

POLICY BRIEF

MICRO AND SMALL ENTERPRISES IN LEBANON

ERF Research Program on Promoting Competitiveness
in the Micro and Small Enterprises (MSE) Sector
in the Middle East and North Africa

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The Policy Brief series is a new publication of ERF that aims at bridging the gap between research and policy by providing concise and summarized outputs of research.

This Policy brief is an attempt to distil the main policy recommendations of major studies that were carried out in four MENA countries: Lebanon, Morocco, Turkey and Egypt. These studies were carried out within the framework of the ERF project on "Promoting Competitiveness in Micro and Small Enterprises in the MENA region". The project was based on field surveys and was the subject of national debate in the respective countries. The regional project was directed by Dr. Nader Fergany.

This Policy brief is based on the Country Report of Lebanon prepared by Dr. Kamal Hamdan as the team leader (Consultation and Research Institute, Lebanon) to whom ERF is grateful for enriching the literature with such a serious and up-to-standard research.

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Similar to most countries in the MENA region, economic growth and technological progress have been slow in Lebanon, with a predominance of small scale enterprises in the economy. The private sector has traditionally been a major partner in the development of the country, with the prevalence of family-owned, micro and small enterprises that constitute the bulk of private sector activity. The MSE sector has, thus, the potential of providing substantial support to the development of the country in the medium and long terms. This is especially true as a large proportion of new jobs generated are in the informal sector - a sector that is, still, characterized by low productivity, poor working conditions, and high vulnerability to shocks.

The present policy brief is based on the country report prepared on the Micro and Small Enterprises of Lebanon within the framework of a larger study on the MSE sector in four MENA countries (Morocco, Egypt, Turkey and Lebanon). The main objective of the study was to improve the knowledge of the economic and social characteristics of the MSE sector in those countries with a view to tapping, its potential contribution to growth and employment generation, especially for the poor.

In this context, the Lebanese study examines the sectors' current status, existing constraints and potential for growth. This enhanced understanding is expected to assist in the design of policies and programs that would allow this sector to fulfil its potential growth with expected spin-off effects for the national economy. Such a framework is crucial, especially given the substantial share of this sector in the Lebanese economy, and in light of the changing environment resulting from globalization and trade liberalization, and the possible threat to traditional incomes and livelihoods of a major disadvantaged segment of the society.

An effecient and comprehensive methodology adopted...

An innovative methodology has been adopted and applied in this study, first, by evaluating the existing data from the Census of Establishments and Building realised by the Central Administration for Statistics (CAS) in 1996, and then choosing a sample of 3,021 MSEs, of which 2,948 completed questionnaires in the field survey⁽¹⁾. The survey was spread out on six Mohafazat, over a period of two months⁽²⁾. The combination between the statistics obtained from the survey and those of the Central Administration of Statistics (CAS) related to Mohafazat distribution allowed us to create a comprehensive database which represents the MSE's distribution (per Mohafazat, size, and gender) at the national level. A correction methodology was adopted and the corrected data was used in the analysis.

...to underline the main aspects of MSEs in Lebanon...

The main findings of the survey, based on the completed questionnaires (2,948) reveal the following characteristics.

The MSE Sector in Lebanon is dominated by micro enterprises ...

Micro enterprises employing less than five employees make up the bulk of operational enterprises in Lebanon, constituting 88% of the total, while those employing less than 50 individuals make up 96%⁽³⁾. Cumulatively, enterprises with less than 50 employees generate the majority of employment opportunities in the country, accounting for about 530,000 employees, 51% of the total working population estimated at 1.24 million⁽⁴⁾.

The survey has confirmed this generally known fact, it revealed that 97% of MSEs employ less than ten individuals, 46.8% employ 2-4 workers, and 2.7% employ 10-49 workers. Enterprises with only one

employee account for almost 45% of the sample, reflecting the individualistic entrepreneurial spirit that prevails in the Lebanese informal economy.

Data suggest that the performance of the enterprise is directly related to its size⁽⁵⁾, with the best performers employing 10-49 workers. Whereas the one-worker enterprises have the lowest value-added accounting for an average of \$534/ month per enterprise. This figure gradually increases with size to reach \$1,218/month for the 2-4 employee category, and \$10,050 for the 5-49 employee enterprises category.

.... with most activities concentrated in trade services.

The survey also revealed that the economic activity in Lebanon is dominated by trade practices, and most enterprises are concentrated in the services and agricultural sectors, with the services sector encompassing the highest percentage of workers. This structure may be explained by several factors, including the fragmentation of markets as a result of the civil war and accelerated urbanization.

Most of the MSE sector is relatively young

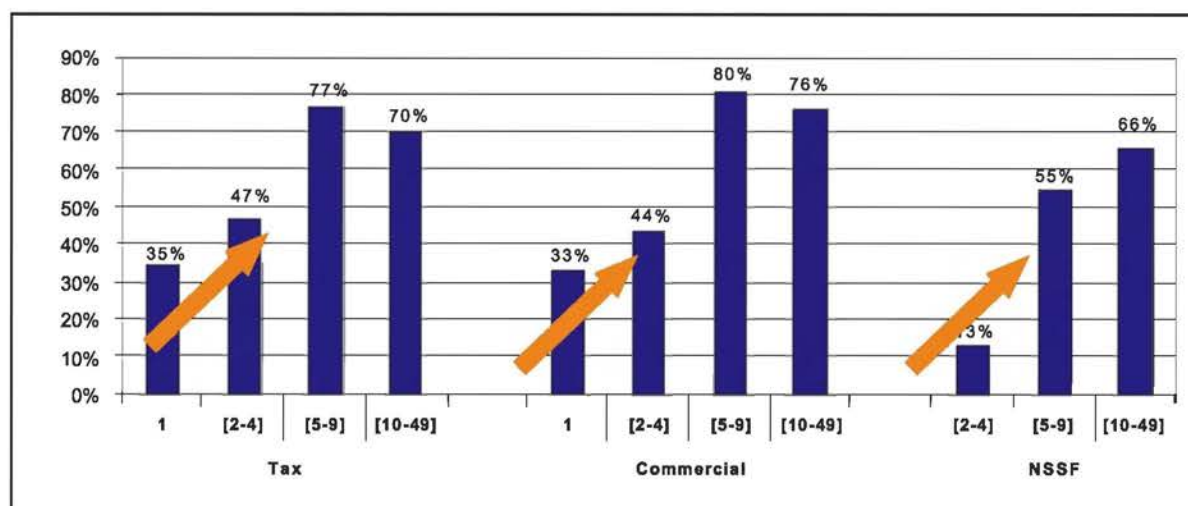
Most of the surveyed enterprises (71%) were established after 1990, while about 58% established after 1995, and about one third established after 2000. This fact reflects the high expectations of the entrepreneurs in the future of the Lebanese economy at the time of the survey after the 15 year civil war. The reconstruction of the country has opened the door for a fast growing sector that was also boosted up by an increasing market demand.

Beirut seems to attract more enterprises than other regions, as it has the largest percentage of older enterprises. Conversely, south Lebanon witnessed the establishment of the largest portion of its MSEs in the period 2000-2004, i.e. directly following the Israeli withdrawal from the region. The distribution of MSEs according to date of establishment and geographic region also reflects availability of and access to basic infrastructures and services.

...with a geographic distribution that depends on the available infrastructure...

The study revealed that more developed regions tend to have larger enterprises, due

Figure1 : Registration of MSEs in Tax, Commercial and NSSF



to higher access to infrastructures, services, finance and markets. Poverty stricken less developed regions are dominated by micro enterprises; the share of one-worker MSEs increases from 32.7% in Beirut to 56.1% in North Lebanon and 47% in the Bekaa. Furthermore, Beirut and Mount Lebanon are the only regions that have above average concentration of 5-9 and 10-49 category MSEs.

This distribution of MSEs testifies that, in order to enhance the development of the enterprises, there is a real need for infrastructure in rural areas where most micro enterprises are located.

...and only half are registered.

The survey examined the informality of sectors and employment through exploring enterprise commercial registration, participation in the national social security fund (NSSF), and registration with the tax authorities.

It is notable that almost half of the MSEs surveyed are not commercially registered⁽⁶⁾. However, MSEs tend to legalize their status and register commercially as they become older and larger. Registration levels also vary with the sector of activity, where higher registration levels are observed in the industrial sector.

A lower percentage (only 20%) of surveyed enterprises participates in the NSSF scheme. Again, this depends on the sector of activity (higher in the industrial and services sectors), size (positively correlated), and commercial formalisation.

Around 44% of surveyed enterprises are registered with the tax department, while 39% are not, and 17% are not required to. Trade enterprises and larger enterprises have the highest incidents of tax registration.

It is important to underline that the survey results point to a positive correlation between the formality and the size of enterprises, therefore, the performance rise, with this aspect.

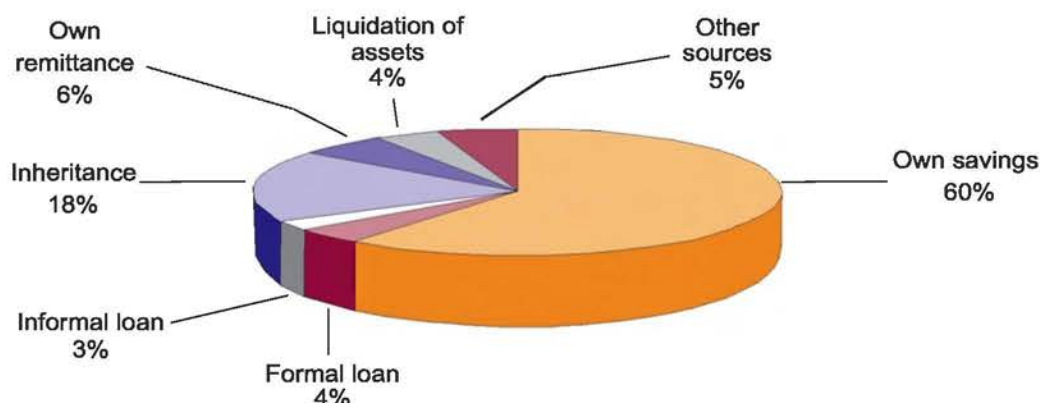
Entrepreneurs record many lacks and difficulties...

...highlighted by difficult access to start-up capital ...

The most prominent constraints faced by the surveyed MSEs seem to include securing start-up capital and the high tax rates imposed by government regulations. The survey indicated that 48% of MSEs are constrained by lack of access to credit facilities to start their business.

It is observed that in most of the cases the initial start-up capital for the MSEs is secured

Figure 2: Distribution of sources of initial capital



through informal channels, such as own savings, inheritance and family loans, reflecting the familial nature of MSEs. It has been shown that the larger the size of the enterprise, the more the likelihood of its accessing other funds to start up. Moreover, accessing formal loans (from banks mainly) increases as the size of the enterprise is larger.

The highest share of enterprises with access to formal loans is for those working in the construction sector (10.5% of total enterprises in this sector). The reluctance of entrepreneurs to go through formal loans channels is due to the complexity of the procedures and the uncertainty.

...difficult regulatory procedures.

In general, entrepreneurs have problems in dealing with regulatory issues, but tax rates constitute the major challenge (according to 43% of entrepreneurs). Tax administration (36%), licensing and registration procedures (35%) and Custom duties (32%) also matter. This could reflect the fact that the majority of MSE prefer to stay informal if they were given the choice.

Entrepreneurs lack education and training...

As for the educational attainment, the survey reveals that 16.3% of the entrepreneurs are either illiterate or have completed only the first elementary level, while 24.7% are either

Figure 3: Constraints recorded by entrepreneurs

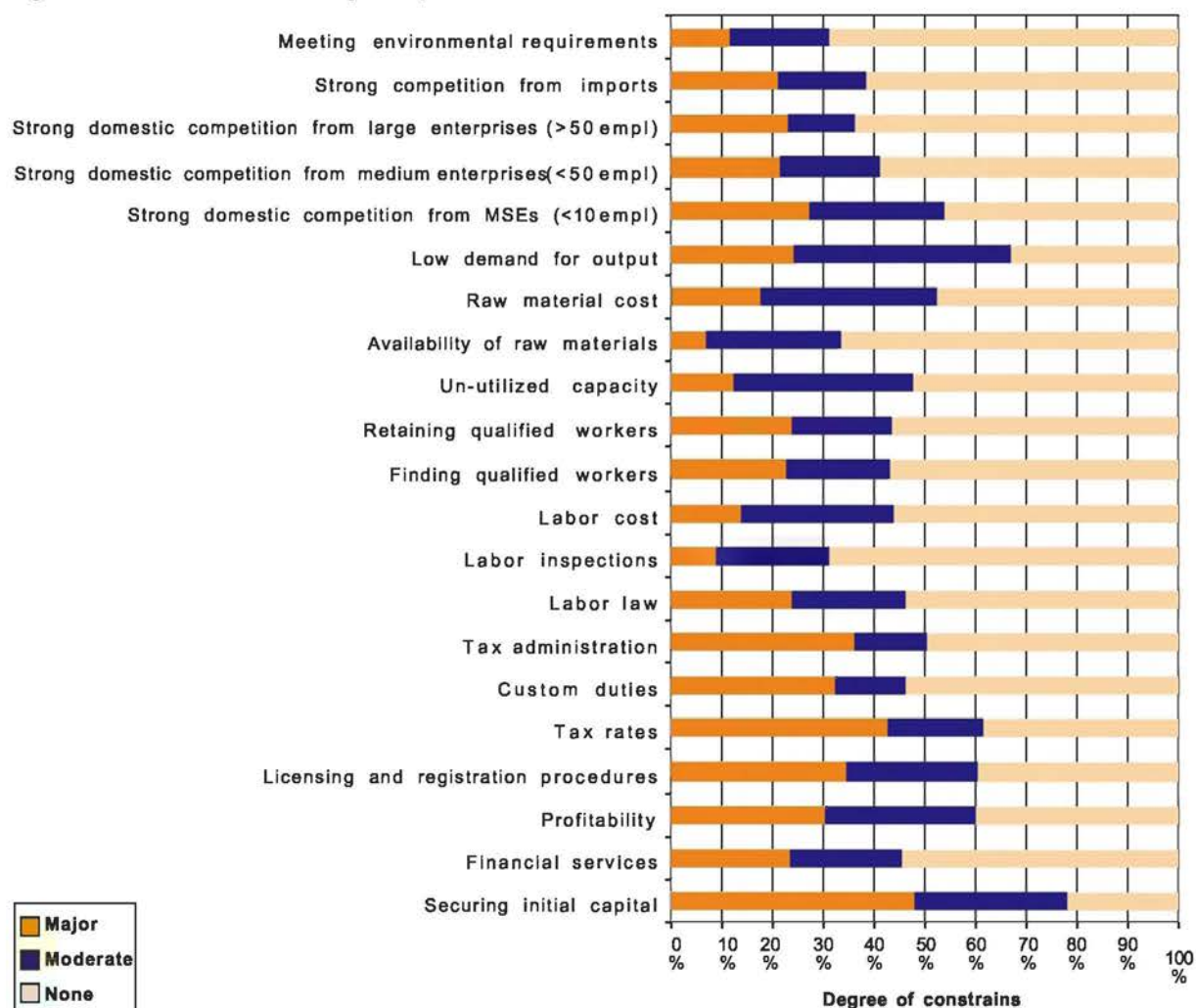


Table 1: Distribution of entrepreneurs according to size and education

| No. of education years | Size (no. of employees) | | | | |
|------------------------|-------------------------|--------|--------|--------|--------|
| | 1 | 2-4 | 5-9 | 10-49 | Total |
| 0 years | 5.1% | 1.9% | 1.9% | 0.0% | 3.3% |
| 1-5 years | 17.8% | 11.7% | 8.7% | 2.6% | 14.0% |
| 6-9 years | 36.6% | 33.5% | 17.4% | 17.9% | 33.6% |
| 10-12 years | 23.0% | 25.1% | 31.1% | 20.5% | 24.4% |
| 13-16 years | 14.5% | 22.4% | 31.7% | 50.0% | 20.1% |
| 17+ years | 2.9% | 5.4% | 9.3% | 9.0% | 4.6% |
| Total | 100.0% | 100.0% | 100.0% | 100.0% | 100.0% |

high school or university graduates. While more educated entrepreneurs, having between 13 and 16 years of education, account for 14.5% of the one employee category enterprise, this percentage increases to 50% of the 10-49 employees category enterprises. This relation between years of education and size of the enterprise is also repeated in the higher years of schooling categories (table 1). This correlation is evidenced also if we use value-added data. Value-added for enterprises belonging to category 5-49 employees are much higher than that for the other categories of enterprises. Thus, a positive correlation exists between education, the size and the value-added of the enterprise.

In terms of vocational training, almost 10 percent of the sample indicated that they have had access to such type of training. There is a clear relationship between the size of enterprise and the level of education for the entrepreneur.

...and a relatively low participation of women.

In general, women's participation in the labour market in Lebanon is low, estimated at 22% of the working population (1997), and 29% of permanent employees. Women participation in the MSE sector varies, with the highest concentration in medium-scale

enterprises. Variations also exist based on the enterprise's type of activity, with increased participation in education, health, textile, sales, and secretarial activities.

The largest constraint faced by women entrepreneurs is personal harassment (74.8%), followed by problems related to setting up an enterprise (40%), hiring workers (31%), and to a lesser extent marketing (23.4%) and joining business associations (20.5%). It is to note that Female-run-enterprises suffer from lowest value added than that of males (a ratio of almost 58%).

Furthermore, illiteracy is higher among female entrepreneurs (4.8% for females and 3.2% for males) yet the percentage of women who have completed schooling or university studies is higher than that of males (31.5% females and 24.1% males). This is perhaps reflected by the fact that most female owned enterprises have a starting date of less than five years, and that, as a consequence, the survey indicates that male-operated MSEs have almost double the present value of those operated by females.

...and tools to improve their performance.

Encouraging the private sector to support the MSEs...

The contribution of the private sector to Lebanese economy cannot be overlooked,

likewise the importance of micro and small enterprises, which has always characterised the economy of the country. This fact has been firmly confirmed by the current research.

It indicates the importance of supporting micro and small enterprises as one of the pillars for any long-term development strategy.

This is especially pertinent for pro-poor development strategies, since these enterprises are mostly owned and operated by poor and more vulnerable groups of the society. The advantage is that such enterprises are easy to support, require low capital per job created, and have the ability to generate job opportunities to absorb the growing labor force, and target women, as well as those who have no other income source. However, this sector is vulnerable to shocks, lacks access to financial facilities, and in general, those who work in it are not covered by social security schemes.

...by enhancing a favourable economic environment...

The overall environment in Lebanon provides several positive aspects that can be utilised to enhance the role of MSEs in poverty alleviation and employment generation efforts.

These include a liberalized economy that allows for the development of the private sector; a flourishing banking sector that could be used for strengthening MSEs if a favorable macro-economic environment is in place; a rich human resources base; and the existence of a number of government interventions to develop the MSE sector. However, this sector still faces a number of constraints that have to be overcome if the sector is to achieve full potential. These include accelerated liberalization and a decline in protectionism, increased access to new technologies, and to financial/credit services from formal and informal sources removal of distortions in the structure of costs and prices,

as well as the strengthening of basic infrastructure and upgrading of labour skill. In addition, SMEs operate under obsolete and irrelevant regulations, as Lebanon still lacks a suitable regulatory framework that organizes the work of MSEs.

...and the participation of NGOs, national and international organizations in boosting up the sector.

Several projects have been undertaken in Lebanon that would assist the development of the economy, many of which may have a spill-over effect on the MSE sector, these include:

- The Community Development Project (CDP, from 2003 to 2008) drawn up by the World Bank in collaboration with the government, this project aims to establish an effective and sustainable instrument to improve the living conditions and the economic status of disadvantaged communities.
- The Economic and Social Fund for Development (ESFD, from 2002 to 2006), the European Union funded projects established the economic and social fund to alleviate poverty with two components: job creation and community development.

Despite their effectiveness, these projects do not include specific measures that target the MSE sector. Special MSE projects are constituted by small organisations, but these have smaller funds and less links with institutions.

Based on the findings of the survey, specific recommendations have been drawn. It should be noted however that the effectiveness of these recommendations would not be realized unless macroeconomic reforms pertaining to infrastructural, fiscal, sectoral and employment policies are adopted. Also, political stability is crucial.

Promoting the MSE sectors needs targeted policies and an enabling environment ...

- One of the most important conclusions of the study is the need for the inclusion of purposeful enterprise development strategies, guided by an overall vision of development.
- An enabling legislative framework that facilitates and encourages engagement in the formal, micro, and small scale enterprises. This will ensure their proper development, increased competitiveness, efficiency, and sustainability.
- There is a need to provide incentives for enterprise establishment and growth, including licensing/registration procedures, regulating taxation, tax administration, customs fees, and costs of essential services in a way that would assist and encourage these MSEs.
- Based on the survey findings, the size of the enterprise is important for increased competitiveness and sustainability, as well as better performance. Size was found to significantly raise profit, present value, value-added, performance. It also assists enterprises to develop into bigger categories, improve working conditions, and raise family/ household incomes. The same holds true for the organisational management of enterprises.
- There is a need to strengthen legislation related to membership of MSEs in professional organizations in order to encourage them to get engaged in partnerships.
- One could look into focusing assistance on promising sub-sectors which have the opportunity to grow and provide the highest added value in income and employment generation, as well as provide the highest performance. This could be a pilot arrangement in which overall assistance to one of the sub-sectors is coupled with a basket of assistance program interventions (access to financial services, technical assistance, know-how, etc.). The results could then be evaluated for impact.
- Aiming at up-scaling the size of currently existing enterprises to ensure their sustainability and improve their overall performance, a law should be enacted that exempts them from income tax profits arising from improved tangible and intangible assets as a result of shifting from sole proprietorships into corporations.
- Enhance the roles of local government, private sector, and civil society organizations in promoting competitiveness in this sector.
- There will continue to be a need for a structure to provide problem-solving quick fixes on a demand basis for MSEs. This could be piloted by governmental and non-governmental organizations as the need arises. Part of the services offered by such organizations would be those of a referral nature- to other institutions that could provide the needed service.
- In an attempt to promote international market competition of Lebanese enterprises' goods and services, it is essential to (a) create and/or upgrade accredited laboratories and qualified centres that would provide certifications according to European Harmonised Standards, and (b) develop an export promotion agency that would study external markets as well as provide local enterprises with necessary information.
- There is a need to increase the access of MSEs to financial resources, both for initial start-up of businesses and for expansion. This access is almost non-existent at

present. Models to ensure increased access to small credit, both through formal banking or through non-governmental organizations, are well-established globally and these models could be adapted to the country context easily. Facilities for accessing short, medium, and long term credit should be provided and improved for MSEs.

... pertinent education and training schemes...

- Review the existing vocational and technical education courses with the aim of adapting it to the present and future needs of the MSE sector. This is a policy issue that needs to be finalised in conjunction with other operational issues to extend access to formal and informal training and education opportunities.
- Access to formal and informal education and training needs to be enhanced. Based on the findings of the survey, education and formal training enhances the development of micro and small enterprises and improves their performance. It is, thus, important to concentrate more on the sustained investment in human resources and technical skills development if entrepreneurs are to lead effective sustained and profitable enterprises.
- Formal and informal training should be combined with business counselling. A wide range of networks can be used for this purpose, including central and local government agencies, non-governmental organizations, and others, where the training provider integrates training, coaching, and consultancy in one single package.
- It is recommended that training and counselling be sensitized to different factors. Gender is one, the size of the MSE is another, and the type of business might be a third. Some sectors and types of MSEs need to be provided with specialized tailor-made courses. In some MSEs, especially family-run businesses, it may be necessary to focus on other issues, such as those pertaining to growth, including decision making and internal organization.
- Since there is no one type of assistance that can effectively meet the needs of all different types of firms, four categories of enterprises can be developed: (a) newly-established enterprises, (b) established non-growing enterprises, (c) established slowly-growing enterprises, and (d) established enterprises that enjoy high growth rates. Each of these categories is to obtain individual assistance relevant to its status, based on its positioning according to the four categories.
- Besides addressing certain sectors and/or occupations, training providers should be encouraged to provide owners and managers of MSEs with specific training programs.
- Training providers should improve their capability in the areas related to the needs of individual firms or coherent groupings through: (a) identifying these needs; and (b) involving owners and managers in the design of training courses.
- The role of intermediaries should be strengthened, where they should be able to provide (a) management services; (b) technical know-how; (c) forums for partnership and dialogue; and (d) visibility, marketing, and others.
- Effective quality assurance mechanisms and tools should be developed, based on clear standards and quality criteria, to allow both training providers and trainees to identify effective training courses and areas for improvement.

... access to technology, infrastructure and services ...

- Access to technology should be improved as it has proved to enhance the performance of MSEs. It is recommended that this increased access be included in any development strategy targeting enterprises.
- MSEs should have access to knowledge-based networks. Knowledge- intensity of production and the emergence of innovation-based solutions would enhance the performance and survival of firms.
- Access to basic infrastructure and services for the operation of MSEs should be enhanced. The findings of the study highlighted the importance of availability of an efficient infrastructure to ensure sustained enterprise growth and performance. MSEs located in Beirut or Mount Lebanon, with higher access to infrastructure and markets, perform better at many levels, such as value-added, present value, and profits.

... accompanied with good interrelations between MSEs

- There is a strong need to develop markets and marketing linkages between MSEs. Both vertical and horizontal expansion should be considered and assistance in marketing interventions should be completed.
- There is a need to establish a strong network among MSEs. This should be “incubated” for the first phase of its establishment, but could then be “hosted” by the business/professional grouping or associations.
- Although international research indicates the importance of clustering for increased competitiveness and higher earnings and profit, the survey did not validate this

hypothesis, since it did not show that MSEs in clusters enjoy better performance indicators. This may be due to the fact that most of these enterprises have not yet sensed the effects of globalisation, as well as the fact that clustering in the Lebanon context is merely a grouping of MSEs in one location rather than pooling resources and collaboration to achieve common goals at certain levels.

- An institutional body or a structured forum should be created, where agencies providing support to MSEs can elaborate their common visions and interests, share lessons learnt and disseminate the experience gained. It should include all stakeholders, including central and local governments, non-governmental organizations, donors, and associations.

..and a special focus on women.

- Special attention should be placed on female-run enterprises, to develop and provide a way out of poverty. The issue of gender differentials is an interesting one. The survey showed that women entrepreneurs resort to the establishment of micro and small enterprises as an alternative to their depressed situation. However, women earn less; their enterprises have less access to earnings and profit, perform less, have lower added-value, and have less access to assets and resources.

- 1- A response rate of 97.6%.
- 2- conducted by 55 trained surveyors on 200 selected clusters.
- 3- Knowing that around 3% of the total number of enterprises did not declare the number of employees.
- 4- Living Conditions in Lebanon, Central Administration for Statistics, 1997.
- 5- with the exception of one-employee enterprises.
- 6- with the exception of those that are not required to register

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