

The Impact of the Global Economic Crisis on SMEs in the MENA Region

MENA and the Crisis

Four groups

- ❑ GCC countries
 - ❑ Reform Countries (Egypt, Jordan, Tunisia, Morocco)
 - ❑ Central Command: social legacy (Syria, Algeria)
 - ❑ Poor Countries and political uncertainties (Yemen, Sudan, OTs)
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How did they Respond

- State of denial
 - Limited Impact and varies across countries
 - Admit .. Then what ?
 - Arbitrary policies
 - Solutions from outside
 - Lack of comprehensive polices
 - Unilateral approach except the GCC
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An Overview:

The role of the SMEs in the MENA economies according to the MENA-OECD Investment Programme:

- ❑ Over 90% of the SMEs employ less than 50 employees
 - ❑ Contribute to over 2/3 of total formal employment (Proportion of employment in firms that have less than 50 employees)
 - ❑ A significant share of value added
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How the SMEs are going to be affected?

- ❑ Sectors' Specific Factors
 - ❑ Uncertainty
 - ❑ Credit Crunch
 - ❑ Slow Down in the Economy (Domestic and Export demands)
 - ❑ Public Spending – priorities
 - ❑ Quality of the Institutions
 - ❑ Savings –disposable income
 - ❑ Formal vs. Informal
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For Example leb. Most industrial enterprises engage in one of eight sectors namely:

- ❑ Food and Beverage (20.3%)
 - ❑ Metal Products (16.1%)
 - ❑ Non-metallic products (11.5%)
 - ❑ Furniture and assimilated products (10.7%)
 - ❑ Clothing and fur (10.3%)
 - ❑ Wood products – excluding furniture (10.2%)
 - ❑ Leather and Tanning (5.9%)
 - ❑ Textiles (3.7%)
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Tunis Moroc. And Egypt

- More export oriented
 - Textilehence they have been adversely impacted more than Lebanon or Jordan where SMEs are producing for the domestic market.
 - Egypt...overall slow down and SMEs also have been marginally affected
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Institutions and Business Environment

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- Early signs point to declines in growth rates in the fourth quarter of 2008 in many countries, and growth projections for 2009 are lower than 2008 levels in all MENA countries with the exception of Qatar.
 - As a whole, the MENA region is projected to grow at 3.3% in 2009 down from 5.5% in 2008. However, MENA is expected to be less impacted by the global recession than most other developing regions.
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Slow down : Foreign and domestic

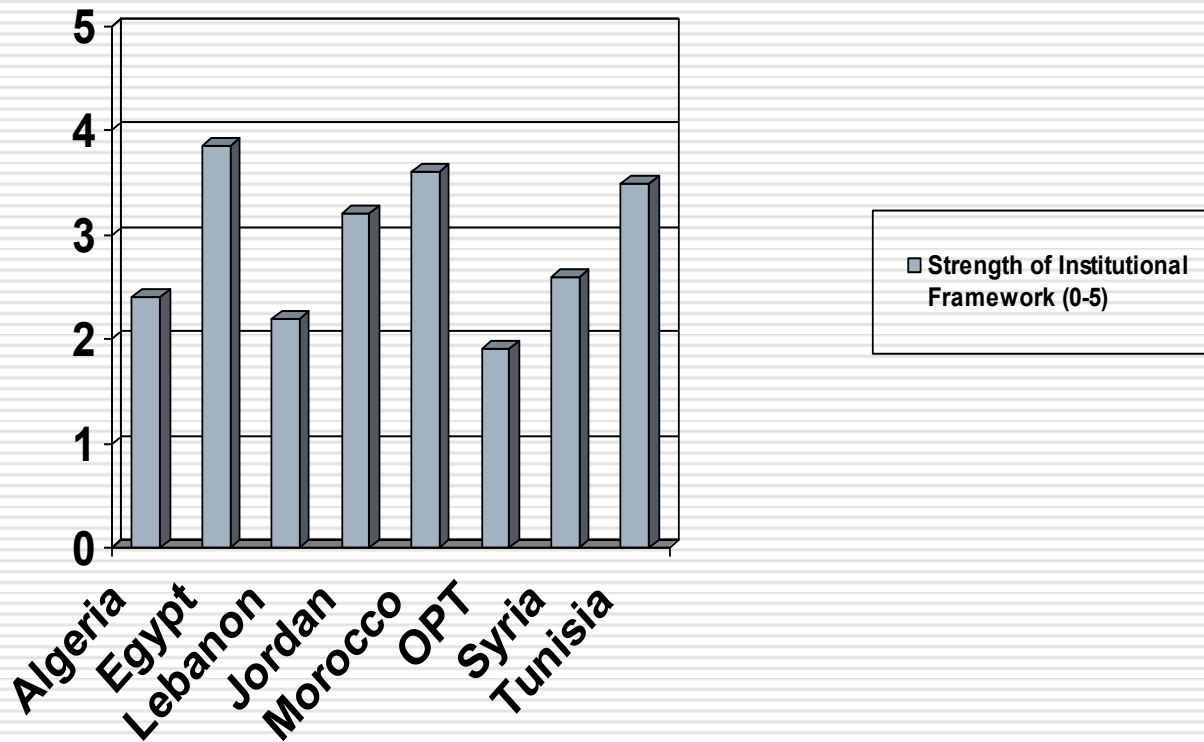
- ❑ Export decline (Jord. Morco. Tunisia)
 - ❑ Growth slow down but not a recession
 - ❑ Expected Growth 2009 Jordan(4 %), Tunis (3 %) , Moroc. (4 %), Egypt (5%), GCC positive growth,
 - ❑ Slow down result in Higher unemployment (Egy. Leb. Syria)
 - ❑ Workers' remittances (Jord. Egypt, yemen, Syria , Leb)
 - ❑ Less FDI
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What has been the impact so far on the real economy in MENA?

- Although financial systems in MENA countries have not been highly vulnerable to the crisis so far due to their limited integration with global financial institutions, the impact of the global recession on the real economy can be significant in many MENA countries. The SME finance supply chain was still robust at the end of Q2 2008, however, the deepening of the recession has reduced expectations of SMEs' future earnings and the deepening of the financial crisis has impacted lenders.
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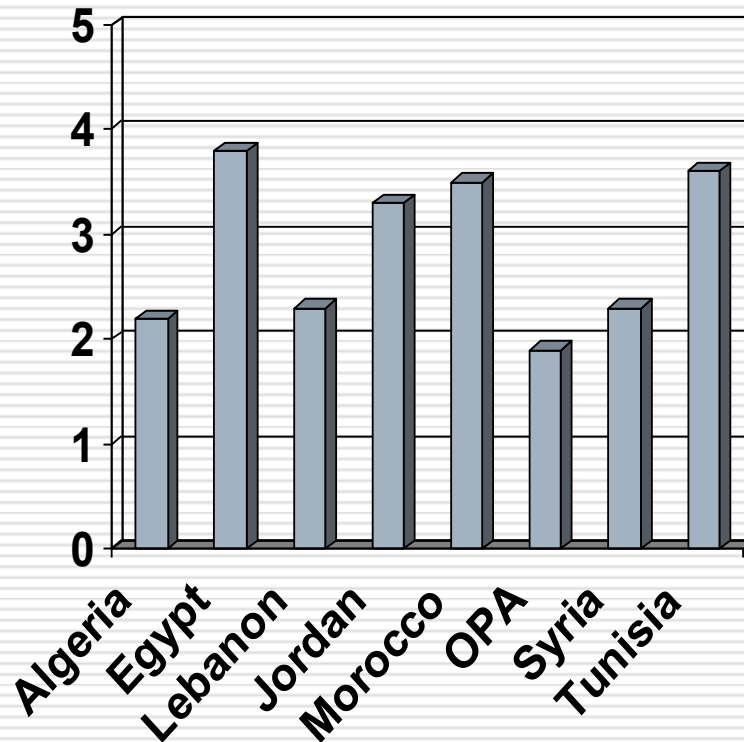
Institutional framework for enterprise policy:

- Delegation of responsibility for enterprise policy
- Co-ordination with other ministries
- Enterprise development strategies
- Clear task assignment

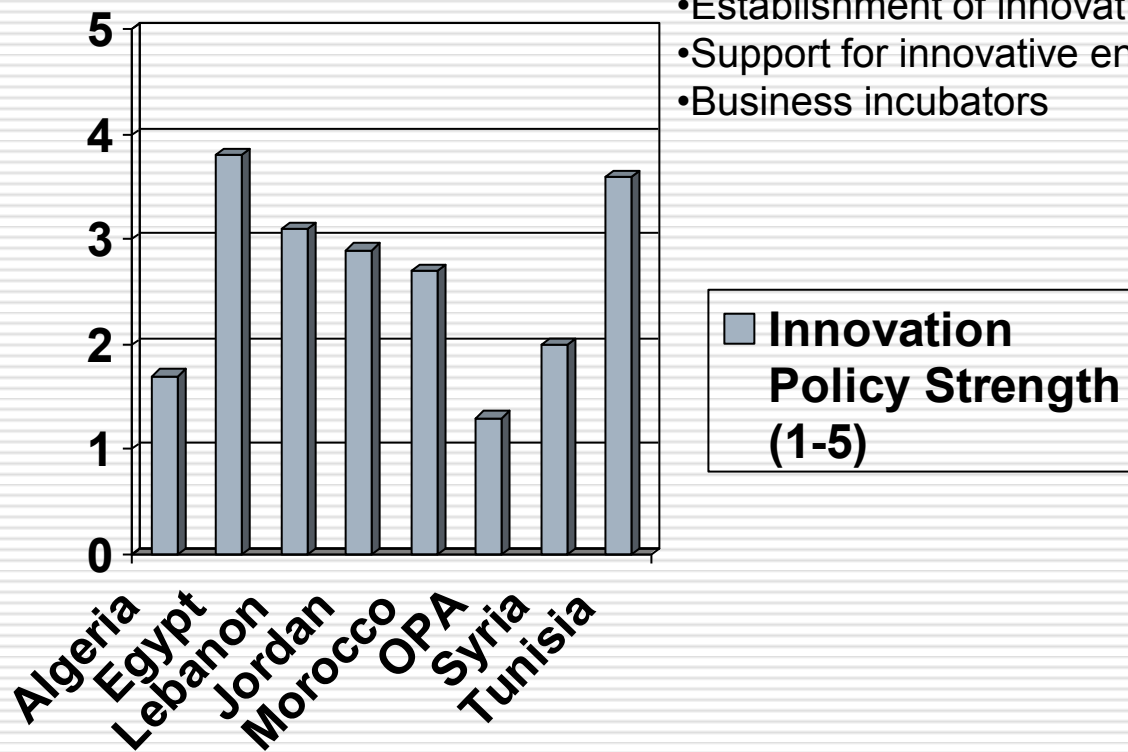


Source: OECD/EC (2008), Euro Med Enterprise Policy Assessment: Dimension 1, sub-dimension 1.1

Quality Business Support Schemes and Services Strength (1-5):



- Range of business services
- Availability of information
- Access to business services
- Business establishment support services



- Enhancing enterprise innovation
- Establishment of innovation and technology centers
- Support for innovative enterprises
- Business incubators

Public Spending

- ❑ GCC can afford that
 - ❑ Other countries are running budget deficit
 - ❑ They target big projects
 - ❑ They tightened monetary policies
 - ❑ Ignore SMEs and informal sector
 - ❑ The outcome has been limited
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Enterprise financing – A challenge in MENA countries

- Financing difficulties can be due to a range of issues related to the depth of the financial system, regulatory or legal gaps or asymmetric information
 - Marginalization of SMEs in emerging economies:
 1. SMEs and informal enterprises account for 60% GDP, 70% employment
 2. Macroeconomic imbalances
 3. Larger informal sector
 - MENA region not “extraordinary” in this sense but extent of the problem varies by country:
 1. Legal system, liquidity in the economy, corporate governance standards, banking and capital markets development
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Distinctive challenges facing SMEs financing:

- ❑ Difficulty distinguishing financial situation of the firm from owners
 - ❑ Monitoring more demanding
 - ❑ Wide variance of profitability and growth
 - ❑ Relationship between firms and stakeholders personal
 - ❑ Good corporate governance principles difficult to enforce in family enterprises
 - ❑ Asymmetric information
 - ❑ Structural rigidities and distortions:
 1. Domestic savings-investment imbalance
 2. Legal, institutional and regulatory framework
 3. Structure of the financial system
 - ❑ Result: High collateral requirements, high rejection rates, informal finance, particular problems for enterprise with intangible assets.
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Enterprise financing obstacles vary by country:

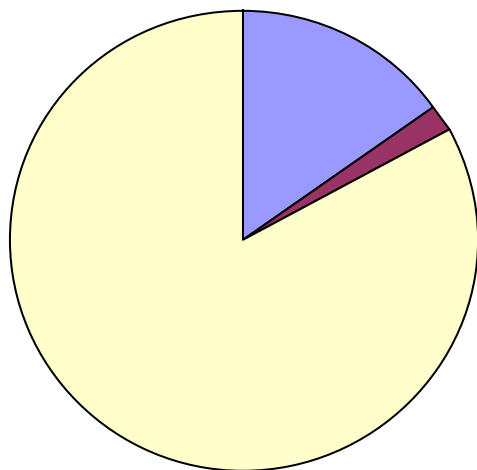
- ❑ Sources of finance to emerging enterprises particularly weak in Egypt, Morocco, Tunisia, Jordan
 - ❑ Lebanon and Palestine present a particular challenge because of high demand of SME support and guarantees
 - ❑ In Lebanon, challenge to deal with explosion of financing demand following the war
 - ❑ Tunisia, Morocco, Syria – private sector risk averse, awaits public lead
 - ❑ Algeria and Syria – banking sector still state dominated
 - ❑ High urban rural divide in many countries
 - ❑ Development of capital markets highly variable, obstacles to IPOs
 - ❑ Several instruments of enterprise financing such as trade credit, leasing VC at early stages of development
 - ❑ Other parameters such as insolvency legislation, monetary policy, credit registry, lack of definitions play an important role
 - ❑ Egypt: lack of a clear policy towards SMEs development, lack of a unified operational definition for the target grp, lack of sufficient and adequate information on the sector and lack of coordination amongst the various institutional actors
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Other financing challenges in MENA:

- Limited competition in the banking sector: high barriers to access
 1. Market is highly concentrated by top 3 banks which on average hold 83% of all commercial assets
 - Limited foreign ownership of banks in some countries, while some countries have opened up banking sector to competition
 1. Egypt: OECD's FDI restrictiveness Index
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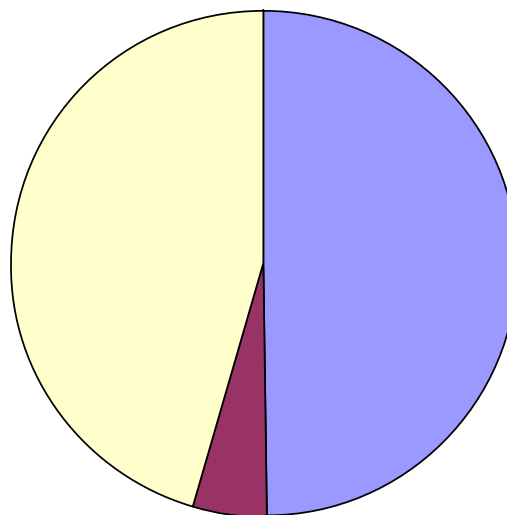
From Bank Dominance to Stock Market Emergence

Middle East Capital Markets Structure, 2003



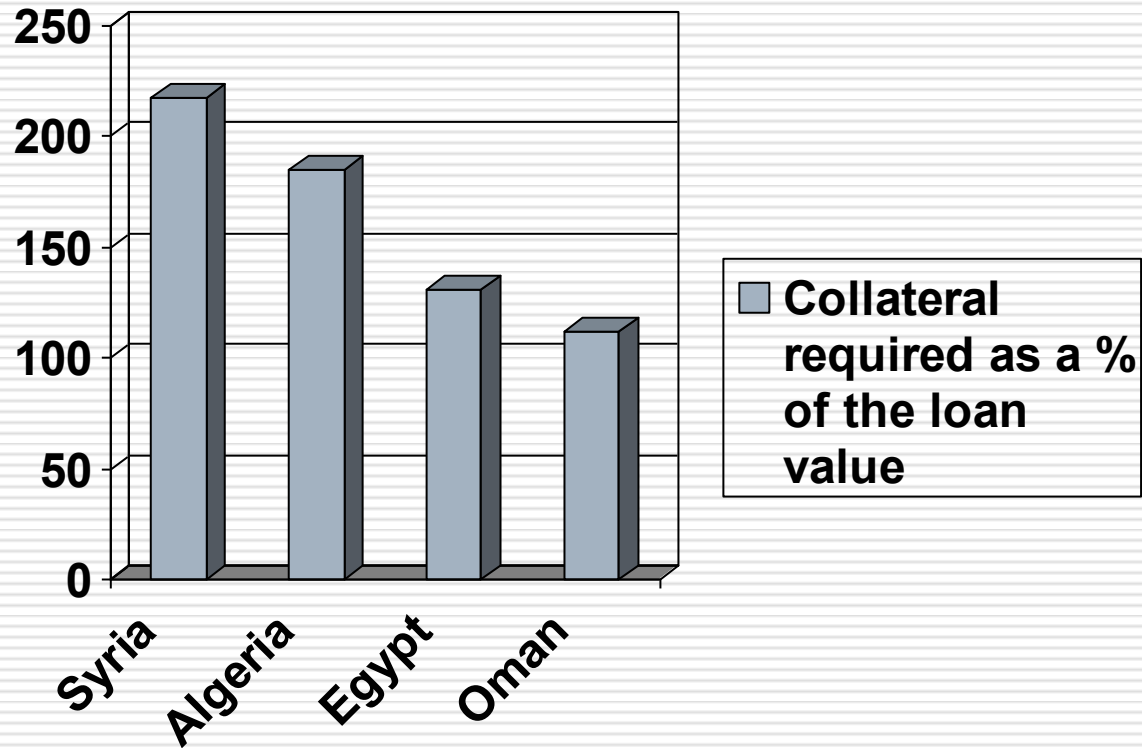
- Stock Market Capitalization
- Debt Securities
- Bank Assets

Middle East Capital Markets Structure, 2007



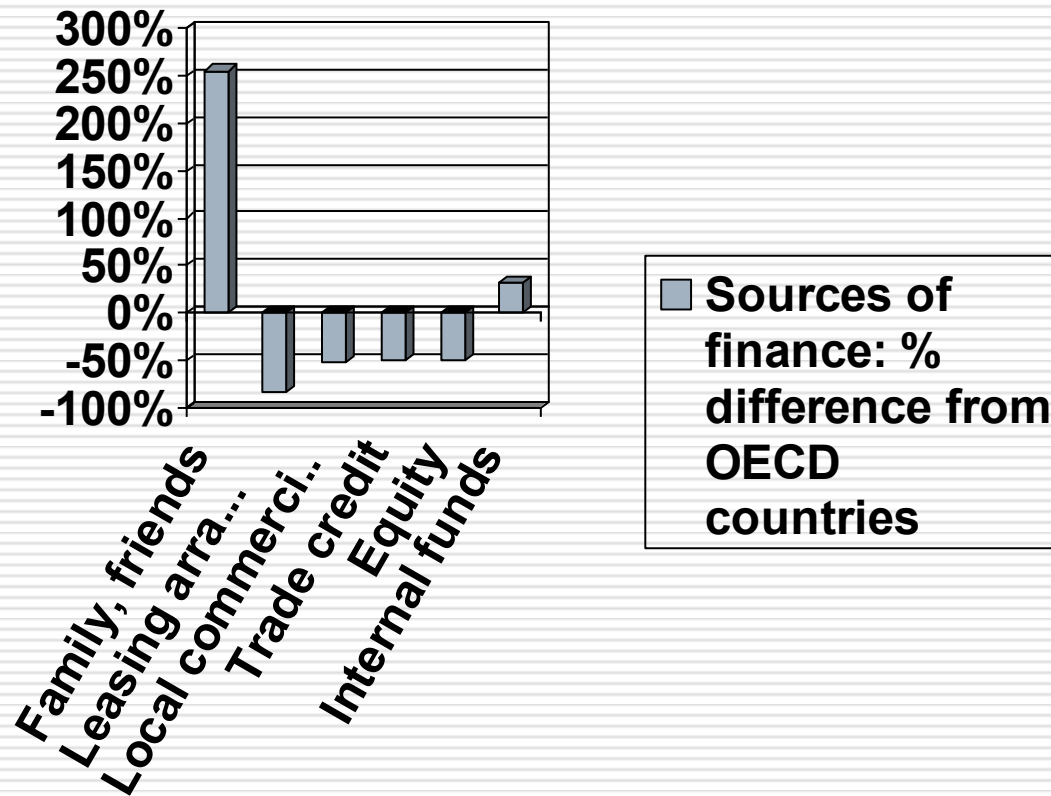
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High collateral requirements in some MENA countries:



Source: WB Enterprise Surveys. Data for MENA countries is for Algeria (2002), Egypt (2004), Oman (2003) and Syria (2003)

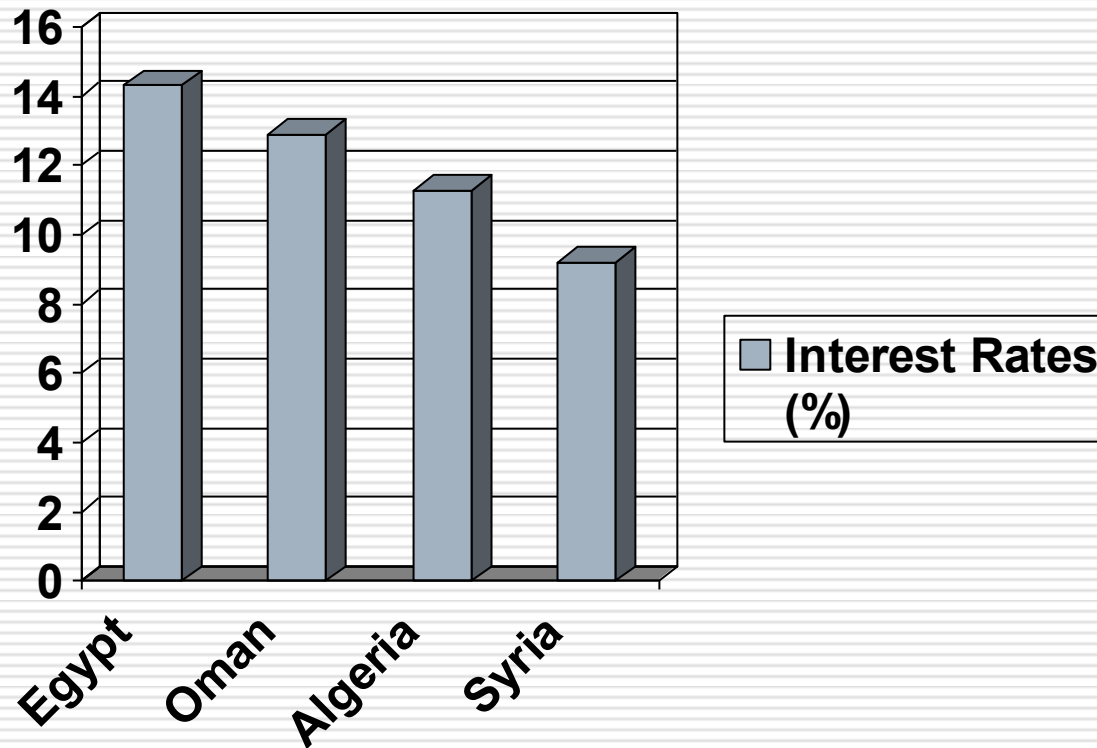
Reliance on other sources of finance in MENA



What is the current situation in MENA countries?

- High cost of capital relative to OECD countries:
 1. High interest rates used to compensate for the lack of credit related information
 2. Credit bureau lacking
 - Low overall pool of credit to the private sector in comparison with OECD countries
 1. Low credit ratios to GDP in a number of countries
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High Cost of Capital



Source: WB Enterprise Surveys. Data for MENA countries is for Algeria (2002), Egypt (2004), Oman (2003) and Syria (2003)

Low ratios of credit to GDP:

Domestic credit to the private sector (% of GDP)

Egypt	57
Jordan	88
Lebanon	78
Morocco	54
Oman	31
Qatar	35
KSA	53
Tunisia	65
UAE	61

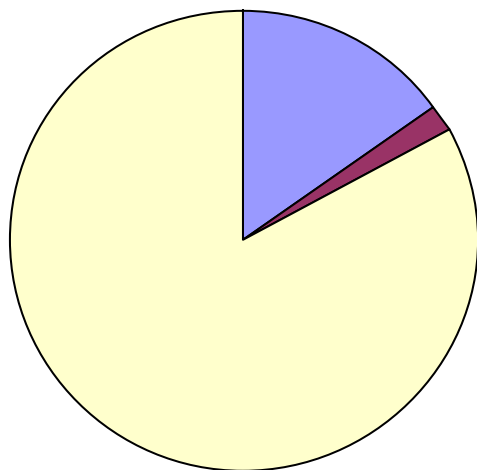
Source: WB, World Development Indicators

Impact on Banks:

- ❑ Visible impact on banks has been limited so far
 - ❑ Credit has slowed down due to uncertainty, weakening real estate market, bearish export financing
 - ❑ Only some Gulf Bank of Kuwait has needed a bailout
 - ❑ Some banks may have suffered due to a decrease in return on their investments in international banks or in foreign currencies
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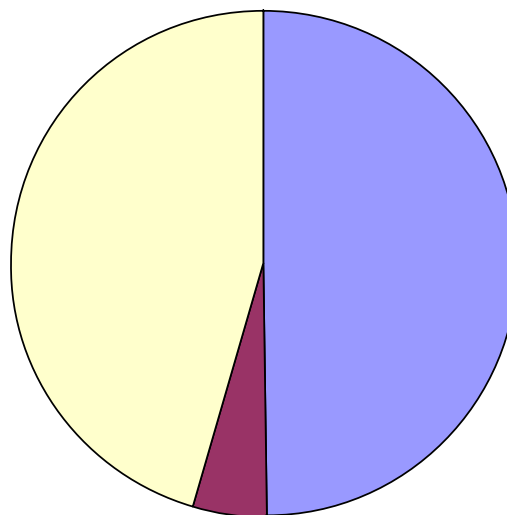
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How to respond:

1. Increase SME awareness:

- ❑ SMEs are not aware of financial products offered by banks and other lending organizations
 - ❑ Many SMEs are also inexperienced in developing business plans, which is key for expressing business objective and growth to lending agents
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Options to consider:

- ❑ Facilitate access to capital markets by establishing secondary tiers with easier access restrictions
 - ❑ Use existing state facilities
 - ❑ Consider providing fiscal or other incentives to financial institutions lending to SMEs (strategic sectors to consider)
 - ❑ Consider providing credit guarantee schemes to reduce risk aversion by banks
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Solutions to “close the gap”:

- **Attempt to streamline and simplify administrative and financial obstacles:**
 1. **Doing Business 2008 shows large improvements in administrative simplification**
 2. **Minimum capital requirements still high in some cases**
 - **Private sector response:**
 1. **Islamic SME PE fund**
 2. **Bahrain: micro credit**
 3. **Credit lines from forging source**
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The Road ahead

- 2009 is going to be difficult
 - Banking is getting more tough and more conservative
 - Monetary policy has been relaxed
...low $\text{\textcircled{R}}$ but not easily lending
 - SMEs were not particularly targeted with the exception in Morocco, Tunisia and Egypt.
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