

Regional workshop: Scaling-up the Private Sector Participation in North Africa

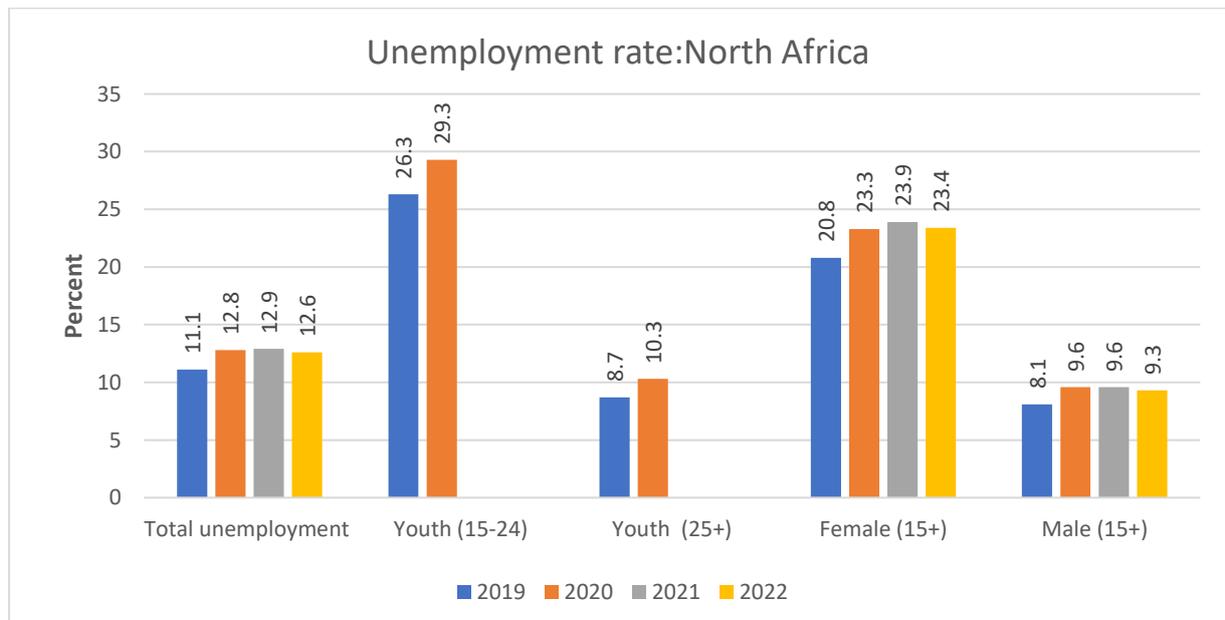
Tangier, Morocco, 20-22 July 2022

Concept Note

1. Context and Motivation

In North Africa, the long-standing issue of high youth unemployment persists and is projected to remain the region's key economic and social challenge over the medium term (Fig 1). Private sector small and medium enterprises (SMEs) could play an instrumental role in tackling this challenge, given their potential to create jobs, support growth and foster innovation. However, large state-owned enterprises (SOEs) continue to be a prominent feature of North African economies. While in some cases major SOEs support development, in others inefficient SOEs crowd out private sector innovation and pose fiscal risks to the country. In addition, public sector wage premium in, for example, Morocco and Tunisia hamper their private sectors and contribute to youth unemployment by incentivizing youth to queue for public sector jobs.

Figure 1. Unemployment rate



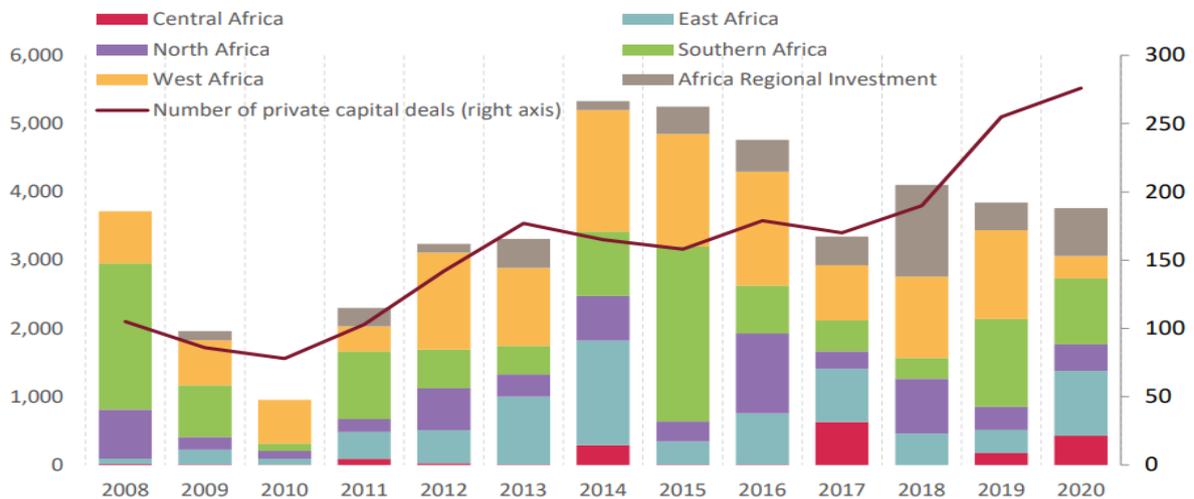
Source: ILO, World Employment and Social Outlook: Trends 2022.

Furthermore, during the post-pandemic recovery and the ongoing war in Ukraine, the private sector has a crucial role to play in helping governments address the economic impact of the two shocks. The COVID-19 crisis triggered multiple shocks that significantly worsened economic and social trends in North Africa. The Russia-Ukraine conflict has mixed impact on North Africa’s growth outlook in 2022. Commodity dependence could weigh on the region’s growth prospects in the post covid-19 world if left unaddressed. The prolonged Russia-Ukraine conflict would negatively weigh on the entire region through increased uncertainty, tightened global financial conditions and enhanced food insecurity, among other factors.

Policy makers have long recognized that state-led growth model adopted in previous decades contributed to economic stagnation. The region is still characterized by a subdued private sector with a low proportion of formal private sector employment, as well as a high level of informality. Today more than ever, it is critical to foster a dynamic private sector in North Africa that would support economic diversification and transition to green growth while reversing the region’s low female and youth employment.

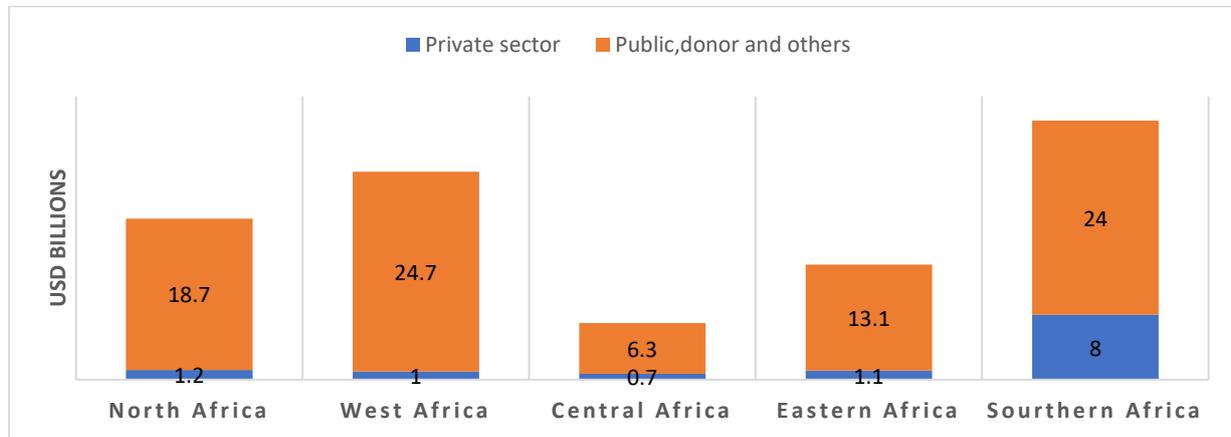
North Africa typically accounts for less than 15% of Africa’s private investment (Fig 2) and only around 20% of total investment, despite having some of the largest economies such as Morocco and Egypt and the region accounting for 28% of African GDP in 2019. For infrastructure projects, the share of private sector financing in infrastructure stood at 1.2 billion US dollar in 2018 compared to 18.7 US dollar billion of public investment in 2018 (Fig 3). North Africa is far behind southern Africa region where private investment in infrastructure is more meaningful.

Figure 2: Total private investment in Africa by region (USD million)



Source: Finance in Africa: for green, smart and inclusive private sector development report, 2021.

Figure 3: Private Sector Financing in Infrastructure, By Sub-Regions, 2018



Source: Economic Report for Africa, ECA (2020).

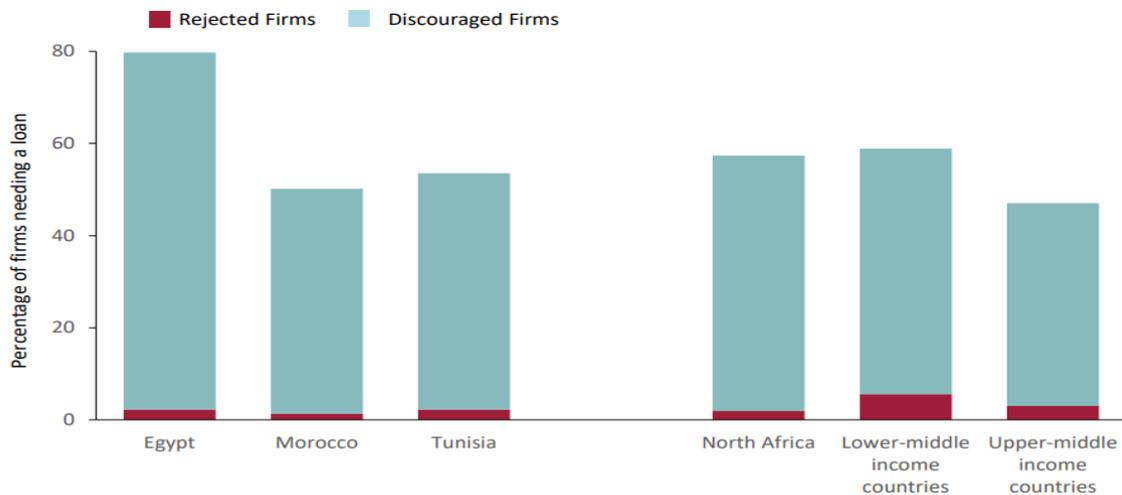
Since private investment remains modest in North Africa, most governments in the region have implemented reforms to develop the private sector. For example, Morocco leveraged Tangiers' strategic location at the Strait of Gibraltar where the Atlantic Ocean meets the Mediterranean Sea to attract private sector investments. Tangier is currently the epicenter of a burgeoning industry-rich region. According to the 2020 ranking fDi's Global Free Zones, Tangier Med Zone in Morocco, which includes six activity zones for the automotive, aeronautics, logistics, textiles, and trade industries, was ranked 2nd world economic zone after "Dubai Multi Commodities Center", in the United Arab Emirates. In 2021, US\$120 million private investments were injected in 28 new projects in all Tangier Med's activity zones.

However, even with numerous structural reforms in the region, local enterprises still face impediments to entrance, poor access to industrial land, poor social capital, bureaucratic obstacles, ineffective legal framework, and a complicated public procurement system, among other obstacles. Further insights according to World Bank Enterprise surveys indicate that funding is a major or severe constraint for 23 percent to 28 percent of Egyptian, Moroccan, and Tunisian enterprises with less than 100 employees, comparable to less than 15 percent of such firms in India, China, and Turkey.

The limited role of the private sector in North Africa has negative economic consequences, including inefficient allocation of resources across firms and sectors and limited economic diversification. On a more positive note, African governments can shift the COVID-19 crisis into an opportunity by putting focus on, among other factors, supporting the private sector, particularly small and medium-sized businesses, and women-led businesses.

Several surveys and studies show access to finance as the main impediment to SMEs and employment. In Morocco and Egypt, the current supply of loans to SMEs stands well below the average level for developing countries (14% of GDP), accounting for less than half of potential demand. Similarly, recent survey conducted jointly by EIB, EBRD and the World Bank shows that 80% of Egyptians firms that need a loan are credit constrained (Loan application rejected or have been discouraged from applying in the first place (Fig.4), significantly exceeding the average of lower-middle-income countries (59%). The share of firms in Morocco (50%) and Tunisia (53%) that are credit-constrained is below the lower middle-income average, but nonetheless significant. A lack of competition among banks reduces access to financing for SMEs. The banking sector in North Africa, is often associated with higher interest rate margins and bank profitability and may discourage lending to smaller firms.

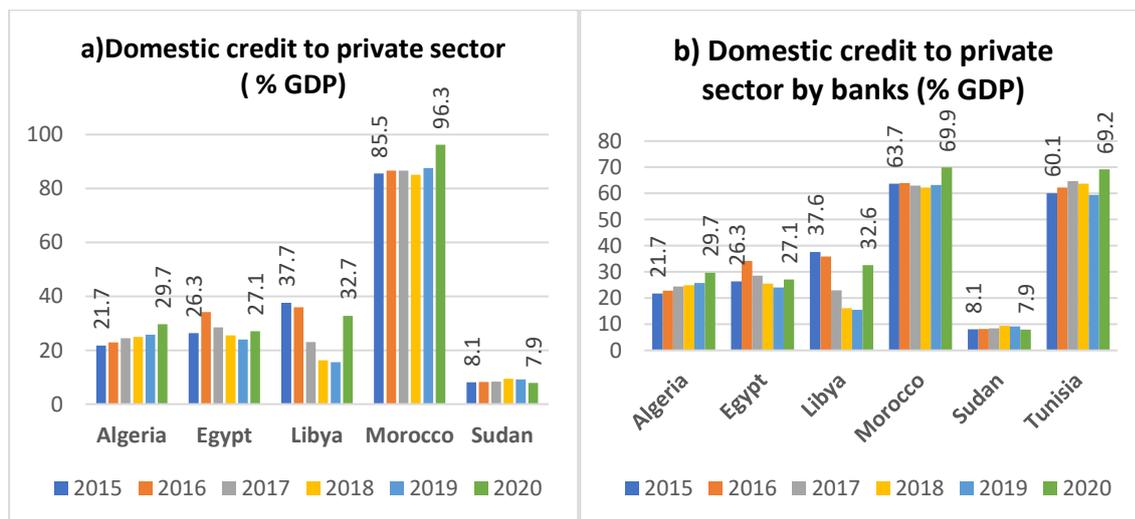
Figure 4: Credit-constrained firms in North Africa



Source: *Finance in Africa: for green, smart and inclusive private sector development report, 2021*

Provision of credit to the private sector varies across the subregion. Credit to the private sector as a proportion of GDP is particularly low in Egypt and Algeria while Tunisia and Morocco's domestic credit is over 60% of GDP. In Egypt, total bank assets account for about 85% of GDP in 2019, yet credit to the private sector is only 24%, reflecting crowding out by public debt (Fig.5).

Figure 5: Domestic credit to private sector (% of GDP)



Source: *WDI, Tunisia and Mauritania data missing in a) and data on Mauritania is missing in b)*

Governments in North Africa have a regulatory, catalytic, and coordinating role to play to enhance a dynamic private sector in the region. To get there, governments need to become enablers and pave the way for a vibrant private sector with minimal barriers to exit and entry and support complementary infrastructure. This will require not just the provision of public goods, including digital ones, but also an overhaul of the regulatory system to ease market entry for new businesses. Strong governance and stable institutions generally support SME access to formal financial services.

2. Objectives of the workshop

The main objective of the workshop is to contribute to accelerate the role of the private sector in North Africa by sharing good practices. The Workshop will be centered around 6 key thematic areas:

- **The effective state:** The state plays a critical role in providing the institutions required for private companies to grow. It sets the climate for investment and commerce through trade policy, competition policy, regulation of utilities, commercial justice systems, taxation, land reforms, labor codes and environmental management. The state needs to develop credible systems for making policy. These systems must show that policy making has predictability, that corruption is being controlled and that the state cannot be hijacked by specific interest groups. States should increase their accountability via the culture of 'value for money'.
- **Access to finance:** Despite significant progress in terms of financial sector deepening and broadening in North Africa, credit is mostly channeled to a small number of large firms. Furthermore, the public sector consumes a large portion of bank financing, resulting in a crowding-out impact on the private sector. This is evident from for instance in Algeria where state-owned banks control more than 90% of the commercial banking sector and in Egypt three of top five banks are state-owned. In addition, improving the governance of the banking sector by increasing entry and competition among all banks (public and private) is necessary condition for private sector development in the region.

Financial markets provide an alternative to the bank finance as a source of financing to private sector. These include capital markets, such as SME-specific equity market segments and fintech. The latter could be a potential game-changer, both by reducing some of the above constraints on bank lending and by opening new financing sources for SMEs, such as crowdfunding, seed capital and peer-to-peer electronic platforms.

Stock markets allow domestic firms to raise funds in developed economies and mobilize domestic savings. However, all these alternative channels require putting in place specific legal and regulatory environments.

- **National and regional value chains:** In North Africa, the presence of barriers to trade, either through non-tariff or tariff measures, reduces market competition and therefore, efficiency and average productivity. North Africa is also the least integrated region on the African continent. In 2020, intra-African exports accounted for only 5.1 percent of total exports in North Africa, and 3.1 percent for UMA, compared to 10.5 percent for COMESA and 19.8 percent for SADC.

Effective national and regional value chains can also help countries to join global value chains (GVCs) especially in the subregion where only Tunisia, Morocco and Egypt have some GVC integration. Tunisia is the most integrated having recorded 45 percent of its exports connected to GVCs. Value chains accounted for 43 percent of the added value from Moroccan exports in 2015 while Egypt has a least level of GVC integration, with GVCs accounting for only 10% of its exports in 2018. Addressing regional disparities will also be instrumental in this respect. Private investment in North Africa has the potential to thrive if opportunities offered by stronger involvement in GVCs and deeper integration in Sub Saharan Africa are seized.

- **Innovation capacity:** Innovation contributes to a strong economy through job creation, income generation and is key driver of long-term economic growth. According to the Global Innovation Index 2020 Report, Morocco and Tunisia are above expectations in terms of

innovation performance while Algeria and Egypt are far below their innovation performance potential based on their level of development. The obstacles to innovation in the region include:

- Little support from the government for innovation, science, and technology;
- Weak institutional framework;
- Low investment in knowledge-intensive services and knowledge creation;
- Fragmentation in the innovation system;
- Innovation inputs not translated into innovation output.

As the Covid-19 pandemic strengthened the role of digitalization for productive transformation in an economy. However, digital transformation must take a people-first, multidimensional approach, rooted in good governance.

- **Skills gap:** A suitably skilled workforce is a key prerequisite for successful innovation and sustained productivity. Tunisia, Morocco, Algeria, and Mauritania have made significant progress in educating their younger populations. Egypt has improved outcomes in primary education, as well as driving significant progress in increasing the completion of secondary and tertiary education. However, North Africa is still characterized by a mismatch between the skills provided by formal education and those demanded by the private sector. ECA research found that the public sectors in Morocco and Tunisia absorbed skilled labor which exacerbated skill shortages in the private sector hence significantly negatively affecting it. It also revealed the need for private sector to invest in employee training and development. Therefore, government assistance may be crucial in stimulating adequate and broad-based private sector human capital investment. The COVID-19 economic shock has also made the skills gap broader and the need to close it more urgent. The region needs new investments and mechanisms for upskilling and reskilling, for both soft skills as well as digital skills.
- **Transition to green economy:** North Africa is at a greater risk to the effects of climate change, which the COVID 19 pandemic and now the Russia-Ukraine war exacerbate. Ambitious action is required to reach net-zero emissions. In the subregion, Morocco and Egypt are ahead of other countries towards investment in the green economy, including through issuance of green bonds. In September 2020, Egypt sovereign government issuance of green bonds in the Middle East and North Africa at US\$750 million and will fund a US\$1.9 billion green project portfolio in pollution prevention and control, sustainable water and wastewater management, clean mobility, and renewable energy while Morocco had issued five green bonds worth US\$416.7 million as of early 2020. Further, Morocco has one of the largest Concentrated Solar Power (CSP) plants in the world, the Noor Complex project.

Given current budget constraints in the public sector, the private sector has a critical role to play in generating and channeling additional finance towards the green transition. Private sector involvement in green investments however still faces several challenges in North Africa. Morocco, for example, is currently lacking remuneration policy framework for solar energy use. The green sector faces high competition from implicitly subsidized coal and gas power generation, modest financial incentives, particularly through guarantees, or tax breaks. Countries also lack national tracking systems for green private sector investment. It is therefore vital that IFIs and other actors provide advisory services and suitable financial solutions to help countries attract investment, assist local firms to create green jobs.

3. Expected Results of the Workshop

In view of the above, the meeting will be a platform for:

- Practitioners to share their understanding of challenges experienced by the private sector across the region as well as good practices and innovative solutions;
- Building on lessons learnt and experiences to identify policy options as well as methods that ensure their implementation can boost private sector participation in North Africa;
- Agreeing on developing a roadmap in tackling some of the challenges considering the institutional and political context of each North African country while identifying common actions.

4. Target Audience

The Workshop will comprise officials from the Ministries of finance, Planning & Economic development and particularly officials from the Investment & Private sector departments and policy makers from the member States. It will include participants from the private sector, academia, and development institutions with an expertise in private sector development.

5. Structure of the Workshop

The workshop will be participatory and interactive through structured case studies analysis, interactive question & answer sessions, and facilitated experience sharing allowing the exchange of personal and international, regional and national perspectives. The workshop is a three-day event that will have in depth discussion and practical understanding of the following pressing challenges for private sector development in North Africa:

Day 1:

- Keynote speaker;
- Session 1: The Role of the State;
- Session 2: Access to New Sources of Finance.
- Session 3: National and Regional Value Chains;

Day 2:

- Keynote speaker;
- Session 4: Panel on Innovation Capacity (with participation from the Tangier Free Zone).
- Session 5: Skills Gap: Success Stories from North Africa;
- Session 6: The Role of the Private Sector in Transition to Green Economy.

Day 3:

- Site Visit: Tanger Med

6. Contacts

For more information on the organization of the event, please contact:

Subregional Office for North Africa:

Focal point/Coordinator

Amandine Nakumuryango

Email: amandine.nakumuryango@un.org

Knowledge Management

Salem Sebbar

Email: sebbar@un.org

Communication

Houda Filali-Ansary

Email: filali-ansary@un.org

Administration/Logistics

Claude Wilondja Kapilukwa

Email: wilondjaclaude@un.org

Documentation

Mohammed Mosseddek

Email: mosseddek.uneca@un.org

Secretariat

Fouzia Assou

Email: assouqaddou@un.org

Phone (office): (+212) 537 71 56 13 & 537 71 78 29