to set up a regional collaboration platform to foster exchange and strengthen cooperation between actors sharing common interests, in particular with a view to opening up to the regional market (through partnerships, exports, regional establishment, etc.). This platform could take the form of a web platform and a calendar of regional meetings targeting objectives already identified as key by actors such as the Lebanese regional think tank *Beyond Reform & Development*.

At the level of support structures, innovative and effective methodologies have been invented or reinvented to equip social entrepreneurs and professionalise the specific and dual approach of a social entrepreneur (social vs business). These methodologies driven by high-growth support structures, working with public and private sectors, such as *MakeSense* internationally or *Ticket for Change* in France, whose founders have been rewarded on several occasions. In addition, the introduction of legislative measures to facilitate the creation of a social enterprise and reduce the taxes imposed on the project leader because of the social nature of the company, in Italy and France for example, seem to be essential to change the scale of the sector. Finally, in the pioneering countries of the sector, telling the stories of solutions and project leaders quickly became a way of bringing together communities of "changemakers" who share a common vision of the world and put them into action.

*Friends of the Middle East* is an association based in Paris and Beirut for which one objective is to share another image of the region through the stories of its citizens experiences,

In particular those of social entrepreneurs. Through our documentary film project ("*Change-makers in the Arab World*"), we promote the inclusion of disadvantaged audiences by representing them in our film. Our partnerships with NGOs and local and regional foundations will enable young people in disadvantaged areas to grow awareness with the aim of removing them from violence and extremism and bringing them closer to "doing together". Our "projections-action" program!

» in several countries, is designed to engage spectators at the end of the screening, through problem-solving workshops and networking with ecosystem stakeholders.

**Shadi Atshan (Palestinian entrepreneur and co-founder of Leaders Organization and FastForward Accelerator)**

: Facilitating the development of the structure of social entrepreneurship as a whole, and more particularly in South Mediterranean countries, should be a priority on three levels, starting at the global level and moving towards strategies at the micro level. A national strategy should be designed to spread the idea of social responsibility and create positive spin-offs through the activity of profitable start-ups throughout the region. Once this strategy is in place, workshops and conferences should be introduced in each country to create and target existing social gaps in the economy and create cost-effective solutions. Finally, incubators, accelerators and associations related to entrepreneurship should include tailor-made programmes that particularly target social entrepreneurship and provide the necessary training and mentoring to encourage the creation of potentially viable start-ups.

Two international good practices that can be found directly in social entrepreneurship

initiatives, and which lead to the creation of new companies in the South-Med region, are recycling and the transition to solar energy. These best practices ensure increased efficiency, lower cost and greater long-term sustainability for the region as a whole. Moreover, they encourage young entrepreneurs to create new start-ups focused on social progress. In order to facilitate such an environment of sustainability and creative thinking, it would be desirable to have (i) research and development programs to encourage entrepreneurs to create innovative ideas and new products, (ii) a network of international experts in the field to help start-ups receive the mentoring and advice they need; and, (iii) a network of business-Angels in the region to invest in entrepreneurs, including social initiative start-ups, to enable them to develop and create positive long-term effects.

Social inclusion and social utility are among the main initiatives of Leaders Organisation, and therefore among the programmes undertaken by the organisation is the Accelerator of Social Enterprises (ASE). The concept emerged due to the lack of support for social enterprises, for which the accelerator is supposed to find sustainable solutions. Particular emphasis has been placed on targeting women and youth, with the ambition and potential to create sustainable social enterprises that will have an impact on their communities, which benefit from an innovative and extensive support programme. This project goes even further in promoting engagement; women and youth from underprivileged communities with potential identity issues (in society, politics, the economy and the environment) develop their own social enterprises and receive support. The program has provided training to more than 150 entrepreneurs aged

Between 22 to 30 years old, and has welcomed and supported 7 start-ups, with a participation rate of 42% among women.

**Emmanuel Noutary (General Delegate of ANIMA):** First, recognise social entrepreneurs, be able to identify, setting aside the legal status of companies, those that deserve that of social enterprise but do not enter within this scope. An ex ante evaluation of the social and solidarity impact of entrepreneurs will allow the targeting of the most effective projects, beyond a simple verification of eligibility on a statutory basis. This assessment is also a useful tool for the entrepreneur, as it highlights the strengths of a project and areas for improvement. ANIMA has implemented practical training courses targeting public officials and/or project leaders, and has noted the inadequacy of existing evaluation methods. ANIMA has therefore developed a tool for rating the local impacts of companies as part of the EDILE initiative funded by the EU in 2013-2016, which has been labelled by UfM. This tool proposes 35 evaluation criteria, rated from 1 to 5, to provide a performance measure for four dimensions: economic, social, environmental, community. pending on the objectives targeted, evaluators may choose to use only certain criteria, for example: "subcontracting and local purchasing"; "direct job creation" etc.

Second, develop incentive schemes reserved for those assessed as social entrepreneurs. These schemes could have different forms: i. The development of brands, labels or other mechanisms, including legislative ones, to improve the visibility of SSE is a first positive corollary of the evaluation, and helps to enhance the social value of the entrepreneur. The role of the public sector in initiating or supporting these mechanisms is essential, ii. Financial tools such as medium/long term capital investment; mezzanine loans

can also reward the societal impact of these companies. The enhancement of these financial products can be subsidised by public donors, this bonus being compensated by a better overall return on investment (jobs created, etc.), iii. structures and programmes to support entrepreneurship (incubators, accelerators, mentoring programmes, seed grants) should reserve places in their programmes for social entrepreneurs, again with preferential conditions due to a higher impact on value creation for the territories. Finally, tax measures can reward the creation of social added value by companies.

**Tallie Hausser (Strategic Director of NUImpact, Researcher in Social Entrepreneurship at Northeastern University):** Beyond the need to have social impact investors in the MC, financial leaders in these countries should be encouraged to better address the issue of social impact investment and to collaborate with community leaders such as the Tunisian Centre for Social Entrepreneurship or Lab'ESS. Intermediate financing" is a major problem in countries such as Lebanon and Morocco, as social entrepreneurs can receive up to \$400k of investment from local impact actors (such as Alfanar in Lebanon) while foreign investors are used to invest at least \$1 million. Nevertheless, investments of between \$400k and \$1 million are the key to the expansion and sustainability of social enterprises. The consideration of financial mechanisms such as SIBs and Green Bonds should also be encouraged.

Interest in social entrepreneurship is growing, but for the ecosystem to thrive, dedicated support communities must be encouraged and maintained. It should be noted that: i. there is great need for

specialised lawyers in MC. Lawyers would do well to specialise in supporting innovative and social organizations, which have specific and growing legal needs, ii. Another key action is to encourage education stakeholders to integrate social entrepreneurship courses into their curricula. Institutions such as the Mediterranean School of Business (MSB) in Tunis and the American University of Beirut (AUB, FEMISE member) have developed impact programmes, enabling students learn about social innovation in their business courses. More generally, since young people are the future stewards of Mediterranean growth and its sustainability, social entrepreneurship should be a concept discussed in all institutions, local engineering schools, medical programmes etc..

Finally, in ecosystems that reach a new level of social innovation development (as in Jordan), the next step is to actively start reaching entrepreneurs from the most marginalised communities. The aim would be to attract innovators from rural, minority or otherwise under-funded populations. The ecosystem will gain when those who feel the pain of inequality and the failure of traditional markets become a part of innovative and inclusive mechanisms.

**Patrizia Bussi (coordinator of the European Network of Work Integration Social Enterprises (ENSIE) based in Brussels):** I believe that it is necessary, in each country of the South Mediterranean, to look for existing social entrepreneurship and social economy structures, helping them to work together so that they gain visibility and be recognised at national level, and so that they can cooperate to unlock the untapped potential of their territories. Following



Following these important steps, cooperation must be built between all the structures of the South Mediterranean.

The identification of international good practices that can be transposed is not a simple task. Some practices have already shown their success, such as the Incorpora programme in Morocco, or certain activities with a social impact in Tunisia, launched by the French group SOS. These experiences confirm the importance of taking into account territorial realities (economic, social, historical, cultural) and adapting international best practices to these realities.

The ENSIE network represents, supports and develops networks and federations of Work Integration Social Enterprises-WISEs in Europe.). It includes effective tools for access to social and professional reintegration into the labour market and for the social inclusion of vulnerable groups. The 2016 "WISE Impact Study" examined the case of 807 WISEs, present in 9 European Union countries and including 12,954 disadvantaged workers. The study found that 48.5% of disadvantaged workers were able to find a job in the same company, in another WISE or in the traditional labour market, while 16.5% became self-employed entrepreneurs or found vocational training leading to a qualification.

**Ada Bazan (International coordinator of the "Femmes du Monde: un réseau d'entrepreneures solidaires" network at Quartiers du Monde):** In the case of Morocco, SSE institutional structures should take ownership of SSE values and principles in order to promote them among local associations that support women in the development of income-generating activities (IGAs), donors and chambers of commerce.

They should support civil society initiatives to foster social and solidarity-based entrepreneurship.

While the private sector is creating entrepreneurial incubators (Casablanca and Rabat), bilateral financing (World Bank, British Council, USAID, CTB, GIZ, AFD) supports (private) entrepreneurship for women and young people, SSE is remains the poor relation of the economy. The promotion, among institutional and financial actors, of social and solidarity-based entrepreneurial incubators with a gender perspective that enables women to take their full place in the socio-economic and political development of their country is important.

**Sami Mouley (Professor at the University of Tunis):** Alternative types of budgetary support for the financing and support of SSE should be explored in Tunisia. The law targeting the promotion of this sector in France, with the assistance of the Caisse des Dépôts group or the public investment bank managing a social innovation fund, can be transposed to Tunisia with the assistance of the Caisse des Dépôts et Consignation Tunisienne.

Other innovative financing can be undertaken, using Islamic and solidarity finance tools (cooperative and citizen banks), through a public-private partnership or as part of an exclusive partnership with the private sector within the new dynamics around the concept of corporate social responsibility (CSR) and socially responsible investment (SRI).

In addition to the interventions of microfinance institutions (MFIs), crowdfunding associations may also be an alternative. In addition, there is the Caisse des Prêts et de Soutien des Collectivités Locales (CPSCL),



under the co-supervision of two Ministries, the Ministry of the Interior and the Ministry of Equipment, Housing and Development. This fund could contribute, through the mobilisation of external or internal financial resources (loans on loan from the State or bond loans to the financing of local and regional development programmes, as well as to the assistance of local authorities and communes in the implementation of local projects, in the form of public-private partnerships (PPP) with ESS structures.

**Nadine Richez-Battesti and Francesca Petrella (Aix-Marseille Université and LEST-CNRS):** There are already some support mechanisms for social entrepreneurship and SSE on the EuroMed level. Regional CoopMed, which strengthens the financial capacities of microfinance, and SEED Euromed, which facilitates exchanges between social entrepreneurs in the Mediterranean, are two mechanisms that support social entrepreneurship on a Euro-Mediterranean scale.

CoopMed, the leading investment fund for the development of the Social and Solidarity Economy (SSE) in the Mediterranean, had a capacity of €10.5 million at its launch in February 2016. It aims to reach €20 million. This fund is managed by Impulse, a Crédit Coopératif subsidiary management company. CoopMed offers medium- and long-term financing in the form of senior or subordinated loans. The financial offer is accompanied by technical and financial engineering expertise in order to consolidate strong partnerships with local actors, financial stakeholders such as microfinance institutions, local banks, mutuals or other non-banking financial institutions..

SEED Euromed is a European Union-funded programme to promote mutual learning and

New entrepreneurs are

offered the opportunity to acquire or exchange entrepreneurial knowledge and ideas with an experienced social entrepreneur, with whom they stay for a period of up to 3 months. This program also develops social entrepreneurship BOOTCAMPs with 4 days of training and intensive practice of innovative methods and tools in social entrepreneurship supervised by international experts.

The Euro-Mediterranean partnership could contribute to strengthening the skills of project leaders, particularly young people, raising awareness among governments in different countries to strengthen legislative and regulatory frameworks for SSE, and developing financial tools dedicated to the social and solidarity economy and social innovation. It could also contribute to strengthening exchanges of "good practices" between countries of the South and between countries of the South and the North at these different levels and to a better understanding of the dynamics under way.

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## Appendices

Table A. Multidimensional Poverty Indicators (MPIs), by MC											
	Year	Population shares (%)		Multidimensional poverty				Population vulnerable to poverty (who experience intensity of deprivations)		Population in severe poverty (with intensity higher than 50%)	
		Urban	Rural	Multidimensional Poverty Index (MPI = H*A)		Headcount ratio: Population in multidimensional poverty (H)		Urban	Rural	Urban	Rural
Urban	Rural	Urban	Rural	Urban	Rural	Urban	Rural	Urban	Rural		
Range 0 to 1				% Population		% Population		% Population			
Algeria	2012/13	63,3	36,7	0,003	0,011	0,7	2,7	2,9	8,1	0,0	0,4
Egypt	2014	37,2	62,8	0,008	0,017	2,1	4,4	1,0	8,0	0,3	0,5
Jordan	2012	81,8	18,2	0,006	0,007	1,7	1,8	0,5	1,6	0,1	0,0
Morocco	2010/11	54,8	45,2	0,009	0,139	2,4	31,2	3,9	22,0	0,2	10,0
Palestine	2014	74,5	16,6	0,004	0,003	1,1	0,9	6,7	2,6	0,1	0,0
Syria	2009	54,8	45,2	0,011	0,023	3,0	6,0	4,0	9,1	0,2	0,7
Tunisia	2011/12	65,8	34,2	0,000	0,012	0,1	3,2	0,7	8,3	0,0	0,2
Source: Alkire, S. and Robles, G. (2016) “Multidimensional Poverty Index Winter 2016: Brief methodological note and results.” Oxford Poverty and Human Development Initiative, University of Oxford, OPHI Briefing 44.											

**Table B. An overview of the main SE structures in five MPs**

	Morocco	Tunisia	Egypt	Algeria	Lebanon
Associations	<p>120,000 associations</p> <ul style="list-style-type: none"> <li>• More than 15 million members</li> <li>• 1.5% of the Active population is employed directly</li> </ul> <p>• MAD8.8 billion of ressources</p> <p>12 Moroccan consumer associations (AMC)</p> <ul style="list-style-type: none"> <li>• 900,000 active customers</li> <li>• More than 6,000 employees</li> <li>• creation of one million micro-entreprises in 10 years</li> </ul>	<p>19,716 associations (19,8% in Tunis)</p> <ul style="list-style-type: none"> <li>• 23.4% in the development</li> </ul> <p>Of schools, 17.8% cultural and artistic, 11.6%</p> <p>In charity and social actions 10% in development</p> <ul style="list-style-type: none"> <li>• More than 10,000 new associations created</li> </ul> <p>Over the 5 last years</p> <ul style="list-style-type: none"> <li>• More than 12 million members</li> </ul>	<p>41,400 associations (NGO)</p> <ul style="list-style-type: none"> <li>• 23% in cultural, scientific and Religious services, 19% in social assistance, 14% in local community development</li> </ul> <ul style="list-style-type: none"> <li>• EGP 1.5 billion in expenditure</li> <li>• More than 3 million members</li> <li>• 101,825 employees</li> </ul>	<p>108,940 associations (10.7% in Algiers)</p> <ul style="list-style-type: none"> <li>• 21.5% in Neighbourhood Committees, 16.6% in Sports &amp; Physical Education, 15.3% in parents associations and 14.7% Religious associations</li> </ul>	<ul style="list-style-type: none"> <li>• Hybrids such as social enterprises exist in Lebanon but are not recognised as such</li> </ul> <p>Latest data of the Beyond Reform and Development report,</p> <p>«Mapping of Civil society organisations in Lebanon» (2015), shows that there are around 1.3 associations per 1,000 inhabitants in Lebanon</p> <p>The minister of the Interior and Municipalities declared that 25.4% of the organisations engage in lobbying and consulting</p> <p>46.8%</p> <p>In awareness raising, 37.1% in local capacity building</p>
Cooperatives	<ul style="list-style-type: none"> <li>• 15,700 cooperatives ( 2,287 run By women).</li> <li>• 450,000</li> </ul>	<p>Dissolved and transformed Into mutual companies</p> <p>In accordance with</p>	<ul style="list-style-type: none"> <li>• 18,000 cooperatives</li> <li>• 12 million members</li> </ul>		

	<p>members</p> <ul style="list-style-type: none"> <li>• more than 25,000 employees</li> <li>• more than MAD 6</li> </ul> <p>Billion of cumulated turnover</p> <ul style="list-style-type: none"> <li>• MAD17 Billion of capital</li> <li>• 66%in agriculture, 14% in crafts 9% in housing, not very high added value activites</li> </ul>	<p>The first article of Law19/63 of du 27 mai 1963, amended by Law n° 94 of 18 October 2005</p> <p>Agricultural service cooperatives become “mutual companies for agricultural services” (SMSA</p>	<ul style="list-style-type: none"> <li>• Trade value EGP 17.8 Billion</li> <li>For 5,000,000 jobs created</li> </ul>		<p>46.8%</p> <p>In awareness raising,</p> <p>37.1% in local capacity building</p> <ul style="list-style-type: none"> <li>•</li> </ul>

Mutuals	<p>50 health mutuals</p> <ul style="list-style-type: none"> <li>• 4 million beneficiaries</li> <li>• 5 billion Dirhams of contributions</li> </ul>	<p>Health mutuals santé</p> <ul style="list-style-type: none"> <li>• 41 Mutuals</li> <li>• 17 in The public sector, 13 parapublic and 11 private Basic agricultural service mutual companies</li> <li>• 151 agricultural service mututals</li> <li>• 60 in the collection and Trade of milk , 32 in the commercialisation And supply of cereals regrigeration And packaging ; the rest</li> <li>Work in different sectors, ,mainly supply of fertilizers, seed</li> <li>And pesticides. 28,000 members</li> <li>40,000 to 55,000</li> </ul>	<p>Sector not/ Very little developed</p>	<p>4% of dissemination of optimal practices, 3.6%</p> <p>Legal support for underprvileged groups, 3.6% surveillance of local and National government, 8.5% policy development, 18.1% humanitarian aid</p> <p>28.6% services, 5.6% research 12.5% dissemeniation Abd sharing of information and 38.3% implementation of development projects</p> <ul style="list-style-type: none"> <li>• Sectors most represented Social services and development (12.9%), Human rights(8.9%) education(6.5%), health (6.5%) environment (5.6%).</li> <li>• Main beneficiaries: women (40.3% Of programmes), youth from 19 to 24 years(39.5%), Lebanese citizens (33.5%), Children of 13 to 18 years old (30.6%) and refugees(23.8%).</li> <li>• More than 74% of organi-Civil society organisations</li> </ul> <p>Have a budget of less than US\$ 250,000 and only 6.3% have a budget of more than one million dollars</p>
		<p>around 1% of GDP</p>		

		•			
		•			
SSE	<ul style="list-style-type: none"> <li>• 1.5% - 2% of GDP</li> <li>• 3% of the Active population</li> </ul>	•	7% - 8% of GDP		
	Employed di- recly				



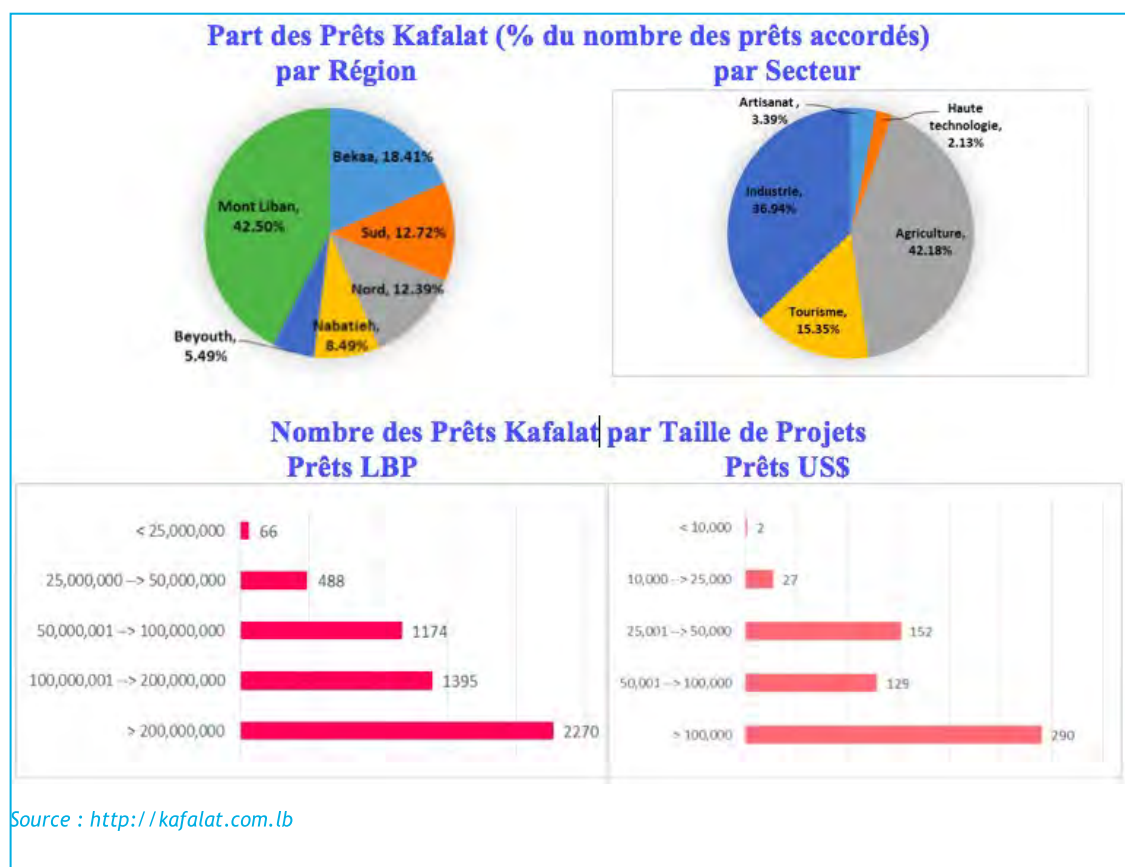
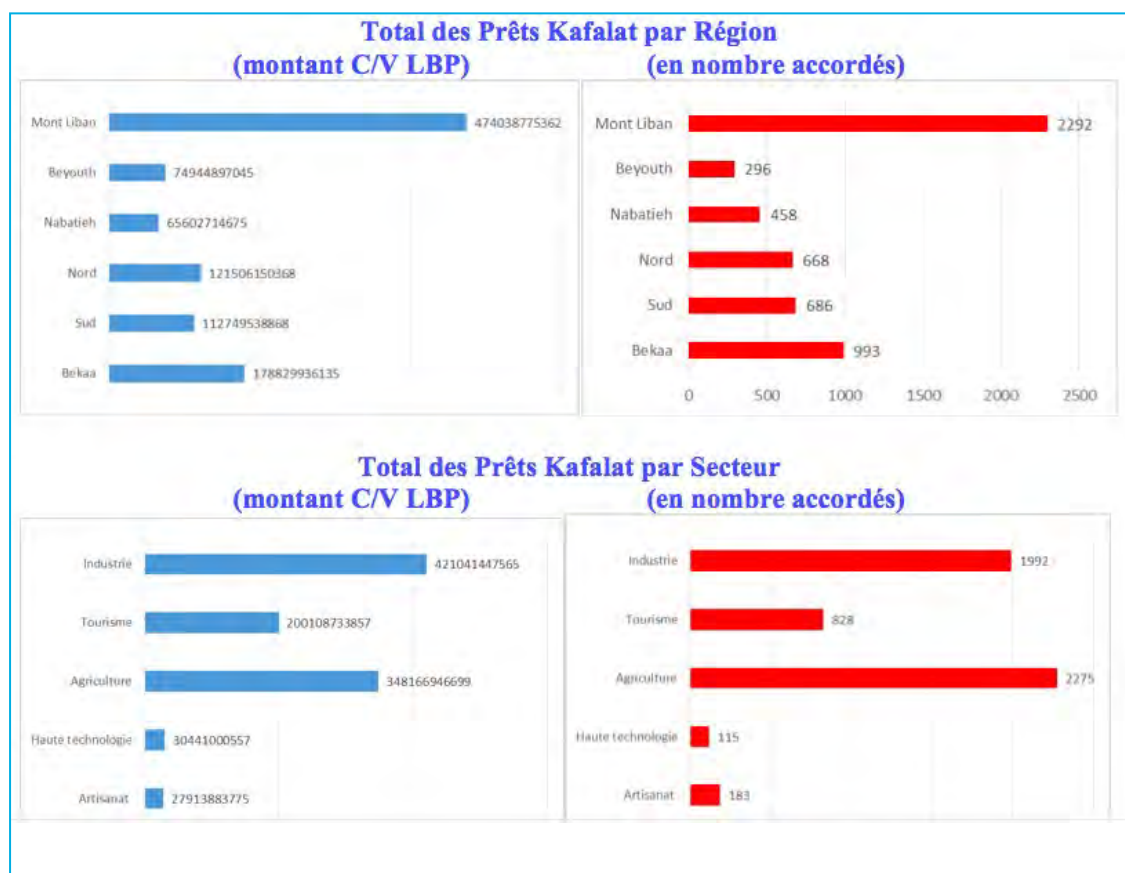
**Table C: The main characteristics of Moroccan cooperatives**

<b>Cooperatives by sector (end December 2015)</b>			
<b>Sector</b>	<b>Number</b>	<b>Members</b>	<b>Capital in MAD</b>
AGRICULTURE	10 542	355 343	1 546 586 107
CRAFT INDUSTRY	2 497	35 584	121 875 157
HABITAT	1 146	50 361	4 748 761 961
ARGANE	299	7 448	2 332 326
FORESTS	236	9 899	9 135 038
FOODSTUFFS	236	2 306	851 851
MEDICINAL PLANTS AND AROMATICS	157	3 715	3 595 668
FISHING	153	5 562	7 499 668
LITERACY	122	1 148	1 480 984
OTHERS	347	12865	28054412
Total	31 509	968 983	12 941 719 544

<b>Women's cooperatives by sector (end of December 2015)</b>			
<b>Sector</b>	<b>Number</b>	<b>Members</b>	<b>Capital in MAD</b>
CRAFT INDUSTRY	987	13 965	7 379 626
AGRICULTURE	763	13 835	6 724 659
ARGANE	274	7 117	1 877 126
FOODSTUFFS	170	1 766	597 501
MEDICINAL PLANTS AND AROMATICS	35	699	187 300
LABOUR	13	101	20 850
RETAIL TRADERS	10	70	20 750
FISHING	8	178	55 300
LITERACY	8	59	102 600
FORESTS	7	127	26 400
CONSUMER	3	22	12 400
PRINTING-OFFICE SUPPLIES	1	7	700
ART AND CULTURE	1	14	7 000
Total	2280	37 960	17 012 212

Cooperatives by region (end of December 2015)			
Sector	Number	Members	Capital in MAD
FES-MEKNES	1 835	36 202	417 055 382
CASABLANCA-SETTAT	1 780	76 958	2 313 779 800
RABAT-SALE-KENITRA	1 667	45 741	930 703 447
TANGER-TETOUAN-AL HOCEIMA	1 486	39 162	395 063 655
MARRAKECH-SAFI	1 407	71 558	594 782 006
SOUSS-MASSA	1 395	38 113	869 377 020
LAAYOUNE-ASSAKIA AL HAMRA	1 293	11 357	12 924 593
ORIENTAL	1 215	53 227	525 896 669
BENI MELLAL-KHE-NIFRA	1 203	57 134	255 545 158
GUEL MIM - OUED NOUN	1 157	11 015	58 555 720
DRAA-TAFILALET	999	41 283	93 139 823
EDDAKHLA-OUED ED-DAHAB	298	2 481	3 349 900
Total	15 735	484 231	6 470 173 173
Source : REMACOOOP (2016)			

Figure A. Operating loan portfolio of Kafalat S.A.L. (Lebanon) as at 31-12-2017)



Source : <http://kafalat.com.lb>

**Box A1. Social entrepreneurship: no consensus, but multiple definitions of the term**

Overall, we can identify four analytical approaches to social entrepreneurship.

**United States : The legal form of a social enterprise is of little importance**

In the United States, there is no legal form at the national level for social entrepreneurship and the development of social enterprise is not closely linked to any state support. Instead, social enterprise emanates from the private sector and civil society. The focus is on income generation to support a wide range of social commitments aimed at improving people's well-being and societal inclusiveness. In addition, social enterprises in the USA can be non-profit and for-profit.

American schools of thought on social entrepreneurship are divided into two currents:

**i. The social innovation school of thought:**

Here, social entrepreneurs are people who address social problems and meet societal needs in an innovative way. As Dees and Battle Anderson (2006) noted, this school of thought "is focused on developing new and better ways to approach social problems or meet social needs", social entrepreneurs who thus create a for-profit or non-profit enterprise. This school of thought is rooted in business entrepreneurship and in the discovery, evaluation and pursuit of opportunities. In the case of social entrepreneurship, "these opportunities are found in social needs, which are recovered through innovative means to satisfy them" (Braunerhjelm and Hamilton 2012).

**ii. The Social Enterprise School of Thought:**

Here, the main subject is the company, described as entrepreneurial and non-profit, producing "profit" while contributing to a social mission. In order to ensure continuity in the provision of a social service, this type of enterprise focuses on the production of income flows that are independent of subsidies and aids. In addition, this school promotes the idea that the adoption of innovative management methods can improve the effectiveness of non-profit organisations, making them more entrepreneurial (Defourny and Nyssens, 2010b).

In short, managerial innovation and the flexibility of the legal form of a social enterprise characterise the American tradition. Non-profit social organisations generate income through the internal sale of goods and services. Sales activities can be organised by a for-profit or non-profit subsidiary (for reasons of tax exemption while engaging in economic activity). Several authors (Ferris and Graddy 1989, Sala i Martin 1997, Scotchmer and Benschoten 1999, etc.) point out that non-profit organisations are becoming more and more commercial. As a result, the boundary between non-profit organisations and traditional businesses is becoming difficult to distinguish (Dart, 2004). Other authors have even described social enterprises as hybrid organisations located halfway between purely philanthropic and purely commercial entities (Emerson and Twersky 1996, Dees 1998).

**Europe: The importance of governance**

In Europe, depending on the country, there are different legal forms of social enterprise for non-profit and non-profit purposes (charities/associations) (Borzaga and others 2001). However, "the cooperative" seems to be the most widespread legal form. In some EU countries, where allowed by the law,

permettent, the associative form may also have a commercial component. For example, a non-profit association in Germany may carry out an economic activity if it is secondary to the main non-profit purpose. German associations have the obligation to produce a profit and loss account, so that the tax authorities can verify the non-profit nature of the entrepreneurial activity.

The governance of the organisation is of great importance in Europe because of its valued role in the democratic transition of the economy (Defourny and Nyssens, 2010b). The European social enterprise thus focuses on autonomous development, decision-making that is independent from ownership of capital and the participation of several stakeholders in the governance of the organisation.

In terms of autonomy, European social enterprises are established and controlled by groups of citizens, rather than by the public sector or private entities. Moreover, alliances between the public and private sectors are not part of the conceptualisation of a social enterprise, even if social enterprises can receive funding from public and/or private sources. Social enterprises are governed by democratic participative principles, based on the concept of decision-making by "individual vote" (one-man, one-vote). As such, social enterprises do not recognise other types of organisations, such as commercial companies, as social enterprises.

There are two European schools of thought on social entrepreneurship, each emphasising the participatory dimension ; these are:

#### **i. The EMES (EU) approach:**

Here, the social enterprise has an explicit goal that is to benefit the community. It is initiated by a group of citizens and is characterised by a high level of autonomy. It is participative

By nature and does not base decision-making authority on the ownership of the capital. This approach is the result of the work of the EMES (Emergence of Social Enterprise in Europe) research network ; researchers cooperating for the emergence and growth of social enterprises within the European Union. According to this approach, the organisations recognised as social enterprises are mainly associations, cooperatives, mutuals and foundations. Unlike the US school of social enterprise, in which a constraint of non-distribution of profits exists, the EMES approach provides for a kind of distribution of profits because of the inclusion of cooperatives (Defourny and Nyssens, 2010b).

#### **ii. BRITISH approach (UK) :**

This approach comes from the English Social Enterprise Unit of the Department of Trade and Industry (DTI), launched when the Labour Party came to power in the United Kingdom in the late 1990s. It was set up to stimulate partnerships between civil society, the public sector and the private sector. Here, the DTI defines the social enterprise as a company with a social purpose e. It produces a surplus, but reinvests this surplus mainly in the company or in the community, to enable it to achieve its social objectives. In 2004, a new legal form was introduced: the Community interest company.

The British government has thus actively participated in the creation of an environment conducive to the development of social enterprises. Unlike the EMES approach, the goods and services provided can be either independent or central to the company's mission. British social enterprises can trade freely in the market.



**Box A2. Two South-Mediterranean centres specialising in the question of SE in the Maghreb: the "Moroccan Center for Innovation and Social Entrepreneurship" and the "Algerian Center for Social Entrepreneurship".**

Several local initiatives from the private sector and civil society seek to highlight SE as an innovative and unconventional response to social problems, especially in view of the ineffectiveness of the few state initiatives in the South-Med region. This box outlines the role of two SE centres in the emergence of this sector. A travers leurs activités ciblées, durables et complémentaires, ils facilitent le développement des entreprises sociales dans deux pays. Through their targeted, sustainable and complementary activities, they facilitate the development of social enterprises in two South Mediterranean countries in the short and long term.

On the one hand, the Moroccan Center for Innovation and Social Entrepreneurship (MCISE), founded in 2012 by a group of 17 civilians, is one of the most successful social business centres and incubators in the region. The MCISE slogan summarises the SE promotion process adopted by the centre with a view to social change in Morocco and even in the region. This non-profit centre places public good issues at the heart of these initiatives for social change and seeks to provide financial and technical support to Moroccan social enterprises. To rethink the Moroccan economy by promoting a more ethical aspect based on social values, MCISE seeks to find innovative responses to socio-economic challenges. A three-step approach has been designed to enable optimal results for the centre's interventions: Inspire, Learn and Develop.

This is how MCISE organises events around the different stages of the establishment and development of a social enterprise. To support of high-potential social entrepreneurs in May 2015 this Moroccan Centre for Innovation and Social

Entrepreneurship set up its start-up incubator Dare Inc., based in

Rabat. The main purpose of this incubator is to promote young social enterprises and support them from the idea stage to the marketing of their product. MCISE has also set up a seed fund that allows start-ups to be financed at an earlier stage than for traditional investors. Other initiatives are also being implemented to provide financial support to social enterprises. Crowd Day is an example of an event that brings together local and international experts around crowdfunding to raise awareness among local and regional entrepreneurs on the modalities and different collaborative financing platforms. In exchange, MCISE takes a stake in the company either by making the incubator a shareholder of the company or by collecting a percentage of the start-up's turnover as soon as it becomes profitable.

In addition, MCISE is partners with several other organisations to allow social entrepreneurs to share a variety of expertise and sources of funding but also to enable them to develop their creative ideas with optimal resource allocation. With partners such as the Drosos Foundation or the National Endowment for Democracy, most social problems are covered by the MCISE network, providing adequate and specialised assistance relative to the contexts of each sector and the needs of each entrepreneur. To promote exchange between the various SE stakeholders, the Moroccan centre also created a co-working space on 30 June 2015. The Dare Space serves as a workplace and also a place of training around innovation, entrepreneurship and other related themes. These training courses, together with networking opportunities, should allow Moroccan social enterprises to gain legitimacy in the Moroccan entrepreneurial environment.

The Algerian Center for Social Entrepreneurship (ACSE) shares the same ambitions in terms of

*Out-of-the-box solutions to overcome the major obstacles to development and socio-economic prosperity in Algeria. ACSE is an NGO founded in 2013 by a group of 9 people with the aim of transforming the challenges and obstacles of Algerian development into opportunities for SE and young entrepreneurs. With the aim of creating sustainable jobs, boosting vulnerable regions, protecting the environment, promoting equity and inclusiveness and facilitating access to culture, ACSE organises a series of workshops, conferences and capacity building sessions designed to train entrepreneurs, connect them with potential investors and guide them in managing their businesses and making decisions. In addition, ACSE assists social enterprises in their development by following a procedure in 4 steps that are key to the operation of an SE incubator. First, the centre seeks to identify Algerian social enterprises that are often unknown. Mapping the different social enterprises would thus allow the promotion of possible partnerships and the creation of more accessible and efficient networks. Second, ACSE seeks to inspire young entrepreneurs to engage in SE by promoting it through partnerships with the media and social networks. It thus uses TedX conferences, which present the advantages of social enterprises and their potential impacts on the socio-economic situation of local populations and holds social enterprise competitions. These incentives are often supported by the third stage of assistance to social entrepreneurs, which is the technical support provided to young entrepreneurs. Through assistance programs, ACSE offers coaching, mentoring, training, sharing of expertise and skills development with the participation of national and international entrepreneurs. Finally, ACSE seeks to effectively connect social enterprises to enable a more optimal sharing of resources, information and more successful collaborations in projects.*

*To this end, the centre has created an online and offline*

*ACSE Community linked to global SE and innovation movements.*

*In addition, the activities carried out by ACSE are in the form of one-off repetitive events with previously fixed frequencies. For example, Connect WEEKENDS consists of a networking meeting throughout the weekend with associations, NGOs and social enterprises in Algeria. This informal meeting aims to strengthen the ACSE network and the potential for collaboration while creating an environment for sharing experiences and expertise. One or two participants in this meeting would then be invited to hold a round table organised by ACSE,*

*"Entrepreneurial Cafe", for young Algerians in order to share their projects, initiatives and experiences and promote SE. ACSE also sets up training and micro-trainings throughout the country with social entrepreneurs, as well as with young Algerians at the university or in schools, to informally introduce them to SE, social problem solving and social innovation. Training can also be specific to certain tasks in social enterprise such as HR management, event planning, communication strategy development, etc. or fundraising campaigns..*

*Consequently, this type of centre provides social entrepreneurs with technical support and access to networks, essential for the development of their businesses in the socio-economic context of South Mediterranean countries such as Algeria and Morocco. In the long term, their isolated but sustained and repetitive initiatives make for a very promising future for SE in these countries, with the creation of a SE culture and a trend towards the discovery of innovative tools stemming from society and possibilities for the resolution of the least invested social difficulties.*

**BoxA3. Beyond reform and Development: a key Lebanese actor with a strong social impact**

Beyond Reform & Development (BRD) is a consulting firm focused on social missions specialised in strategic research, public management, capacity development and partnership building. BRD is a member of Beyond Group, including Beyond Consulting & Training. This group has been supporting the leadership, modernisation and organisational development of multinationals, large companies and SMEs in the Arab world for more than ten years. Based in Beirut, BRD serves customers in the Middle East, Gulf and North Africa. It provides decision-makers with innovative, evidence-based policy solutions while strengthening civil society leadership and participation in the region. BRD's clients are therefore varied, ranging from between government agencies, public institutions, international organisations to universities from more than 15 different countries.

One of BRD's specialities is its ability to adapt global knowledge and expertise, in terms of constitutional dialogue, administrative reform and HE, to the Arab context, through partnership and experimental and collaborative methodology. Thus, BRD has managed more than 120 projects in 24 countries since 2008. In addition, in 2017, BRD piloted 51 projects in 12 different sectors. 44% of BRD's activities are in capacity building while 29% were in policy innovation and 27% in public management consulting. This has enabled BRD to carry out 120 institutional reforms in the region, publish 85 reports and policy papers and develop 30 new educational programmes and training courses.

In the field of policy research, BRD offers perception studies, impact assessments and interdisciplinary policy analyses using a methodological approach adapted

to each context and project. With regard to the public management consulting activities, BRD offers effective solutions adapted to the needs of public and parapublic entities such as ministries, parliaments, parapublic institutions and civil servants. The purpose of these activities is to stimulate the performance of public institutions by helping to develop strategies, reform management systems and empower public servants. Finally, BRD offers more than 50 highly experiential programmes focused on the specific needs of civil servants, practitioners and civil society actors. All learning interventions focus on practice, simulations, role plays and cases from the participants' environment. More than 10,000 leaders from the public, private and non-profit sectors have participated in these programs over the past five years. This has also enabled BRD to develop partnerships between these different stakeholders, particularly in SE.

The strategy adopted by BRD to promote SE in the MENA region, "Social Entrepreneurship Momentum", is based on three main axes: Promoting the tools and logic of SE through formal and informal education by collaborating with universities, schools and development agencies; Capacity development of SE ecosystem actors such as financing institutions, incubators, accelerators and other business support structures; Research in the SE sector and SE mapping to support evidence-based advocacy activities to improve the legal environment for entrepreneurship and policy decision-making for it.

BRD's impact on the social environment is considerable in Lebanon, where more than 60 localities have participated in the development of social stability mechanisms through collaboration between the various local actors to address the socio-economic, political and cultural challenges specific to each region. In terms of training, more than 200 social enterprises,

incubators and NGOs participated in BRD training courses on social innovation and business modelling and planning. Similarly, more than 60 teachers from the MENA region have been trained in SE, in particular to introduce more creative, inclusive and flexible curricula, developed to meet the needs of the SE ecosystem in Lebanon and the ever-changing challenges of the economy. To this end, BRD has also collaborated with universities in the region, such as Saint Joseph University in Lebanon and IHEC Tunis, to establish the first bachelor's and master's degree programmes specialised in SE. The process gave rise to the idea of creating a free and accessible application (for the application available for certain regions of Lebanon), The Hub, was also created to facilitate collaboration between the different actors of the

**Box A4. SSE and Corporate Social Responsibility (CSR): A sometimes conflictual relationship that needs to be clarified**

We often hear about the dynamics of CSR, which sometimes tends to overshadow communication about the benefits of SSE. Competition with lucrative "Social Responsibility" companies is sometimes a problem for SSE. Many sides of SSE's activities are nowadays invested by profitable companies. SSE companies are not developing on an equal footing, particularly in sectors such as home help. We therefore believe that it is necessary to put the two concepts in perspective in order to better understand their differences and understand whether mutually beneficial complementarities can be found.

SSE is a set of organisations with a specific status, collective and social utility. The SSE also has a "project", i.e. objectives that it aims to achieve with the means it puts in place to achieve them. As for CSR, it could be described as "the transposition to companies of the logic of sustainable development, which is often presented as a combination of economic, social and environmental concerns". In concrete terms, CSR approaches involve the construction of an extra-financial information system (reporting) and action to improve the results of the system and thus the company's "image". SR therefore concerns large transnational firms that are well integrated into international markets. SSE generally concerns small structures (such as SMEs or VSEs) and is governed by national legal and tax rules. However, lucrative CSR companies can have a real "social" impact and, moreover, they cultivate links with SSE structures, leading to mutual stimulation. More concretely, it should be noted that:

- The SSE statutory rules are certainly stronger than voluntary



reversible) CSR commitments. However, traditional companies whose brands are known to the general public can make great efforts (e. g. to control the working conditions of many subcontractors and raise real questions, because they are subject to public scrutiny. SSE structures, on the other hand, can stick to the strict rules dictated, without seeking to bring them truly live and, paradoxically, they become less inclusive because they do not raise the same questions. The two types of companies stimulate each other, creating positive overall dynamics. The communication of lucrative companies on their socially responsible nature encourages SSE companies to further affirm their values and show that, on the ground, they remain well ahead of their lucrative "competitors". SSE includes certain NGOs that encourage profitable companies to improve their practices and communicate more about their actions. At the same time, some NGO and foundation activities may be the result of the CSR policy of profitable companies.

It would therefore be wrong to consider CSR as a substitute, or only as an obstacle to the development of SSE. It is true that CSR companies benefit from more resources for their development, but when their purpose is "of social utility", they must be welcomed. CSR should be seen rather as an "ambiguous stimulant" that allows the regeneration and self-evaluation of SSE.

Source: Blanc (2008) , CG13

**Box A5. DIVERS'ETIK: Successful example in the PACA Region (France) of capacity building for small producers and regional synergies for the import of products from Mediterranean terroirs**

Description: the project is part of a collective commitment to facilitate access to the European market for products and services from the South. Divers' Etik, works on the import and distribution, in the PACA Region, of South Mediterranean products, in a fair trade context. With its partners, it seeks to support the capacity building of Moroccan producers in order to structure and consolidate distribution networks. The first part of the project concerns capacity building for Moroccan producers

; implementation of a pilot training-action program for cooperative leaders and future Moroccan coaches. The second part is to carry out a feasibility study prior to the construction of a Mediterranean platform for the import of fair trade products and to organize a capitalisation and mobilisation meeting aimed at creating links with new Mediterranean Fair Trade actors with a view to sharing experiences, know-how and economic cooperation. Results: At least 4 managers from 2 producer organisations and 6 future coaches trained in social entrepreneurship; at least 4 managers from these structures and 6 future supervisors trained on food safety standards and import/export procedures for their products ; 6 future coaches have acquired new methods and tools for training/coaching producers

; a core group of SSE actors from the North and South of the Mediterranean committed to a collective support of the platform; a network of 10 distributors in the PACA region that mobilises the diaspora of the countries of origin of the products; regional logistics partners with strong links



o the countries of origin of the products;  
project experience shared with new  
actors/regions in the Mediterranean basin  
Partners: Migration and Development; Inter-  
Made; ACIM; Citizens of the Earth; SODEV  
Territory (s) involved: PACA, Morocco Target  
public: 4 representatives (managers or  
managers) of 2 producers/ice groups located  
in the Tangiers/Tetouan and Souss Massa  
Drâa regions

Regional participation: €21,250 (via AAP  
2015)

**Box A6. AREMDT Living Lab: Original  
example PACA (France) of the Living  
Laboratory of Solidarity Entrepreneurship in  
the Mediterranean - Citizens of the Earth**

*Description: the overall objective of the AREMDT  
network is to develop the solidarity  
entrepreneurial spirit and strengthen the  
entrepreneurial capacities of young  
Mediterranean people. The Living Lab project  
aims to create a collaborative workspace for  
Franco-Moroccan solidarity entrepreneurship  
in the Tangiers-Tetouan Region and to  
strengthen the skills of a group of young people  
with Moroccan solidarity business projects  
(tourism sector), followed by students from the  
PACA Region (Marseille and Toulon), to  
support their creative careers and the  
development of activities.*

*Results: emergence of cooperation and  
innovation; PACA students are made aware and  
trained through case studies of solidarity  
entrepreneurship in the Mediterranean;  
enhancement of the AREMDT Living Lab project  
in the Mediterranean as a pilot project to support  
solidarity entrepreneurship for youth; field  
research-action work on sustainable tourism and  
solidarity entrepreneurship to capitalise on and  
promote the innovative approach of the project*

*Partners: SODEV Morocco, the rural commune  
of Ain Baida, GRM laboratory of the University  
of Toulon-Var, the association Femmes d'ici et  
d'ailleurs, the association Le Loubatas*

*Impacted territory(ies): PACA, rural  
municipality of Ain Baida (Morocco)*

*Target audience: 50 young students from the  
PACA region (under 35 years old); 10 promoters  
of solidarity entrepreneurship projects in the  
territory of Ain Beida (including at least 5 young  
people); 1 research professor and a doctoral  
student from the University of Toulon-Var; 2  
solidarity entrepreneurs from the AREMDT  
network in the Mediterranean (Tunisia or  
Algeria)*

*2 solidarity entrepreneurs from the PACA*

**Box A7. Mowgli Mentoring**

Mowgli Mentoring is a non-profit organisation working on inclusiveness and economic and social change in the MENA region. It provides a supportive framework that allows entrepreneurs, employees, women and youth to realise their potential and explore new opportunities. Since 2008, Mowgli has been working with philanthropists and government and private, local and international partners to provide mentoring services to entrepreneurs, in all sectors, in 14 countries in the Middle East, North Africa and the United Kingdom. Mowgli Mentoring seeks to create and protect jobs, with an emphasis on economic and social investment, with the ultimate goal of helping the region achieve its target of 80 to 100 million jobs by 2020.

In addition, Mowgli focuses its work on developing leadership and supporting entrepreneurial ecosystems by highlighting their potential to solve social problems such as unemployment, poverty and economic instability in the region. Mowgli offers three distinct programs: an Entrepreneur Mentorship Program, a Mentor Training Program and an MFI Mentor Training Program. All three promote inclusiveness and diversity: between 2008 and 2015, 29% of Mowgli alumni, 32% of Mowgli entrepreneurs and 27% of Mowgli mentors were women.

The first level on which Mowgli focuses is personal growth and leadership development. Each entrepreneur receives long-term support and counselling, by at least one trained and competent mentor, to develop a relationship based on trust. Mowgli's impact on entrepreneurs and mentors is obvious. By strengthening the entrepreneurial potential and qualities of entrepreneurs (resilience, motivation and trust), Mowgli seeks to

remove the obstacles that hold back informed decision-making, encourage entrepreneurs to move outside their comfort zone, boost their motivation, and build on their successes. In 2010, 81% of entrepreneurs felt more confident in general and 76% of them gained confidence in their decision-making after working with a Mowgli mentor. The program also allowed them to overcome their fear of failure and adopt a healthy work-life balance. As for the mentors, 77% have developed a strong sense of self-awareness and more than 85% feel that their role has helped them to better understand others.

The second level of programs for which Mowgli has had a significant impact is the growth, sustainability and success of the company. 89% of the companies supervised by Mowgli were still operating 5 years after the program. In addition, in 2010, 71% of entrepreneurs felt more confident to develop their business and about half of them successfully increased their company's customer list and turnover during the year. For Mowgli mentors, approximately 80% have developed both leadership and coaching skills and an ability for active listening. In addition, 70% say they have used their mentoring skills in a professional setting with more junior colleagues.

The last level where Mowgli has been a key actor for change is Economic growth, job creation and safeguarding. It is by working on personal aspects and leadership development that social enterprises become more prosperous; this explains why 92% of Mowgli entrepreneurs and 82% of Mowgli mentors say they would recommend Mowgli to other entrepreneurs and professionals. In the long term, the process leads to the creation of a greater number of jobs and these are more sustainable, resulting in economic growth and greater prosperity at the national level.

*Apart from the level of return on investment in mentoring, Mowgli entrepreneurs have each created an average of 3.3 new jobs and preserved more than 90% of existing jobs, corresponding to a total of more than 3,470 jobs. In fact, Mowgli Entrepreneurs have contributed \$18.4 million to the region's economies through the creation and preservation of jobs. Mowgli's impact on job creation was rewarded in 2016 with the Ta'atheer Social Impact Awards for job creation..*

*Over the period 2008-2015, Mowgli provided more than 90 mentoring programs in the MENA region and the United Kingdom, corresponding to more than 1,800 entrepreneurs and mentors, while providing investors with an average return on their investments of 890%, helping them to support their businesses, to create jobs and to preserve them. As a result, Mowgli has been recognised as a major player in SE in the MENA region, winning a number of awards and prizes such as the European Quality Award (EQA) awarded to Mowgli in 2016 by the European Mentoring and Coaching Council (EMCC) for its Mowgli Mentoring Experience (MME) program and program structure. This recognition is due to the organisation's interest in maximizing its impact in three key areas of synergy.*

*Therefore, Mowgli Mentoring is an organisation that believes in the power of social entrepreneurship as a vehicle for growth and prosperity and sees structured mentoring and complementary and personalised training as a way to promote SE and to engage in optimal investments to develop the social impact of social enterprises. Ultimately, Mowgli seeks to create a global community of trained mentors and entrepreneurs who can access opportunities for networking, learning and growth.*