



FEMISE Policy Seminar on¹
“Unlocking the Potential of the Private Sector in South Med Countries”

American University of Beirut (AUB)
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Minutes

Welcome Note and Opening Remarks

Dr. Ahmed Galal initiated the seminar by welcoming all the participants and introducing the theme: “**Unlocking the potential of the private sector in South Med Countries**” while emphasizing that it was important to understand what is locking the private sector from flourishing.

Dr. Galal elaborated that the seminar will try to answer three main questions:

- One factual question that needs validation: the private sector performance in the region is below potential and below the expectations. It is neither dynamic nor productive enough. Furthermore, it is not creating enough jobs.
- What is preventing the private sector from reaching its potential? Two ideas are being advanced: macro and micro constraints.
- What is the role of the international community to these regards?

Dr. Galal also emphasised that private sector development is not by definition a good thing. He explained: “On the one hand a *good* private sector is one that is creative, adopting new technologies, entrepreneurial, benefiting and making societies benefit, innovative, productive and efficient. On the other hand, there is a private sector that flourishes on the back of everybody else, which is a rent-seeking private sector. In this later, the private sector is not in the business of advancing development, it rather exploits resources and deprives individuals”. He concluded his introduction by saying that we need to worry about the wellbeing of the whole society, i.e. be interested in developing the “good” type of private sector development that does not just benefit a certain group of interests.

These introductory remarks were followed by a welcome note from Dr. Simon Neaime, who highlighted briefly the importance of the private sector in contributing to growth and employment.

Prof. Patricia Augier also welcomed the participants and thanked the AUB for hosting the event. She added that the value added of this seminar was to provide an opportunity to better understand the macro and micro issues behind the performance of the private sector and to provide recommendations on how to address these issues.

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Session 1: Macroeconomic Challenges and the Private Sector in South-Med Countries

Dr. Galal introduced the first session by highlighting its objective, which is to address the macroeconomic conditions of the region and its effect on private sector performance. He added that the Arab Spring caused volatility and put pressures on the macro balances (budget deficits, exchange rates instabilities, etc.), which may have not helped the private sector. In Egypt for instance, the wide gap between the exchange rate of the US Dollars against the Egyptian pound in official channels compared to black markets was huge, which hindered the private sector investments due to instability in selling prices and cost structures. This is evidence that one macroeconomic policy decision can affect, not only investment decisions, but also existing firms and their operations.

Monetary policy and meeting the challenges facing the private sector in Lebanon

After a short welcome introduction, Dr. Youssef El-Khalil, Head of the Financial Operations Department-of the Central Bank of Lebanon (Banque du Liban) explained that he is going to speak about the specificities of the Central Bank in Lebanon and its interventions to support the private sector. Moreover, that he will add some ideas on the constraints facing the private sector in the region.

He argued that Lebanon is blessed with its code of money and credit that was adopted in 1963. He stated that, the code is very modern in today's terminology as it provides the central bank with almost full independence. Moreover, the mandate of the central bank is not only about stable inflation or stable currency but also about having an efficient economic cycle and reduced unemployment. The code also considers the social responsibility in promoting inclusive growth.

Dr. El-Khalil listed three pillars among which the Central Bank of Lebanon policy has been operating for the past 20 years:

- First, stable currency. At the beginning of the war, one US Dollar was equal 2 Lebanese Liras and by the end of the war one US Dollar was equal 1500 Lebanese Liras.
- Second, designing a proper framework to assure a sustainable financing of the Lebanese debts in national and foreign currency.
- Third, designing a framework by which no bank is allowed to fail and this was tested practically many times.

These three pillars are very interlinked. They provide high levels of confidence and help preserving high level of foreign reserves. Also the adoption of the Basel III framework has contributed towards a solid banking system in Lebanon.

However, the impact of the Syrian war in 2011 has caused negative spillovers on the Lebanese economy: For instance, the balance of payments has been on deficit, with a net outflow of capital, reaching around 3 billion US dollars in 2016, cumulating for around \$ 9 billion between 2011 and 2016. Moreover, before 2011 and for the previous seven years, Lebanon had a potential growth rate of around 8 percent and the actual rate was around 4 to 4.5 percent. After 2011, the growth rate was between 0 and 1.5 percent accompanied by deflation.

As a result, the central bank had to intervene by providing incentives to the banks to lend to the private sector. Accordingly, the central bank reduced the reserve requirements for the banks that provide loans towards projects in certain sectors such as construction, energy, education. It is not only about corporate social responsibility and inclusion, it is also a macroeconomic policy tool to boost growth and job creation. This is a tool that is



controllable and insures that no bubbles will be created. Building costly and luxurious apartments became less and less popular as the central bank only provided incentives to finance small and medium apartments.

Lebanon now ranks better than MENA countries in terms of access to finance and inclusion. However, Lebanese firms complain mostly from the uncertain political situation and related security issues in addition to the quality of infrastructure (e.g. electricity and internet). He added MENA countries' most investment funding is provided through the public sector. Hence, the problem is not in the lack of funding but rather on efficiently directing funds to the private sector.

He added that there is a kind of new environment that allows developing entrepreneurs from the young and educated. Therefore, there is a need to include entrepreneurship as part of the education and reach all classes of society. By doing this, we would facilitate the road for the youth to be included in the growing economy.

Dr. El-Khalil concluded by saying that Lebanon has its own problems; the rural sector is neglected and this is common with the rest of the Arab World, but there is a room for improvement and proper introduction of the Knowledge economy.

The impact of monetary policy and exchange regimes and the IMF program on the private sector in Tunisia

In his speech, Dr. Sami Mouley, professor at the University of Tunis El Manar, explained that the difficulties that the Tunisian economy has been going through are more or less similar to those in Egypt in spite of the differences between the two economies.

Regarding the private sector in Tunisia, the speech deals with four main issues:

- (i) Why the SME's problematic and the role of private sector are an old but new issue in Tunisia now?
- (ii) The responses of monetary and exchange policies to boost private investment: crisis's exit or trigger strategies?
- (iii) How IMF's programs implemented in Tunisia give external inducements for reforms?
- (iv) What are the next issues and open questions in the short - medium terms?

Comparing to the initial conditions in 2011, Tunisia witnessed a cumulative decline in the Global Competitiveness Report (WEF) ranking (55 places), due to the poor performance of the efficiency enhancers' factors. Major barriers to business practice are attributable mainly to a weakness in the level of financial market development and a low efficiency of the goods market, particularly because of prevalence of non-tariff barriers and other rules restricting foreign investment. However, Tunisia improved the SME's access to internal financing sources, which has resulted in a small improvement in the Doing Business ranks.

Dr. Mouley contrasted these findings with some facts from the enterprises surveys by the World Bank as well as the national ones. The Tunisian SME's still complaining from some obstacles including: access to financing sources, banking inclusion, weak financial intermediation and political stability.

Some indicators were presented by Dr. Mouley as follows:

- Tunisia was able to control the capital outflows and to provide some finance to SME's.

However the investment rate decreased from about 24 percent to about 19 percent and the contribution of investment to growth was weak. Relatively to household loans, financing to the private sector remained lower, with banks remaining rather risk-averse.



- Foreign direct investments continued to be resilient since in majority they were concentrated in the energy sector. However, external portfolio investment was very low. This is linked to the fact that the portfolio investment in equities is only 50% liberalized for listed companies, and a rule of 20% ceiling is still adopted as an authorized rate of subscription by non-resident of public debt securities.

Therefore, Tunisia underwent two IMF-based programs with an amount of \$1.75 million and \$2.9 million, respectively to endorse macroeconomic and financial reforms.

Therefore, accompanying responses mechanisms in terms of monetary policy were put in place by the Central Bank of Tunisia (CBT) and can be summarized as follows:

- Monetary tightening in 2012-2013, to break the chronicle of inflationary pressures (effects of pass-through, output gap, informality, exogenous factors, etc.)
- Since the end of 2015, monetary policy has returned to a more accommodating way in favor of reinvigorating investment, while at the same time putting in place an advanced alert system on cyclical, fiscal and balance of payments (Of monetary policy).
- Modernization of instruments of monetary policy operations and liquidity management (refinancing)
- Better transmission of the impulses of monetary policy through the rate of interest
- From implicit targeting to formal targeting of inflation to better anchor inflationary expectations of economic operators
- A new banking law to strengthen the CBT's efforts to develop more effective means of preventing systemic risks posed by financial institutions (stability protocols, crisis simulation exercises, crisis resolution mechanism, mechanisms for bank resolution.....)
- A deposit guarantee scheme: to consolidate confidence in the banking sector and to facilitate the handling of a possible bankruptcy
- A new status of CBT's in regard of the best practices and international standard to stimulate better quality bank loans that would boost the investment
- Tools to boost banking competition and developing a system of credit information to support the supply of credit (credit bureau)
- Better exchange rate flexibility and flexibility of foreign exchange regulation in favour of the private sector.

Dr. Mouley concluded his presentation by clarifying the three next steps for the central bank, they were:

- Attracting more portfolio investment to compensate the current account deficit and progressively proceed to liberalization of the Tunisian Dinar.
- Development of the bond market and consolidation of its role in financing the economy
- A new scheme of refinancing led growth for SME's

Sustainability of EU-Med macroeconomic policies and their impact on the private sector: post-financial and debt crises

The third presentation was made by Dr. Simon Neaime, professor at the Institute of Financial economics, AUB, who explained that he will provide an overview of the macroeconomic situation today, especially post financial crisis and post Arab Spring. He added that the 2008 international financial crisis and the economic and political uncertainty that has characterized the MED region since the uprisings of 2011 continue to dampen the prospects for growth, job creation, fiscal balances and macroeconomic stability.



Dr. Neaime elaborated by adding that in the MED countries, there is a limited fiscal space and that the fixed exchange rate regimes have prevented the central banks from being sufficiently effective. Therefore, Egypt did the right move by liberalizing its exchange rate, despite the negative short term outcomes.

On another front, central banks have adopted policies that were not always in consonance with the received wisdom. After the financial crisis, the massive injection of money in the EU and the US economies had no impact on growth and inflation. So we ask ourselves: where did this money go? The central problem in monetary policy making has been in finding out how much of the extra money results in an increase in output and how much in inflation. The major policy issue was whether the monetary policy reached a dead end. The question is "are there new directions that will solve the current financial crises"? What about the introduction of macroeconomic stabilization programs in EU and MED countries, is there still room to use both monetary and fiscal policies in tandem to curb those macroeconomic imbalances?

In addressing these questions, Dr. Neaime started by reviewing the macroeconomic environment of the region EU-Med region. He highlighted that the region is facing a sort of recession and deflation coupled with large fiscal imbalances (large budget and current account deficits and accumulated public debts). Traditional macroeconomic stabilization mechanisms cannot be used any more. Average unemployment rates increased to over 15 percent in Europe and more than 20 percent in the MED countries. Interest rates have increased and this has discouraged spending and investment and has lowered real GDP growth rates. Austerity measures were introduced in Europe to tackle these fiscal imbalances at a time of a recessionary environment.

As for the macro indicators, starting December 2015, negative inflation rates in EU have been recording and it is still ongoing. Growth rates were declining in the MED countries from 2010 to 2019, while public debt as percentage to GDP has been increasing. Lebanon recorded the highest public debts among its peers, and its real interest rates remain high compared to those in Egypt which are declining. Moreover, budget and current accounts deficits remain significant in the MED countries.

The EU adopted a quantitative easing mechanism (QE) in 2015. The main objective of that policy was to fight deflation and stimulate growth. However, this mechanism cannot be implemented in MED countries due to their fixed exchange rate regimes. When central bank buys bonds from banks with new money, this will increase money supply. Therefore, this will lower interest rates and will lead to currency devaluation. However, in EU despite the monetary policy, there was no response on GDP growth neither on inflation. This is due to the fact that in a recession environment, agents tend to hold cash and do not spend it. After the financial crisis of 2008, the injection of liquidity did not have an effect on growth rates. EU and MED private banks piled up liquidity without extending more credit to the private sector and contributing to money creation. Therefore, EU monetary base and M3 were disconnected from each other.

In terms of financial markets, the loans influence the real economy in terms of consumption and investment. With the financial crisis in 2008, banks became risk averse and did not extend lending to private sector. Hence, growth and lending were flat.

Monetary policy will remain ineffective as long as it is not connected with private sector expectations. Consumer and business confidence are very low in EU and MED countries. On top of that, we have the Greek debt crisis that is affecting negatively the business confidence. Moreover, austerity measures are negatively affecting aggregate demand and the growth rate of GDP.



Another channel that is expected to affect the growth is the exchange rate channel. Quantitative easing is causing the depreciation of the euro which will subsequently stimulate exports. However, this option is not available in the MED countries because of the fixed exchange rate regimes.

In conclusion, Dr. Neaime said that first, the absence of fiscal space in most MED and EU countries is due to the accumulation of large public debts and recurrent budget and current account deficits. Second, monetary policy is ineffective. This boils down to no role for government policies (fiscal and monetary) to deal with the current macroeconomic imbalances paving the way for future fiscal and currency crises.

He added that what needs to be done is the following:

- Reducing the size of public sector;
- Improve private sector's expectations in both the EU and MED
- Encourage commercial banks in both regions to provide more liquidity to private sector, especially SMEs, through loans and encouraging investments;
- Reducing government spending;
- Increasing taxes if possible;
- All the above would increase the growth rate of GDP and would render debt more sustainable;
- Once the above is achieved, can austerity and structural adjustment measures be introduced
- EU must acknowledge the importance of fiscal policy in the monetary union;
- For those EU and MED countries with fiscal space: use expansionary fiscal policy if available and possible.

Discussions

Discussions in this session revolved around the following:

SMEs and their capacity to create jobs.

To launch the discussion, Dr. Galal made a comment about a book entitled "Rich People, Poor Countries" where the author argued that SMEs do not create jobs but rather large corporations.

Dr. Raed Safadi argued that SMEs are the ones which create jobs: seven out of ten jobs in the OECD area for the last ten years have been created by SMEs, especially if we look at SMEs interaction and participation and supply chains with the large corporations. These SMEs also have an added value through what we call the indirect exports. Dr. Emmanuel Noutary intervened by saying that SMEs have a growth problem yet they are more efficient in creating jobs rather than large companies. Dr. Galal concluded the discussion by saying that SMEs and their value in job creation is an empirical question that should be tested.

The role of fiscal and monetary policy.

Dr. Galal made the comment that the session was about the following: First, the extent to which macro environment is impacting the private sector. Second, it was also about the actions that governments and central banks have undertaken. He added that the stories in the South-Med countries are similar since 2008 but their responses were different. They faced the global financial crisis and then the Arab Spring. With the political instability, these countries faced fewer external resources, there was a decline of capital from outside, investors and tourists are not coming anymore and exports have not increased. Therefore, foreign currencies have dried up in most of these countries. Their response was to draw down international reserves before liberalizing the exchange rate regimes under pressure. There were also pressures on the fiscal side represented in the form of social demands: wages and benefits mainly. The different governments responded differently. In theory, targeting exchange rate through monetary policy is not efficient. Also, on the fiscal side, there is level and there is composition: you can reduce the energy subsidies (which account



for a large part of the expenditures in the region) to reduce budget deficit and inject more money in the economy. Therefore, there is some room on the fiscal side. In Egypt for instance, we had sluggish economic growth, budget deficit and current account deficit. We had two options accordingly: activating and stimulating the economy or squeezing the economy like the Greek way or the IMF way. We opted for a stimulus because we had some resources and this is similar to what the US did.

Dr. Raed Safadi raised the question of where do we find ourselves now in this secular stagnation: a decreasing propensity to invest, increasing propensity to save and about zero percent interest rate in the United States, negative interest rates in the EU. He added that what we really miss is to go structural starting now (competition laws and labor laws for example).

Dr. Samir Makdisi raised a question on whether there has been a good effective monetary policy for the private sector. He also asked whether it is recommended in the case of Lebanon to abandon the monetary anchor. He added that the stable exchange rate regime in Lebanon has also good effects but there is a cost of huge public debt.

Dr. Emmanuel Noutary raised a question concerning the circular 331 by virtue of which there should be 75 percent of investment within innovative companies and whether there is an evaluation of the costs and jobs created.

Dr. Alain Santi made the comment that the macroeconomic environment has an important influence on the private sector concerning inflation and fiscal decisions. However, entrepreneurs and the private sector cannot affect policy makers' decisions.

Mr. Christophe Malherbe raised a question on how to reconcile between the macro and the micro sides. Figures fail to account for the informality of economies in the region. In Tunisia for instance, 60 percent of the GDP is generated from the informal sector.

Dr. Zafiris Tzannatos made the comment that one of the problems in Greece that has to do with macroeconomic policy and private sector was that in the period of crisis, you tend to formalize the informal economy. However, this informal economy is productive and spends most of its money in the formal economy. In Greece, the government is trying to control the fiscal gap by chasing up everybody to collect money. Therefore, this closes hundreds of thousands of SMEs while they used to contribute to the formal economy. This is a case where we had a macro policy with a fiscal objective but that negatively affected the private sector. Second, fiscal space should be interpreted broadly. It is not whether we spend more but rather the quality and composition of spending and corruption. Again, giving the example of Greece, there is one of the lowest levels of spending in health and about half already goes in pharmaceuticals. This hints at the existence of corruption and when the program to reduce spending arrived, spending was reduced everywhere, instead of keeping the already low level of spending on health stable and reassign the spending from pharmaceuticals to a sector such as services. Third, regarding banks and capital controls, Dr. Tzannatos argued that the Lebanese banking sector which supports the private sector has two problems: first it is very expensive and second it is not an efficient banking sector that promotes entrepreneurship.

Nicola Ehlermann (OECD) argued that there is an analogy done between the North and the South in the Mediterranean and there are basic assumptions regarding how the macro environment function in the South and North: in tax rules collection and spending, transparency and regulation of the systems, informality and corruption. But there is a great asset in the region, population growth is a potential for the South countries compared to the North countries. Moreover, South countries have market needs which is a potential for the private sector to grow. There are high deficits and these countries import a lot. However,



this is a potential for the private sector to grow to serve those markets.

Dr. Neaime responded to these comments and questions by saying that on the monetary and fiscal policies, after the financial crisis in the US, they injected to push the economy back. We still have some space but we need to readdress fiscal spending priorities. Moreover, he added that he does not recommend keeping a fixed exchange rate in a crisis situation. It is better to move to floating regime: we can do this in normal situations better than being pushed to do it.

Dr. El-Khalil, on his side, responded to the questions and comments by saying that austerity measures exacerbated rather than helped the situation in Europe. Injecting liquidity does not always work, especially in a recession because there is the issue of confidence. He added that he agrees that the policy of the Lebanese Central Bank imposes costs. But this is because the Central Bank is the only entity that accommodates the high deficits. We face so many inefficiencies so implementing stability is costly. For example, 40 percent of Lebanon accumulated debt is due to electricity. Moreover, he agrees that banks have been enjoying relatively high levels of profit but were encouraged to use substantial parts of those profits to consolidate their capital structure and meet international standards and requirements. As for the circular 331, the central bank is trying to assess and revise its strategy and its impact in terms of size and targeted sectors.

He responded to a remark related to the outflows of migrants from Lebanon by saying that this is a very important problem for the country however, it should not be tackled as a loss-loss since many of the migrants gain experience from abroad and can return to participate in rebuilding the economy. He thinks that the growth model such as Cobb Douglas or other models, such as the Endogenous Growth model, can link the micro and macro sides together. In the Arab World, we have the youngest population, yet many frustrations and unemployment exist.

Finally, Ms. Marie-Jo Char raised a question on the role of the private sector and its involvement into SMEs policy making process. In reply and concluding the session Dr. Galal stated that the private sector is not entitled to make policies, however it can have a consultancy role. As policies impact all the population, policy making is the privilege of the government, which is entrusted with the wellbeing of the whole society.

Session 2: Private Sector Development: Obstacles and Opportunities

Obstacles facing the private sector in the South Med region: an overview

Prof. Patricia Augier opened the second session by presenting some of the main obstacles that firms face in some MED economies using data from the World Bank Enterprise Surveys. In some countries, these surveys are available for two different points in time which gives an idea on the evolution of the business environment.

In Egypt, the two main obstacles were the political instability for almost half of the firms followed by the access to finance. As for Jordan, in 2006 and 2013, the main obstacles for firms were access to finance and the tax rates. In Lebanon, the main three obstacles were the political instability, the electricity, and the access to finance.

In summary, and according to the most updated data in 2013, the main obstacles for firms were as follows:

- The political instability particularly in Lebanon and Egypt;
- Access to finance mainly in Jordan, Egypt, and Lebanon;
- Corruption in Lebanon and Morocco;
- Electricity in Lebanon.



She added that this type of global information is useful but is just a first step, as there is a need to focus on each of these obstacles to better identify the efficient measures or reforms needed while bringing observations from real life experience. This is what this session is for.

Best practices for boosting the private sector and SMEs in the South Med countries

Ms. Marie-Jo Char explained how the "Enhancement of the Business Environment in the Southern Mediterranean - EBESM" project helps SMEs to grow, expand and create jobs. She explained that this three-year regional project funded by the EU and implemented by GIZ is part of the Private Sector Development Programme in the Southern Mediterranean targeting MSMEs by intervening at:

- Macro level: MSME business enabling environment - EBESM project
- Meso level reinforcing MSME support agencies - Euromed Invest ANIMA
- Micro level: support for regional clusters - UNIDO

She added that the project activities are linked to the Euro-Med industrial cooperation process to promoting SMEs, entrepreneurship and industrial cooperation in the framework of the 2014 -16 Work Programme adopted at Brussels 9th Ministerial meeting. Moreover, the project follows the assessment of the implementation of SME policies carried out by the EC, OECD, ETF and EIB in 2014 based on the Small Business Act for Europe (SBA), a comprehensive policy framework for SME policy adopted by the EU in 2008.

Ms. Char added that the SBA Assessment is a joint process implemented by the European Commission, OECD, EIB and the European Training Foundation (ETF), based on the SME Policy Index which is a policy tool that has been developed by the OECD and the EC in order to assess the implementation and development of policies in favour of SMEs. EBESM project aims at following up and supporting the implementation of policies on key topics identified in the recommendations for the South Med region.

On the importance of SMEs and their position in the MED region, Ms. Char explained: 90% of businesses in the MED region are MSMEs; the average number of SMEs per 1000 people in MED area is 23 but SMEs have an important development potential in the Region; 82% are micro firms (1-9 employees) and they represent around 33% of total employment.

Ms. Char highlighted that the objectives of EBESM are to enhance the business environment and promote SME and entrepreneurship development in the MED region, in line with EU best practices, namely the Small Business Act for Europe (SBA); and to expand the private sector through the development of more robust, inclusive and sustainable growth. She then elaborated on the activities of the project, its structure and its different phases.

She added that the project was successful in implementing reforms in favour of SMEs development in MED countries. For instance, in Lebanon, they institutionalised a Public Private Dialogue (PPD) mechanism to boost industrial exports in Lebanon. Similar PPDs were developed in other countries such as in Egypt for improving SMEs policy making process through structured, participatory and inclusive approach. In Morocco and Jordan, they developed the SME test tool which is a legal tool to measure ex ante the impact of a new legislation on SMEs. As for Tunisia, they developed a platform to identify the administrative obstacles and challenges facing entrepreneurs in the country. This was achieved thanks to a very good cooperation with national counterparts.

She concluded her presentation by saying that the three important keys of best practices for boosting the private sector and SMEs in MED countries are: (i) The government will that



must be reform minded and show active leadership; (ii) The choice of the right institution to coordinate the policy-making and reform process; and (iii) the involvement of the private sector into the SMEs policy-making process.

Overcoming constraints to develop SMEs sector in Lebanon: initiatives of Kafalat

Dr. Khater Abi Habib, CEO of Kafalat, presented the initiative of "Kafalat" and its responses to overcome the constraints faced by the SMEs in Lebanon.

Dr. Abi Habib started by reviewing the historical background of the Kafalat initiative. By the end of 90s, when Lebanon overcame the war period and the banking and financial sector became quite solid, various financial economic actors were looking at the issue of bank financing. SMEs needed support and at the time the commercial banks were the only serious source of financing in Lebanon. However, there was a fundamental inefficiency in the financing market for commercial banks, which were related to the notion of risk over the war and turbulence period that Lebanon went through over 15 years.

In most cases, one would expect that the banking sector, which was fully private, to collapse. However, the banks did survive, but commercial banks were functioning on the notion of survival with the primary responsibility to refund depositors and make profits. The consequences of this defensiveness approach were the following: first, lending under highly changing circumstances and second, the difficulty in the ability to recover. Therefore, the tendency of banks was very short term lending and favoring certain sectors because of the risks of long term: lending was therefore restricted to merchants, traders and direct services who had the ability to repay loans quickly. Hence, the long-term investments in agriculture, tourism and industry were negatively affected. Over and above, regions away from the capital were considered of higher risk and hence there was a sort of concentration of lending to projects established in the center on the expense of the peripheries.

Dr. Abi Habib explained that they had to present something that acts against these market inefficiencies. The best thing is to have a secured institution in terms of capital and management which represents a high guarantee for longer periods to cover intermediate and long terms loans to the sectors that seem to be mostly affected: agriculture, industry, tourism, traditional crafts, and high technology. The guarantee was 75 percent for these sectors with loans up to seven years with a grace period minimum 6 months and up to 1 year. The sealing for guarantee was about 300 million Lebanese Liras equivalent to 100 thousands US Dollars. The company was created as a financial company with a limited liability public company (SAL). The shareholders included the National Institute for the Guarantee of Deposits and all the banks operating in Lebanon. Its equity was set at 20 million Liras equivalent to 13.4 million US Dollars.

A typical SME that is able to benefit from this company has to be active in one of those sectors and with 40 formal employees or less (registered at the national security center not seasonal employees). The limit of the loan was set to be 200 thousands US Dollars but it could also be a smaller loan if accepted by the bank. This is how Kafalat started: Any eligible person or company, whether it is a startup or an expansion could get a loan from the bank while complying with the rules. As Kafalat started its activities, the central bank came on board by providing incentives to the Banks which provide loans to SME to use 60 percent of the liquidity from the secretary deposits: banks at that time had to deposit 10 percent of their deposits in Lebanese Liras at the Central Bank to mobilize the cash and they will receive 0 percent of that deposits. Accordingly, they can give 60 percent of the loan at 0 cost and that would be reflected in the rate of interest charged to the borrower. Then, the government came in to give a subvention to the interest rate and made it 7 percent. At that time, interest rate in Lebanese Liras was very high. Later, the interest rate was reduced to 4.5 percent. That made the cost of the loan to the borrower lower: the loan was highly



secured with 75 percent cash guarantee. Banks can only charge in the following way: the yield on the one year treasury bill (yield opportunity cost) plus 3 percent. Kafalat would charge for its own risk of its equity: 2.5 percent on the guaranteed amount of the loan. And accordingly, the program started to function. Banks were permitted to take guarantees. 2 years later, we decided that the banks could take guarantees up to 50 percent of the value of the loan. Today, about 58 percent of the loans have other guarantees. 42 percent of the grants are content strictly with our guarantee.

The program of course addressed only a part of the problem. Later, Kafalat negotiated with the EU and they were very generous. Kafalat could not change certain rules and parameters because they are indicated by virtue of law: the National Institute for the Guarantee of Deposits should be a shareholder. The EU put at their disposal 4 million Euros to take the risk of the extra engineering of the products which we created: Kafalat plus and Kafalat innovation. In the Kafalat program, loans would go up to 600 million Euros to be able to cope with expanding SMEs and give them a wider scope. The loan covers the period of seven years. But, they gave a guarantee of up to 85 percent and the bank could not ask for any other guarantee: personal and real. However, borrowers have to be formal: either joint stock company (SAL) or a limited liability company or an NGO. When a company applied for a loan, including the new loans, on its balance sheet declared to the government there has to be at least 30 percent of equity against a maximum of 70 percent of external liabilities. Hence, Kafalat encouraged people to retain more equity formally on their balance sheets.

The second program was for innovative startups. Here the program gave a guarantee of 90 percent. The company should be a startup (should not be established for less than two years) and the project has to be innovative. Later to solve other imperfections in the market, Kafalat created with the help of EU, a program with 10 years and another program with 15 years for sustainable energy. It took another dimension, because in innovation and Kafalat plus, they realized at some stages that lending was the best form available to the country. With the help of the World Bank, through the Lebanese Government borrowing 70 million US Dollars, they served some companies by lending them but also wanted them to have a strong equity base, stronger participation by institutional investors therefore the extendibility of financial knowledge and market knowledge. They also encouraged these companies to go regional and international through the participation of larger companies and hopefully to be listed on the stock exchange.

Improving the business environment for the private sector in Morocco: initiatives of the CNEA

Mr. Khalid Benabdallah, member of the Secretariat of the National Committee for Business Environment (CNEA), presented the Moroccan experience in reforming the business environment through the experience of his institution. The CNEA, chaired by the Head of Government, was created in 2010 with the objective to develop dialogue between the public and private sectors on the Business Environment. Its main purposes are the following:

- To propose to the Government the reforms and measures aiming to improve the Business Environment;
- To coordinate the reforms' implementation and evaluate their impacts;
- To ensure a sustainable improvement of the Business Environment.

He elaborated on the reasons behind the establishment of CNEA as private-public structure and its role in enhancing the business environment in Morocco. As a public-private dialogue platform, CNEA brings together the involved ministries and public agencies from one side and from the other side the private sector representatives such as the General Confederation of Moroccan Enterprises (which is the most representative association of private sector in Morocco), the Professional Group of Moroccan Banks and the Federation of



Chambers of Commerce, Industry and Services. The other partners are the Competition council, the Central bank of Morocco and the Central Authority for Prevention of Corruption.

Mr. Benabdallah then elaborated on the structure and organization of the CNEA. In terms of functioning, the National Committee meets at least once a year to review the progress of the engaged reforms, approve the annual report and the next annual action plan. The National Committee is supported by a Technical Committee, whose function is to facilitate the role of the secretariat by providing the technical approval of the working groups, and the Permanent secretariat, whose function is to coordinate the whole process of the committee, set agendas, manage communication, provide methodological and technical support to all actors of the reform and be a point of contact for other stakeholders. Then, he explained that each reform included in the action plan, a working group is created and chaired by a project manager appointed by the department that is the most interested by the reform. The project managers insure the implementation of the various projects included by the CNEA action plan in coordination with the Secretariat and the relevant stakeholders.

In terms of cooperation, there are four main aspects through which CNEA is currently oriented: developing a regional approach by coordinating with the regional committees to take into consideration the local specificities, developing sectorial committees for business environment, studying the opportunity of cooperating with the academic world, and cooperating with various international partners like GIZ, the World Bank and the EU.

On the organizational and methodological sides, Mr Benabdallah highlighted that a set of projects has been launched to streamline and enhance CNEA's process and make it more efficient as the following:

- The launch of an organizational and communication audit;
- The setting up a new project management methodology to conduct and implement the selected reforms, with a collaborative governance approach and a new IT platform;
- The development of a new strategy for Business Environment improvement based on a better constraints-to-entrepreneurship analysis.

As for the main achievements of CNEA since its creation in 2010, they are as follows:

- The implementation of the legal framework on the Public Private Partnership;
- The implementation of a Single Window Operation for International Trade and the dematerialization of the import/export titles;
- The approval of the General Construction Regulation (RGC);
- Facilitating the process of starting a business by reducing the time, the cost, and the number of procedures;
- The implementation of an electronic payment of duties and taxes;
- The implementation of the Unified business identifier (ICE);
- The reconsideration of the regulation (decree) on payment delays in order to help companies to cope with the treasury problems that they might face.

As pointed out by Mr Benabdallah, after more than 20 years of waiting, the decree modifying the General Construction Regulation was approved in 2013 through CNEA's process. The key contributions of the reform are the following:

- The standardization and homogenization of forms and authorization procedures adopted at national level;
- The clarification of the responsibilities assigned to the various stakeholders by the texts in force;
- The access to information and the follow-up of applications for authorization process;



- The establishment of a procedural mechanism adapted to the size of the communes and respecting the principles of proximity and progressivity (One-stop shops systems).

This reform has enabled Morocco to improve its ranking on dealing with construction Permits indicator -Doing Business report- by 81 places to occupy the 18th place in the last edition among 190 economies.

These reforms, among many others, helped to improve the business environment in Morocco, to attract more foreign investments and to improve Morocco's ranking in international reports like the Doing Business report. In fact, since the creation of CNEA, Morocco was able to improve its ranking by 60 places in the ranking of doing business report, moving from the 128th place in 2010 to the 68th in the last edition, and to rank at the top of North African countries, third at the African level and fourth in the MENA region. Moreover, the Doing Business Report classifies countries into five categories and put Morocco for the first time in the second one beside several emerging and developed countries such as Turkey, Italy, Russia and Luxembourg.

To maintain these achievements, the CNEA's approach is the following:

- Improving the participatory approach in the reform process by :
 - Strengthening the role of the private sector and its involvement through the integration of some professional associations in the composition of the CNEA.
 - Establishing new electronic tools to improve the feedback and exchange with business leaders and organisms about constraints, complaints, and reforms.
- Improving the reforming approach;
 - The CNEA intends to develop for the first time a medium-term strategy for the improvement of the business environment.
 - The CNEA is managing and coordinating reforms focusing on the following categories :
 - The modernization of the legal and regulatory framework;
 - The simplification and dematerialization of administrative procedures;
 - The creation and generalization of the one-stop shops.
- The Openness to regions, sectors, and the academic world;
- The setting up of an IT system to monitor and improve Morocco's ranking in the international reports. Morocco's evaluation in those reports represents a real challenge and a source of inspiration and identification of reforms to implement.

Discussions

The discussions in this session revolved around the following issues:

On the Kafalat initiative:

Christophe Malherbe raised the following questions: What is the measure of relevance of outreach of Kafalat in the universe of SMEs in Lebanon? And to what extent Kafalat is able to cover your cost? And do you see some banks learning from Kafalat positive experience with SMEs? Moreover, Dr. Alain Santi asked whether Kafalat works closely with micro credit enterprises? What is the percentage of bad loans compared to its total portfolio?

Dr. Noutary raised a question on whether the initiative applies to individuals? And how would you think of incentives to have more private and individual investments?

Dr. Constantin Tsakas raised the following questions: did Kafalat closely cooperate with public authorities to facilitate giving guarantees in specific sectors? And does Kafalat cooperate with international institutions? Dr. Augier asked whether there is a possibility to emulate or extend Kafalat on a regional level.



Dr. Abi Habib responded to these questions by saying that legally they do not have the authority to operate outside Lebanon. Regarding the outreach of Kafalat, they gave guarantees to 16500 projects, compared to the total SMEs in Lebanon, this is considered minimal. But given that the sectors that they cover represent one third of the GDP, then they can magnify their results. Statistics in Lebanon are difficult to handle because of the categories which do not have official registries. For instance, much of the activities in agriculture are not registered. 40 percent of their guarantees operate in agriculture and at least two thirds of those are individuals. In the industry sector, for SMEs, they have probably reached around 15 percent or 18 percent. Regarding the regional statistics, 60 percent of guarantees are in distant regions. The pace of Kafalats' business was rising until 2011. In the last four years, they faced a high decline but are re-stabilizing now.

Regarding the costs, he clarified that Kafalat started with an equity base of 30 billion Lebanese Liras. Currently, they have an equity of 150 billion Lebanese Liras. So Kafalat was very profitable. He added that this year they made very small profit given the difficult circumstances of insecurity and drop in oil prices, which might end up next year with a small loss. On the banks developing, he said that banks give subsidized loans by the central bank for larger enterprises but these have to have their own guarantees.

On the **CNEA initiative in Morocco** and **EBESM project**, the following discussion took place:

Dr. Galal raised a question on how can someone assess if an initiative is working or not? Is the process leading to something tangible? Also, what is behind the success of the Morocco program, especially politically?

Mr. Benabdallah responded to the question he was asked about the key factor behind CNEA's success by saying that CNEA was an initiative of the minister of economic and general affairs with the help of some other organizations such as the World Bank which made a study about how to improve the business environment in Morocco. The study highlighted the presence of many inter-ministerial committees without having the expected impact on the development of the private sector in the country. The idea was to create a structure with a participatory approach. The second factor was that CNEA is chaired by the head of government and this helped facilitating the process.

Session 3: The Role for the International Community in Enhancing the Private Sector

EU approach to promote the private sector in South-MED countries

Ms. Malin Elander Oggero presented the European Union approach to private sector development and access to finance from a regional perspective.

The European Neighborhood Policy, that dates back to 2004, had the objective of creating a closer cooperation with the neighborhood countries in addition to enhancing the regional economic cooperation. The economic and political scopes have currently changed. Therefore, the stakeholders and the European Commission called for a review for this policy. This review was launched in the beginning of 2015. The main political priority that came out from the review was how the EU can create conditions for stabilization in political, economic, and security terms. Also, the EU wanted to account for the principle of differentiation: we should apply a flexible approach recognising that not all partner countries aspire to EU rules and standards. Therefore the ENP should reflect the wishes of each country as regards the nature and focus of its partnership with the EU. Different approaches should be based on the needs' assessment by each country.



Ms Elander also added that another priority for the EU is on finding ways to achieve economic development along with stabilization and modernization. In that perspective, what was emphasized was that there is a need to enhance economic governance by supporting macroeconomic structural reforms for improved competitiveness and also working for inclusive growth as well as social development. Moreover, the EU works on strengthening partnership with private sector.

She added that by reaching these different objectives, the EU should work with more innovative approaches, such as blending. Blending is currently a common term in the donor community, where the European Commission (EC) provides grants which are blended with loans or equity or other risk sharing mechanisms. With these new approaches the EU hopes to create better conditions for jobs and growth while at the same time mobilising additional funds.

Based on these assumptions, she explained that there is a need to have a more comprehensive approach for private sector development, which addresses all the different levels: macro, meso and micro. We also need to work on the regional and national levels since these two should be complementary. Ms Elander stated that inclusive and sustainable growth should be at the core of our activities.

Ms Elander added that the political dialogue is usually carried out in the Union for Mediterranean where meetings take place at the ministerial and technical levels. As regards trade for instance the EU supports at regional level the Aghadir agreement with some of the MENA countries. As for the national level, negotiations have started on deep and comprehensive free trade areas with few countries. For other countries with a less ambitious approach, the EU is seeking alternatives for cooperation within the existing Trade Agreements.

She explained that at the macro level, the EU works mainly on policy reforms and how to create an enabling business environment. At the meso level, they usually have some activities of institutional capacity of business support organizations. At the micro level, they focus on access to finance and financial inclusion activities. One of the challenges for the EU and the partner Financial Institutions is how to improve access to finance for SMEs, with a particular emphasis on financial inclusion. The EU would like to also mobilize other funds from the private sector as they believe that this has a certain leverage effect.

On the most common way of working to support private sector, Ms. Elander highlighted that this is done through blending so we do that through the Neighbourhood Investment Facility (NIF) in cooperation with financial institutions like the EIB, the EBRD and the EU member states bilateral agencies. And so far, when they have supported private sector through blending, it was mainly in form of regional facilities, rather than bilateral projects. They also need to link this to the delegations, which are made aware when proposals are assessed by the banks. There is also need to verify what works better on regional level and what works better on a bilateral level.

Besides blending, which is usually project based, the Commission also needs to work on the enabling environment which works in parallel with policy dialogue. She added that she would like to illustrate all this with an initiative that has been adopted recently which is the EU initiative for financial inclusion. It was prepared by the EU in partnership with key financial institutions (EIB, EBRD, KfW, AFD) in 2015 to expand financing to MSMEs (including support to innovative start-ups). These are five complementary regional facilities financed through the Neighbourhood Investment Facility (NIF), with different Lead Financial Institutions, representing a comprehensive support package launched in 2016. The initiative addresses different aspects of MSME finance with different instruments:

- Risk capital/venture capital to support business start-ups and microfinance – EIB;



- Guarantee funds to cover losses of local banks lending new funds to SMEs – AfD;
- Advisory services to SME through grants – EBRD;
- SME credit lines and capacity building to local financial institutions – EBRD;
- Microfinance through local financial institutions and capacity building – KfW.

Ms. Elander stated that the EC funding that went to this initiative was 150 million Euros. They pooled resources between the EC and Financial Institutions which may leverage more than EUR 1.2 billion in new financing for MSMEs in the region. The initiative represents a potential to reach up to 200 000 MSMEs in the region, targeting less served populations. The EU coordinates this initiative in order to make sure that a certain complementarity is reached between the banks and activities and also to have a joint visibility with the banks.

Overcoming the challenges to the private sector from a policy perspective and the role of women entrepreneurs

Dr. Nicola Ehlermann explained that many international organizations work in the region and they have different but also a lot of complementarities.

She provided a general overview about the structure and work of the OECD which is an intergovernmental organization that includes 35 member countries that are committed to democracy and market economy. She explained that the approach adopted by the OECD is to compare policy experiences, identify problems, find common answers to those problems and exchange good practices. Most of the time, these are captured in the recommendations or soft law approaches. Most of their instruments are to be transposed by the countries in their own way and according to their own evolution and institutional setup. The work is carried out on intergovernmental groups level and international policy framework. But then it is also coordinated at national level. It is also important to note that OECD works with non-member countries and they are playing an important role. Over the past ten years, the OECD has developed an initiative with the North African and Middle Eastern countries. Within this initiative, they tried to transpose the practices of the OECD into the region. They do not provide funding like the World Bank or the IFC or others but rather stay at the policy advice level. They work at the highest political level in order to steer directions.

Dr. Ehlermann said that the OECD MENA competitiveness program is instrumental for creating a better business environment in particular investment, private sector development and entrepreneurship. We work mostly at regional level. They also engage in trainings and capacity buildings. The areas that are covered are: investment and trade, SME policy and entrepreneurship, business integrity, corporate governance, public private dialogue and women entrepreneurship. They believe that all these areas play together to support an adequate business environment and that they have been working in these areas with governments but also including the private sector. This is a practice that is always adopted in the OECD: when policy areas are being addressed, you consult with the private sector.

Regarding the international organizations and their role in enhancing the private sector, she added that OECD help in setting the institutional framework and developing adequate policy frameworks while listening to the needs of the private sector, as she believes that it is the government which sets the environment and framework for operation. However, it is important that the private sector comes to the table. This public private dialogue needs to be structured.

In terms of impact, she highlighted that the OECD program has exchanged good practices from OECD countries to MENA countries but also between countries from the region. They made contributions towards establishing new rules and regulations, carrying some studies



for the region like the SME policy index and were engaged, through the request by the EU to engage in a program to enhance investments in the Mediterranean.

Overcoming the constraints facing SME development in MENA countries and enhancing access to finance

Marcel Rached, from the IFC, World Bank Group, presented some of the challenges that SMEs face in the MENA countries and their operating environment as well as the lessons learnt from each country.

He explained that IFC is part of the World Bank, which focuses on the private sector in terms of advisory and investment.

Formal SMEs contribute to up 45 percent of employment and up to 33 percent of GDP in Emerging Economies. These numbers are significantly higher when taking into account the estimated contributions of SMEs operating in the informal sector. The missing middles describe the gap in financial services because most of the bank clients are too small to be financed by commercial banks and too big to be financed by micro-finance agencies.

A thriving SMEs sector is a sign of a grown economy and the banking sector has recently realized its importance as a profitable potential. According to official numbers, SMEs typically account for more than 10 to 40 percent of all employment in MENA. However, employment in SMEs is likely to be significantly underestimated in official records. The majority of enterprises in MENA are SMEs and estimated as 23 million enterprises, which is around 90 percent of total business in these countries.

Mr. Rached added that access to finance is one of the main constraints that face SMEs, particularly in the MENA countries.

The majority of enterprises in MENA are SMEs, estimated at 23-19 million (formal and informal) in number and comprising 90-80 percent of total businesses in most countries. Access to finance is one of the greatest challenges facing SMEs across the globe, and particularly for MENA where nearly 63 percent of the MSMEs do not have access to finance.

The total financing gap for MSMEs in MENA is estimated at 210\$ to 240\$ billion (of which formal MSME finance gap is estimated at 180-160\$ billion). A recent World Bank/Union of Arab Banks survey of over 130 MENA banks shows that only 8 percent of lending goes to SMEs across MENA, and even less in GCC countries at 2 percent. This is substantially lower when compared to the middle income countries lending average of 18 percent and high-income countries average of 22 percent. Regarding the operating environment, there are also some constraints facing the MSMEs, for instance the sealing of interest rates do not necessarily help the MSMEs, the legal framework is also a constraint both on the supply and demand side. On the demand side, the MSMEs do not enjoy enough capital to be able to register and to formalize themselves. On the supply side, banks hesitate to finance them due to lack of a higher risk appetite. The third constraint is the macroeconomic factors.

As part of the work for the G20, the SME finance subgroup identified some lessons learned from different markets:

- First, to develop a country specific strategy and this is to account for the different dynamics in each country. For example, in Malaysia, there has been an initiation of an SMEs corporation that ensures effective collection of data which is key to understand where these SMEs exist. This also helps to avoid over restrictive licenses requirements to significantly increase competition levels.



- Second, the infrastructure that requires to be strengthened for improved transparency. Many countries in MENA lack a transparent auditing system and credit bureaus and registries.
- Third, some countries initiated SMEs rating agencies like in India.
- Fourth, infrastructure for VCs and for private equities like in Brazil Inovar Program which is a VC to strengthen new technologies in SMEs in specific sectors.

Moving to the effective public sector intervention, Mr Rached offered BDL as an example which has been incentivizing SMEs for years. They allow stimulus packages to be able to support SMEs locally.

Finally, the key elements in driving financial institutions to serve SMEs are the following:

- **Business Model:** Various business model options, which are not mutually exclusive, include retail-based for mass market, advisory differentiated, segment-based, supply chain linked, mobile money-based, niche markets positioned (e.g. women in business), and alternate financing models.
- **Segmentation:** Typical approaches to segmentation are industry led, sales turnover, profitability, geography or customer need based, and gender; these not being mutually exclusive. A powerful segmentation can help define a bank's participation model and help optimize costs. **Products and Services:** These include heavy customization of products, Islamic and non-Islamic banking provision, non-financial advisory provision (e.g. training), and information dissemination. Moreover a strong cross-sell focus and bundling of products. Also customer value proposition aligned branding, campaign and communication strategy is needed. **Sales and Delivery:** for small SME volumes, and investment in alternative channels not only enhance customer experience but also help reduce operating costs. Specific customer acquisition, activation, retention and churn policies are required. **Organization and Systems:** upgrading of IT platform for achieving scale, investment in loan origination platform, credit scoring, credit approval factory, data warehousing, loan management systems, CRM, analytics etc.
- **Risk Management:** Pricing needs to incorporate data driven risk scoring, development of statistical application and behavioral scoring, strong portfolio management, operational risk management, strong collections framework, and participation in risk sharing facilities driven by government entities etc.

He concluded that IFC had adopted a model that serves SMEs on the investment side and on the advisory side. He noted that SMEs sector is not only the missing middle but it is at the core of our economies and the opportunity is still within reach.

Why international cooperation is still essential to develop an efficient and vibrant private sector in South Med region?

Dr. Emmanuel Noutary introduced the ANIMA Investment Network, which was established 10 years ago with the main objectives of: promoting the economies of the Mediterranean countries, to contribute and to favour networking and cooperation between economic actors from European and Mediterranean countries.

Following its 10 years of creation, Mr. Noutary confirms that there are some challenges and priorities for the private sector. He added that there is a sort of resilience in the MED countries despite the political instability and the economic crisis. The economies are sort of stable, foreign investments have not been really decreasing compared to the populations growth. There is a ceiling on FDIs (2.5 percent of the global FDIs) compared to the population of MED countries in the global world population. There is also a sort of sector rotation in these countries where most of FDIs are in 5 major sector representing 50% of FDI flows amounts (Energy, Telecoms, Cement, Banks and concrete works). These sectors have long-term effect in job creation although they have a little short term job efficiency.



Since the last three years, we have seen the share of FDIs in the new industrial sector like food, health, mechanical technology increasing and reaching almost 50 percent of total FDIs, which are more contributing to industrial value creation and short term job creation.

However, he added that the last 10 years have showed that there is a sort of lack of efficiency: the reforms made in terms of liberalization, transformation, reforms of institutions and creation of infrastructures for investments and new financial tools were insufficient to bring results on social development. There is also a sort of lack of coordination between education, research, industrial and attractiveness policies. Research and Development is still mostly concentrated in public sector. So, this hinders innovation as well as South-South industrial value chains. So in the end, we have a low job creation. Overall, we have a challenge of inefficiency in institutions dealing with the private sector. They have to be more efficient and learn from best practices from abroad.

On the enterprise side, there is a lack of impact and positive spillovers. ANIMA developed tools to monitor economic and social spillovers from investment projects in order to allow companies and territories to better monitor the expected impact and develop win-win deals.

In conclusion, Mr. Noutary said that the MED countries need a new economic vision based on sustainable and inclusive development as well as value creation.

Discussions

The discussions in this session revolved around the following:

On women entrepreneurship:

Ms. Nicola Ehlermann added a comment on women entrepreneurship by stating that at the OECD they use the term "missing middle" for women: those who are not at the traditional rural areas neither those that are working for big companies. These women, while they have high educational attainment, they do not make it into the labor markets. But more competitive thinking is needed, in Norway for instance, it has been proven that the growth provided by the integration of women in the economy is more than growth generated by oil. Ms Ehlermann stated that when you integrate an additional set of skills you create more growth and become more innovative. So the OECD MENA initiative will focus in the next 5 years on how to mainstream womens' participation. Also, a point that needs to be mentioned, when it comes to business development services they are absolutely indispensable, but we often see that these services do not know where women entrepreneurs are and accordingly cannot target them. On the other had, Ms Ehlermann stated that well-trained women may not know what they would need to set-up their business.

Dr. Raed Safadi made the comment that there is no evidence that women have less access to knowledge and finance relative to men.

On the IFC and the EU initiatives for private sector:

Dr. Raed Safadi raised some questions on whether lending to SMEs is profitable to banks. Experience is Lebanon and other countries in the region and even some OECD countries prove the contrary. In fact, the impact of Basel III could be negative on SMEs.

Dr. Alain Santi asked whether IFC directly lend SMEs or through banks. Does the IFC lend banks to lend on cash basis and not on collateral basis? Also, how the IFC tackles the informal sector?

Dr. Marcel Rashid replied to these questions by saying that 60 percent of the profitability of banks come from non-lending. Banks have not done the necessary homework to be able to trigger these risks and to address SMEs sector. He added that they work with regulators to



be able to bring these SMEs the correct products that they need. One of the key challenges is creating registries.

Another question was raised on the diversity of instruments thrown at the region on the private sector, is that all necessary with the presence of refugees and migration. Do the international organizations do something regarding business creation? Also, can we save all the money by promoting export oriented strategies and allowing SMEs to enter the EU markets?

Dr. Malin Elander Oggero responded to that question by saying that the EU stepped up its support to private sector and this is quite recent. Today, the EU does a lot on bilateral level with individual countries and also through regional programmes. The private sector is quite new to the EU, they have not yet got at the aggregate level a lot of results. At the project level, they have quite good results when it comes to reach out and lending to SMEs, especially through structural funds. As for focusing more on export oriented enterprises, they do that as well but this is also quite new for the EU. We work on trade, competitiveness and enhancing value chains. On migration, the financial inclusion initiative was launched in 2016 so no results are in yet.

Another question was raised where do we see the added value of the EU in its intervention in the private sector in the region?

Mr. Malherbe made the comment that the EU should put more emphasis on the monitoring and evaluation process. One way of doing this is to have a scoring system to generate a competition among implementing agencies. Ms. Char added that evaluation reports should be heavily disseminated and lessons learned should be discussed with relevant stakeholders.

Dr. Noutary said that the next stage in ANIMA is to certify some services and rating tools for performance to overcome the inefficiencies.

Session 4: Roundtable Discussion and Closing: Way Forward for the Private sector in South Med

Dr. Raed Safadi started this session by asking each panelist to conclude what they have taken from the workshop.

Dr. Simon Neaime mentioned that the macroeconomic environment is important. The region has faced the financial crisis in addition to the political stability in MED countries. This added to the fiscal and monetary problems that already existed: budget deficits and public debts. In response to this crisis, the FED reserve of the US had to inject trillion US Dollars. In Europe, the ECB has been conducting monetary policy. The fiscal policy still being conducted by the governments. Some EU countries are facing a debt crisis like Greece, Italy, Portugal and Spain. Turning to the Middle East, Jordan and Lebanon for instance are facing high debt to GDP levels, deficits and adopting fixed exchange regimes. Egypt has recently made a good move and adopted a free-floating regime. Overall, the fiscal space is shrinking. It appears we are really moving in a tight environment and we need to address the right tools. For the austerity measures, we need to get those economies back to the growth path and then perhaps see how policies need to be shaped for the future to prevent debt and currency crisis from happening.

Dr. Galal said that the discussion was about the private sector, not only the SMEs. It was good to learn in which way the macro environment affects private sector, constraints facing different enterprises and especially SMEs, and how the donor community can help the process of transformation in the region.

He added that three things were missing or not sufficiently integrated in the discussion:



- First, politics. Those who believe that all what we need to do is only technical solution are wrong. There is "politics of policies". The calculus of politicians is different than economists. Economists prefer optimum solutions. This applies to poor countries as well as EU and US. Politicians choose which policies to adopt on the basis of political benefits, not always according to wellbeing.
- Second, the approach. Most of the discussions looked at enterprises by size. The informal sector is also made of rational people. Due to market constraints, they conclude that it is better to stay informal. Therefore, formalization should be useful and beneficiary for them. Improving the formal business environment should be an incentive to moving from formal to informal.
- Third, we should worry about the details. It is not good enough to suggest things that look useful, we need to worry about how these suggestions could be implemented.

Dr. Malin Elander Oggero made the comment that regarding the informal economy, this is a real challenge for the EU. They have an interest to work with the countries on the policy dialogue to tackle this topic of formalization. Another topic, a huge part of SMEs do not want to have access to finance because it is too complicated. So how do we address this and how can we reach them? This is also a challenge for the international community. Another challenge is what do we do if we cannot have a policy dialogue with a certain country.

Mr. Emmanuel Noutary said that we need a broad vision for the MED region and then we can go to details. We need an inclusive society where everyone is part of the distribution. The social impact of policies should be taken into consideration before validation. Private sector should be advocated and convinced that contributing to wealth and social development will lead to a better competitiveness of the companies. Being inclusive and responsible in the conducting of business means sourcing locally and thus reducing costs and supply chains risks. It means also reducing social risks and turnover. It also means a better loyalty from the companies' stakeholders (clients, workforce, communities, public authorities). Another important topic that was not tackled is the employability and education. If we talk about attractiveness of private sector, it is about infrastructure, aligning policies, having the capacity to employ people.

Ms. Marie-Jo Char mentioned that helping MED countries creating a conducive business environment to unlocking the potential of the private sector and to create more jobs in the MED region is a complex and political issue, although there is fairly widespread consensus regarding the policies required to do so. A holistic approach would be difficult to adopt; also, she asked whether a top down or bottom up approach would be more efficient? This still needs evidence. Furthermore it would be important to help MED countries not only to develop but more importantly to implement a national strategy for private sector/SMEs development. The involvement of the private sector through a structured and efficient policy dialogue is very important.

Another issue raised that would contribute to business competitiveness is to encourage regional economic integration and South-South policy dialogue, as countries in the region are not close to each other.

Dr. Raed Safadi said that we should not believe that whatever we push for in terms of optimization will be adopted by politicians. Moreover, the services will remain to be a forgotten aspect in regional integration. Moreover, he added that even technocrats choose politically sound decisions rather than an economically supported one.

Discussions and questions

Dr. Zafiris Tzannatos made a comment on the corporate social responsibility (CSR) issue which is related to the private sector. He said that the difference of outcomes in different



countries in Europe depended on the competence of government. In terms of outcomes, bad policy that is implemented is better than good policy that is not implemented. He added that the macro and micro sides are linked through the banking sector. They are here to serve the real economy and this side tends to be forgotten in this micro policy analysis.

Mr. Malherbe made a comment on a dimension that is rarely mentioned when talking about private sector development which is involving the civil society in dialogue because it is this civil society that can make the government accountable. It is worth also working with journalism and media in order to increase people awareness of the policies that are being adopted.

The panelists responded to these questions and comments:

Dr. Neaime said that regarding the macroeconomic environment, the fiscal and monetary policies are constrained. The solution is to unlock the private sector and this should be on top of the adjustments reform agenda. The private sector has a lot of potential to achieve growth.

Dr. Galal mentioned that regarding engaging the civil society, he thinks the theory of change implies that the best way is to share as much as information as possible, including civil and non-civil society and they will make enough pressures on policy makers. Regarding SMEs, given that they represent a large number of people, politicians do well by trying to please them. But, to apply this we should have an open society and this is not the case in many countries in the region. As for the Arab economic integration, it is more of a hope rather than reality for good objective reasons. Until these reasons are resolved, no integration can successfully happen. On the corporate social responsibility, he said that the government is the one responsible to achieve social justice and we cannot count on corporate social responsibility.

Mr. Noutary reckoned that the private sector cannot replace governments. However both can develop partnerships and win win relationships – employers' federation in Morocco or Tunisia are already paving this way. Regarding integration, he added that ANIMA conducted a survey with private sector representatives in Maghreb and found that they report being unaware of the opportunities on the neighbouring markets and lacking of opportunities to meet other businessmen in the neighbouring countries.

Dr. Raed Safadi concluded this session by saying that what one needs to do regarding the private sector development is to think about the incentive structure and maybe implicitly *locking* the public sector through reducing the benefits presented there.