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“Financial development and Micro, Small, and Medium Enterprise : Engines for the Euro-Mediterranean economic stability and growth”

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Report

I. INTRODUCTION

1. The Euro-Mediterranean region is facing a series of challenges due to the lasting political instability of many countries and to the difficult national reconciliation processes, such as those of Syria and Libya. Besides, extreme climate-related disasters sharply increase uncertainty for businesses, and, in many cases, outdated national legislations and trade borders are perceived as obstacles to integrated economic growth and financial inclusion in the region.
2. Such challenges limit the implementation of ambitious policies meant to foster and stabilise the economic sector in the region. The Parliamentary Assembly of the Mediterranean (PAM) is convinced that national economies in the region need urgent co-ordinated political actions to rebuild trust, foster business inclusiveness and improve livelihood conditions for all citizens.
3. In this regard, micro, small, medium-sized enterprises (MSMEs) and start-ups, are essential to boost innovation, job creation and local development, while financial inclusion, new technologies and youth serve as key drivers to the establishment of new dynamics and sustainable development synergies. However, despite their considerable economic potential, these sectors and actors are still facing major challenges that hinder their progress.
4. In addition to macro issues, the region is confronted with national financial crises, such as the one that has recently hit Lebanon, with effects propagating to the economy of neighbouring Syria.¹

¹ Al-Khaleidi S., “Lebanon crisis wreaks havoc on Syria’s war-torn economy”, Reuters, 29 November 2019, <https://www.reuters.com/article/us-syria-economy-lebanon/lebanon-crisis-wreaks-havoc-on-syrias-war-torn-economy-idUSKBN1Y3117>

II. FINANCIAL CONSTRAINTS FOR EURO-MEDITERRANEAN MSMEs AND START-UP: AN ENDEMIC ISSUE

5. Throughout the Mediterranean region, MSMEs generate more than 90% of new jobs, while according to the European Investment Bank (EIB), in the European Union in particular, SMEs and Mid-caps represent 99% of businesses, and employ two third of the active working population. Despite the fact that SMEs and start-ups represent the backbone of Euro-Mediterranean economies, their access to financial instruments remains a critical issue. Improving SME's financial inclusion could increase economic growth, job creation, and fiscal and monetary efficiency and could also contribute to financial stability.²
6. State representatives and senior experts, who attended the recent ISPI/MED Dialogue high-level conference in Rome, highlighted that financial development is crucial for the Mediterranean region, which accounts for more than € 3.500 billion in commercial trade and has many possibilities to prosper. In this regard, it is useful to reflect on the opportunity to shore up the financial system for the entire region, as financial inclusion and accessibility foster job creation, support entrepreneurs in developing their businesses and reduce income inequality.
7. However, costly listing requirements, financial illiteracy, information asymmetries, a non-conducive business environment, and lack of access to finance are blocking the development of a sound and thriving Euro-Mediterranean MSMEs ecosystem.³
8. Access to finance for MSMEs and start-ups remains a challenge as shown by researchers.⁴ In 2013, while roughly 6% of MSMEs in Egypt successfully received bank loans, large companies reached 18%. In the same period, in Jordan approximately 8.5% of MSMEs had access to loans, although three out of four applications for funds were successful.
9. The GEM Global Report also stresses that the lack of financing is identified as the main breakpoint factor which leads SMEs, and especially start-ups, out of business in early development stages.⁵ Looking at the data, it is possible to notice that the vast majority of start-ups rely considerably, at the beginning of their activity, on personal resources rather than financial opportunities as concrete options.⁶
10. According to the World Bank Enterprise Survey, political instability is considered another major factor behind investment decisions that negatively impacts sound financial flows, forcing business owners to embrace a 'wait and see' attitude. This trend is further confirmed by

² 'Financial inclusion of Small and Medium-Sized Enterprises in the Middle East and Central Asia', International Monetary Fund, Paper no. 19/2, 2019.

³ The Mediterranean Middle East and North Africa 2018, SME Policy Index, OECD, 2018 https://read.oecd-ilibrary.org/development/the-mediterranean-middle-east-and-north-africa-2018_9789264304161-en#page1

⁴ "Micro, Small and Medium Sized Enterprises Development in Egypt, Jordan, Morocco and Tunisia", EMNES Studies, December 2017, http://emnes.org/wp-content/uploads/2017/12/emnes_study_003-msmes-development-in-the-southern-mediterranean-countries.pdf

⁵ "Global Entrepreneurship Monitor", Global Report 2017/8, 6 April 2018, <https://www.gemconsortium.org/report/gem-2017-2018-global-report>

⁶ Sandri S. and Alshyab N., The Impact of Institutional Uncertainty on Employment Generation Perspectives of Firms in Jordan, *EMNES Working Papers*, 2018.

specialized reports⁷ showing the negative impact of institutional uncertainty on growth and job creation in Jordan.

11. Nevertheless, women, youth and migrants are the most vulnerable individuals and encounter greater obstacles when trying to access any type of bank finance, especially in developing countries, where 80% of firms are excluded from formal financial sectors.⁸
12. Despite the information highlighted, new technologies and digitalization need to be duly taken into account. Digitalization plays a key role in new businesses and is expected to unlock new chances for young entrepreneurs, MSMEs and Start-ups through more efficient business models and to facilitate access to alternative credit. Digital financial instruments will also develop financial inclusiveness, having the capacity to reach rural regions and marginalised realities, otherwise excluded from business opportunities.
13. New technologies will create smarter business environments and more technological skilled figures through remote and offshore jobs. This means that a robust inclusive digital economy will enable an increasing number of firms to offer their services and products remotely thanks to 5G and 3D printing technologies.
14. In addition to that, Fintech must be analysed with great attention, as it is changing SMEs' financing and has generated growing interest among policymakers. Developments in recent years illustrate the potential of Fintech as an alternative source of financing. Fintech innovations can support SMEs' financing, including credit provision and equity capital, both by facilitating bank credit supply and by opening new lending channels.⁹
15. As a case in point, Fintech is nascent in the MENA region and its development has accelerated in recent years. The UAE, Lebanon, Jordan and Egypt host three-fourths of the MENA startups and have established large Fintech accelerators. Fintech companies have focused primarily on payment solutions, marketplace lending, and crowdfunding, including for SMEs. Moreover, the MENA region is also characterized by a high share of youth and migrants in the population, an increasing use of digital commerce, a large informal economy, and a strong need for economic and financial diversification. In this context, Fintech could underpin greater financial inclusion of SMEs and underbanked population groups.¹⁰
16. According to the OECD,¹¹ some States already amended their legislative frameworks in order to promote exports and open access to financial markets. Despite these efforts, concrete instruments to support the internationalization of MSMEs are still weak and inappropriate. In this regard, the role of policymakers remains fundamental to prevent the abuse of these technologies and use them as a unique opportunity, alongside with the private-public partnership which could close the gap of public financial restrains.

⁷ Ibid.

⁸ "Enhancing SME access to diversified financing instruments", *OECD*, 22-23 February 2018, Mexico City, <https://www.oecd.org/cfe/smes/ministerial/documents/2018-SME-Ministerial-Conference-Plenary-Session-2.pdf>.

⁹ 'Financial inclusion of Small and Medium-Sized Enterprises in the Middle East and Central Asia', *International Monetary Fund*, Paper no. 19/2, 2019.

¹⁰ Ibid.

¹¹ "The Mediterranean Middle East and North Africa 2018, cit.

III. THE IMPACT OF ENERGY INSECURITY ON MEDITERRANEAN ECONOMIES

17. The energy sector is of great importance for the stability of the Mediterranean economy. Energy insecurity has the potential to cause severe impacts on economic and societal development.
18. Therefore, modern energy systems need to be able to go through shocks generated by a wide range of sources, including natural disasters, geopolitical conflicts, and emerging threats related to the ongoing digitalisation of energy systems.
19. In 2018, global energy demand grew by 2.3%. However, 850 million people still lack access to electricity.¹² Most of these people live in Africa, whose population is expected to reach 2 billion by 2040. As highlighted by the stated policy scenario of the International Energy Agency (IEA) World Outlook 2019, the increase in Africa's energy demand by 2040 will be higher than that of China.
20. At regional level, the sharp development of Southern and Eastern Mediterranean Countries (SEMCs) increased the energy demand and is shaping the economic and energy environment of the region. These changes are supposed to increase by 40% the overall energy demand of the region by 2040.
21. Furthermore, data shows that the current primary energy demand of Northern Mediterranean countries outweighs that of SEMCs, representing 63% of the total Mediterranean energy demand, whereas by 2040 the trend will switch and the energy demand of SEMCs will exceed that of Northern countries.¹³
22. Energy infrastructures (EI), fundamental in guaranteeing national economic stability and resilience, consisting of pipelines and facilities, human capital (staff), and information infrastructures, have been repeatedly attacked in several Mediterranean countries such as Algeria, Libya, Egypt, Turkey, Tunisia, and Syria over the last 14 years.¹⁴
23. Instability in the energy sector has also triggered violent demonstrations and protests over the years, such as the ones in Iran (November 2019) fuelled by the raise of the price of petrol, whose consequences were felt by many Mediterranean economies.
24. For these reasons, adequate and resilient energy supply systems are essential for a robust socio-economic development of the entire region. Although the Mediterranean basin holds 4.2% of the world's proven oil reserves, and 4.6% of the world's proven natural gas reserves,¹⁵ the energy situation remains highly vulnerable and unstable.

¹² “World Energy Outlook 2019”, *International Energy Agency*, <https://iea.blob.core.windows.net/assets/1f6bf453-3317-4799-ae7b-9cc6429c81d8/English-WEO-2019-ES.pdf>

¹³ “Mediterranean Energy Perspectives”, *Observatoire Méditerranéen de l’Energie*, 2018, <http://www.ome.org/wp-content/uploads/2019/01/EXECUTIVE-SUMMARY-MEP-2018.pdf.pdf>

¹⁴ Giroux J., “Energy Infrastructure Targeting in the Mediterranean: a Shifting Threat”, *IEMed Mediterranean Yearbook 2015*, https://www.iemed.org/observatori/arees-danalisi/axius-adjunts/anuari/med.2015/IEMed%20Yearbook%202015_Panorama_EnergyInfrastructure_JenniferGiroux.pdf

¹⁵ “Mediterranean Energy Perspectives”, cit.

25. By 2030, the peak oil demand is expected to be reached, and renewable energies will play a central role at global level. The International Energy Agency (IEA) underlined that by 2024 the share of fossil fuels consumption could be reduced to almost half of the energy mix production systems, while renewable sources will increase installed power by 50% from the current 2500 to 3700 gigawatts. This will allow renewables to cover half of the new electricity production, while the other half will still rely on gas and coal production.
26. In order to achieve these targets, to meet the growing demand for energy and to increase EI resilience, approximately 3 trillion euros need to be invested by 2040. In this context, technological innovations and new financing instruments are already shaping the Mediterranean future, making renewable energy more attractive and accessible for global investors.
27. According to the IEA, in 2018 the global growth rate was 3.6%, while energy demand grew by 2.3%. This data demonstrates that economic growth and energy demand do not increase proportionally. Nevertheless, the IEA estimates that the increase in energy efficiency – 1.2% in 2018 – will not be enough to support predicted growth trends. Therefore, it is crucial that policy makers and regulators work towards adopting modern and harmonised legislative frameworks to hold on the pace of disruptive technologies and the rising need for flexible operation of power systems.
28. Energy efficiency represents the single most important element to bring the world closer to a Sustainable Development Scenario and has positive impacts on energy consumption – reducing global energy intensity by more than 3% annually, while also improving industrial competitiveness and driving economic growth.

IV. THE ROLE OF PAM

29. PAM continues to work on a far-reaching framework of partnerships with leading international financial institutions, such as the World Bank, the EBRD, the EIB and the UN economic commissions to maintain thriving synergies between policymakers and economic experts.
30. While reinforcing its current partnerships, in May 2019, PAM expanded its network and signed an important Memorandum of Understanding with the OECD to better deal with financial, economic and legislative challenges in the region. The Paris based organization also offered PAM to further explore collaboration with the OECD Working Party on SMEs and Entrepreneurship, which is the OECD platform for policy makers to compare national experiences, seek answers to common problems and co-ordinate policies.
31. Moreover, in July 2019, PAM launched a new program and convened a special meeting on investments, with over 170 delegates from 40 countries and international financial organizations gathering in Milan on “Alternative Capital Markets for economic growth in the Mediterranean”. Focusing on the importance of alternative sources of funding to support MSMEs and start-ups, three PAM projects have been approved.

32. Notably, the “Start-up Market” project was finalised and launched in December 2019 consisting in a digital platform meant to bring together start-uppers and investors and to provide electronic tools to share better structured “capital calls”, supported by clear and transparent pricing systems.
33. This platform aims at drastically reducing search costs and information asymmetries, while further supporting already existing regional or local projects, such as incubators, info-mediaries, business angels, venture capital firms and funds, and innovation agencies. Such actions will contribute to the raise of confidence in financial opportunities and help MSMEs and start-ups in the early stages of their business life.
34. The Assembly also maintains its solid partnership with the World Trade Organization (WTO). This partnership enables PAM MPs to be concretely involved in the Organization’s activities and learn more about its policies and developments.
35. In this regard, it is worth highlighting that, while the main part of the WTO structure remains active, the WTO dispute system is facing the biggest crisis of its 23 years of existence, threatening the future of the organization. In fact, despite being a very successful dispute settlement system, ‘which has contributed to ensuring that WTO rules are respected and to the security and predictability of the multilateral trading system’,¹⁶ the selection process of new Appellate Body (AB) members faced a dangerous deadlock. On 10 December, the mandate of two of the three remaining members still in charge expired, leaving the AB without the legal quorum to review new appeals.¹⁷ Consequently, many WTO Members have also made clear that they regard a dysfunctional AB as a major problem for the trading system that could generate serious repercussions on financial stability.
36. Nonetheless, PAM and the WTO have already agreed, in February 2019, to convene a major Parliamentary Forum on trade facilitations, supposed to take place in November 2020 in Geneva, on the margins of the Ministerial conference. The meeting would be the first event organized as part of the “PAM/WTO Euro-Mediterranean Parliamentary Forum for Trade and Investment Facilitation”, established in Belgrade in 2018, and it would be crucial in outlining the main issues at the core of this crisis, as well as in evaluating possible parliamentary strategies to facilitate a coordinated solution to the backdrop.
37. Moreover, on 13 November 2019, PAM contributed to the UNCTAD High-level International Investments Agreements (IIA) Conference, to take stock of the IIA reform process. The meeting reviled to be a fruitful opportunity to evaluate future joint activities related to the issues addressed. In this regard, there is great potential for PAM - UNCTAD cooperation on investments for development, which will find its first strategic application in the preparation for

¹⁶ “Crisis of the WTO Appellate Body”, European Parliament, 28 November 2019, https://www.europarl.europa.eu/doceo/document/TA-9-2019-0083_EN.pdf.

¹⁷ “Members reiterate joint call to launch selection process for Appellate Body members”, *World Trade Organization*, 22 November 2019, https://www.wto.org/english/news_e/news19_e/dsb_22nov19_e.htm.

the World Investment Forum, scheduled to take place in December 2020, and hosted by the United Arab Emirates, the PAM newest associate member State.

38. The PAM Panel on Trade and Investments in the Mediterranean will be at the centre of the economic activities of the Assembly in 2020, having proven to be a unique forum of discussion, which closes the gap between technical and policy requirements to develop updated regulatory frameworks and making the parliamentary dimension duly and concretely translated into actions.

V. CONCLUSIONS AND RECOMMENDATIONS

39. Parliamentarians need to provide public policies that are conducive to resilient and reliable economic policy frameworks. Trustful and sustainable oriented policies would generate positive synergies and a greater involvement of the private sector.
40. PAM MPs shall fully support the new strategy launched at the PAM conference in Milan. As agreed during the Bureau meeting, in November 2019, the conference will be organised annually in Milan, in parallel to a second thematic meeting in another PAM member country.
41. All PAM members should strongly endorse the facilitation of financial inclusiveness, using disruptive technologies and digitalization. In this regard, the “Start-up Market project” shall be duly supported by all members of the Assembly.
42. Modern educational trainings for the young generations should be developed to match job offer and demand. This will enable a smooth transition of the working force to be employable in new green and digital realities. Courses should be also considered for those who are currently employed and need to adapt their competencies. In this regard, the PAM Academic platform should be a propulsive engine.
43. The WTO Appellate Body crisis should be duly considered and addressed. PAM is concerned about the severe consequences for the rules-based multilateral trading system. PAM stresses the importance of interparliamentary dialogue, as a way of contributing to the ongoing discussions to overcome the WTO AB crisis.
44. Moreover, PAM welcomes a more structured cooperation with UNCTAD and should work towards signing a comprehensive Memorandum of Understanding, in the shortest possible timeframe.