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MINISTRY OF ECONOMY & TRADE



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LEBANON SME STRATEGY

A ROADMAP TO 2020



2014



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The “**Lebanon SME Strategy: A Roadmap to 2020**” has been initiated by the Ministry of Economy and Trade to ensure the long term planning and support for a key sector of the Lebanese economy.

The UNDP project at the Ministry of Economy and Trade: “Institutional Assistance for Economic Policy and Trade – Phase III”, has supervised, reviewed the strategy, and assisted with the organization of the wide consultations.

A steering committee composed of representatives of the public and private sectors was engaged in wide consultative process in order to ensure **transparency of the process of developing the strategy**, and broaden the participation by including the views and opinions of all stakeholders.

A number of workshops were organized with the Steering committee and expert groups during the process of developing the strategy to examine the validity of the approach, data and analysis.

In addition, the strategy document was disseminated to a large number of public, private and international organizations requesting their valuable feedback, which was incorporated where appropriate.

Thus, this strategy document is the result of the collective efforts of many experts and stakeholders, and I take the opportunity to express my appreciation of their efforts and to thank them all for their time and concern.

The Ministry of Economy and Trade will continue working with the key stakeholders from the public and private sectors to ensure the **proper and effective implementation of this strategy**, in order to empower and develop this important **SME economic sector** – which is the nerve of the economy and the main toll for fighting poverty – and promote economic growth, job creation and sustainable development.

Alain Hakim, PhD
Minister of Economy and Trade,
December, 2014

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01.

Executive Summary

Lebanon has built a reputation for a vibrant entrepreneurial landscape and a strong base of SMEs contributing significantly to its open economy. Indeed, throughout the past two-to-three decades, Lebanon has gone a long way in developing its ecosystem for entrepreneurs and SMEs. Starting by strengthening the enabling environment, moving to subsidized loans spearheaded by the Banque du Liban, to the establishment of national champions such as Kafalat and IDAL, to the more recent emergence of private sector led support and Banque du Liban's new initiative allowing banks to invest in startups, accelerators, and incubators, there has been a multiplicity of initiatives targeting especially the early stage entrepreneurs. Due to a myriad of reasons, impact seems to have been diluted, despite significant resources and efforts expended on the topic.

In this context, devising a guiding strategy upon which stakeholders can channel and coordinate policies, initiatives and programs is paramount to the success of the very SMEs all stakeholders are trying to help. This study is probably one of the few reports encompassing a holistic assessment of the current situation of SMEs and entrepreneurship in Lebanon and the strategy blueprint for the way forward for all stakeholders of the Lebanese entrepreneurial and SME ecosystem.

As nations grappled with the aftershocks of the global recession and search for employment creation, the benchmarks of other countries in the region and around the globe indicate a revival of interest in entrepreneurs and SMEs as one of the main driver for their economic recovery. They have established dedicated entities to spearhead the efforts, developed comprehensive strategies and plans, issued policies that nurture the ecosystem, and mobilized various stakeholders to support their SMEs, especially around talent, capital, and growth. Stakeholders in Lebanon are encouraged to take a similar approach.

The analysis of the entrepreneurial and SME ecosystem in Lebanon is driven along a 4-level framework covering the entrepreneur, the enterprise, the industry and the national elements. The analysis also took into account the differences between early stage entrepreneurs and more established SME business owners. Almost thirty challenges have been identified, of which five are overarching across the ecosystem.

They are summarized below:

OVERARCHING CHALLENGES

- **The Growth Barrier**, especially for SMEs which are unable to break through the next stages of growth and face high risks of long-term sustainability.
- **A Lingered Old Economy** delaying the transition to the knowledge economy due to limited leveraging of differentiated capability systems and meager R&D expenditures and efforts.
- **Changing Business Environment** stemming from globalized competition, empowered customers, and fast-changing technologies disrupting existing business models.
- **Economic Uncertainty and Cash Stressing** due to the slowing of business cycles combined with inadequate financing measures, which together put unenviable pressures on SMEs.
- **Uncoordinated Institutional Setup and Initiative Inertia** leading to limited concerted efforts and compounded by the rigidity of support initiatives in the face of an evolving landscape.

AT THE ENTREPRENEUR LEVEL – Culture

- **The Everlasting Owner Manager**, showcased by limited readiness for institutionalization, transition to professional management and true corporate governance.
- **Family First and Ownership Control**, a hereditary culture of ownership and highly valued unrestricted control causing small family-run businesses to keep their capital bases closed.
- **The 2nd two-million**, representing the enormous potential of women entrepreneurs who still reel under a continuing patriarchal culture and inadequate supporting environment.

AT THE ENTERPRISE LEVEL – Capabilities, Capital

- **The Middle Management Gap** driven by high emigration levels and poor talent retention ability leading to stagnation in the growth of companies and weak managerial pyramids.

- **An Ephemeral System of Capabilities;** whether organizational or individual, capabilities are not developed and built-upon to provide systemic competitive advantages.
- **A Mismatch in Demand and Supply of Capabilities** mostly pronounced in the lack of technical specialists and highly skilled workforce, and the shortage of vocational programs.
- **Distorted Cost of Capital Leading to Weak Capital Bases** driven by taxation policies and subsidies which encourage restrictive debt financing and shareholder loans.
- **Capital Mismatch** in the availability of the required type and volume of capital supply with a clear dominance of collateralized inflexible debt rather than more suited risk-sharing equity.
- **Limited Appetite for Outside Investors,** exacerbated by limitations of available financial instruments, restricting professional investment companies from playing an active role.

AT THE INDUSTRY LEVEL – Market Structure, Legal/Regulatory/Taxation Framework, Research and Innovation

- **Uneveled Playing Field** stemming from exclusive agencies, de-facto oligopolies and yet to be implemented antitrust laws and authorities.
- **Trading Inefficiencies** which remains lengthy and tedious, further impaired by a still idle trade promotion agency and lack of trade agreements with new top trading partners.
- **Legal Enforcement vs. Contractual Goodwill,** a conundrum due to still inefficient judicial system resulting in costly and lengthy proceedings reducing the utility of contracts for SMEs.
- **Weak Creditor Protection** with recovery rates barely over 32% and a process stretching for almost 3 years leading to high collateral requirements and limited effective restructuring.
- **One-Size Fits All Taxation** revealed through insufficient differentiation for SMEs and underutilized incentives available in existing system.
- **Persisting Red Tape** especially apparent in bureaucratic inefficiencies and costly regulatory and setup processes, often putting SMEs at a disadvantage compared to larger competitors.

- **Companies in Perpetual Limbo** due to the enduring cultural stigma of failure further aggravated by the procedural difficulty of teetering SMEs to restructure efficiently.
- **Untapped Innovation Potential** due to insignificant budgets and low innovation efficiency despite the availability of the required institutional setup and human capital.
- **Nascent IP Protection** exhibited in the 2000 patent law and the IP protection office at MoET, however still marred by a weak deposit-based framework.
- **Poor Market Research** leading to unreliable and irregular information, upon which SMEs and entrepreneurs develop strategies, build business plans and size their markets.

AT THE NATIONAL LEVEL – Employment and Labor, Financial Markets, Infrastructure and Enablers

- **Informal Workforce Market** sustained by the perception of high fixed employment costs and the relative availability of ‘freelancers’ and contract workers.
- **Hurdles for Foreign Skilled Labor** with no special provisions for high value-adding professionals and limited encouragement for knowledge transfer.
- **Shallow Beirut Stock Exchange** with low capitalization (at ~US\$ 11 billion¹) and very low trading volumes, reducing its attractiveness for listing and as a possible source of capital.
- **Infrastructure Patches** across the country to cover for the poor state of development across the territory, particularly in terms of cost and quality of ICT, broadband, roads, and electricity, and leading to significantly reduced competitiveness of SMEs.

Historically, Lebanon’s lack of a formal unified definition for small and medium enterprises has often been used as a scapegoat for inaction. Moreover, statistical information is scarce with the most quoted reference dating back to 2004 from the Central Administration of Statistics. More recent information on SMEs in Lebanon has been gathered to better understand their distribution. More importantly, a simple definition is proposed in line with the approach suggested by global benchmarks adjusted to the specificities of the Lebanese market. Namely, the proposed definition combines annual turnover and number of employees as follows:

¹ As of July 2014

- **Micro Enterprise:** Less than LBP 500 million AND less than 10 employees
- **Small Enterprise:** Less than LBP 5 billion AND less than 50 employees
- **Medium Enterprise:** Less than LBP 25 billion AND less than 100 employees

Exceeding either dimension would position the SME in the subsequent category. Adopting this definition, SMEs in Lebanon constitute between 93 and 95% of enterprises in the country.

In this context, and based on the review of the landscape, the gaps between challenges and support initiatives currently in play as well as the global and regional benchmarks, the study proposes a national strategy for Lebanon's entrepreneurs and SMES with the ambitious vision of:

SMEs as Key Economic Engine for Growth and Job Creation

Achieving the vision is incumbent upon all stakeholders to execute the mission:

Foster the Creation of Vibrant and Globally Competitive SMEs that Contribute to Employment Opportunities and High Value-Added Economy

The strategy's main objectives are four-fold:

- **Small to Large:** Grow SMEs through their next stages of development;
- **Sustainable:** Ensure the long-term sustainability of businesses;
- **Innovative:** Develop innovative and creative SMEs to transition to a high-value economy;
- **Competitive:** Transform SMEs into more productive, competitive and global players.

Achieving these objectives rests upon six strategic thrusts, which are essentially families of initiatives that constitute the pillars upon which rests Lebanon's National SME strategy. These are namely the following:

- **Evolving Business Leaders:** aims at assisting SME owner-managers in evolving their corporate culture, professionalizing management, developing new leaders, and transitioning to real effective corporate governance;
- **Facilitating the “Right” Funding:** aims at encouraging SMEs to strengthen their capital structures for growth and resiliency, ensuring availability of adequate sources of funding adapted to SME needs, and providing a supporting framework to match smart VC/PE capital to entrepreneurs and business owners;
- **Improving Access to Markets:** aims at minimizing structural market inefficiencies to improve SME competitiveness, and enhancing access to foreign markets and in particular to fast-growing economies and ones where Lebanon has an edge;
- **Enhancing Capabilities and Innovation Capacity:** aims to build Lebanon’s core specialized capabilities, and to develop supporting framework as well as interdependent networks that build upon Lebanon’s differentiated capabilities found in both individuals and organizations;
- **Developing a Conducive Business Environment and National Environment:** aims to address SME-critical elements of the business environment, focusing on developing SME-friendly employment, legal, regulatory and taxation frameworks, as well as concentrate infrastructure development efforts into coherent and comprehensive sector-focused zones;
- **Ensuring Coherence and Effective Coordination:** aims at developing strong effective coordination mechanisms among public and private sector stakeholders in order to ensure coherence and streamlining of SME support efforts.

Around forty initiatives were identified across the six aforementioned strategic thrusts. These were prioritized into three implementation waves that will take place until 2020, depending on the respective impact and ease of implementation of each.

The study concludes with a frank call for action and collaboration by all public and private sector stakeholders to implement the strategy in order to benefit from SMEs as one of the main drivers of the Lebanese economy.

02.

Introduction

Touted as one of the primary axes for the salvation of national economies, SMEs and entrepreneurship have become one of the foundational drivers for the creation of economic value, source of innovation, employment, and wealth generation across the globe. In Lebanon, over 90% of enterprises currently active in the economy can be categorized as SMEs. Despite the significant attention Lebanese SMEs and entrepreneurs garnered over the past few years, leveraging this economic engine has been a series of independent efforts that have led to mixed results.

However, as this study will show, Lebanon boasts all the right ingredients for success: educated entrepreneurs who seek to monetize opportunities, a sophisticated financial industry with global tentacles, talent with multinational experience, and unique capabilities that historically allowed Lebanon to outshine its expected fair share of the global economy. Yet, Lebanon still faces several challenges that impede reaping the full benefit of SMEs.

Today Lebanon has a unique opportunity to galvanize all parties to work in unison towards developing SMEs and entrepreneurship as a new pillar of the Lebanese economy. This strategy document, while mandated by the Ministry of Economy and Trade, is meant to be a working roadmap for both the private and public sector entities in order to ensure the coherence of efforts to support and develop this undoubtedly vital element of the economy.

2.1. Short History on SME and Entrepreneurship Development in Lebanon

After emerging from the Lebanese civil war, considerable efforts were spent to redress the national economy. In fact, over the past two decades, Lebanon witnessed several waves of interest in supporting private sector as the main engine of growth.

The 1990s were focused on setting the stage: strengthening the enabling environment to allow private enterprises to succeed. As companies were seeking to establish a solid footing for recovery, most efforts were naturally government led and included initiatives such as the enactment of new laws (e.g., the National Investment Law which was promulgated in 2001), improvements in administrative setups (e.g., the establishment of the Investment Development Authority of Lebanon (IDAL) in 1994 to encourage large investments in the country), the reactivation of the Beirut Stock Exchange in 1996 and the launch of economic zones.

The early 2000s witnessed the second wave of efforts focused on sectorial initiatives: long-term subsidized loans focusing on selected industries became in vogue. The main actors during this period were Banque du Liban with significant involvement and support of foreign development agencies (e.g., European Investment Bank). A major actor in the Lebanese private sector ecosystem also emerged: Kafalat, Lebanon's credit guarantee scheme, was jointly established by a group of fifty Lebanese banks and the National Institute for the Guarantee of Deposits. In this context, the launch of Lebanon's first "Ease of Doing Business" report in 2004 by the World Bank Group became the initial trigger for attention to SME support.

Since 2005 onwards, the focus of support in Lebanon shifted to SMEs and more considerably to entrepreneurship. This was buoyed by the global attention to the topic, especially in the context of the global financial crisis and rising unemployment, as well as more local findings such as reforms prompted by the 2007 Lebanon-Paris III program. During this period, the Lebanese scene also saw the advent of new players, namely from the private sector and NGOs. Initiatives and entities such as the Bader Program, Berytech, Arabnet, MIT Enterprise Forum, Endeavor, and Middle East Venture Partners were established and took an active role in funding, supporting and developing entrepreneurs.

The government and chambers of commerce also partook in these recent developments through initiatives such as the launch of IBEL², and business development centers (SouthBIC, BIAT)³. In particular, the Ministry of Economy and Trade (MoET) coordinated

a working group on improving the overall business environment focusing on the regulatory side. Later, MoET established an SME Unit - "Enterprise Team" - with the support of the UNDP. In 2005, this unit started the implementation of the Integrated Small and Medium Enterprise Support Programme (ISSP); however adoption of this strategy lacked sufficient traction.

During the past two years, after consultations and workshops with several government and private sector stakeholders, the Ministry of Economy and Trade⁴ defined three priorities to set the path forward:

1. Set a comprehensive five-year National SME Strategy
2. Prioritize ongoing initiatives, key challenges and opportunities
3. Ensure multiparty participation in the development of the SME Strategy

Simultaneously, the outcome of these consultations indicated the need to set up working teams and units to execute the prospective strategy.⁵

In this context, MoET has mandated the development of this study to accomplish these priorities.

² Improving the Business Environment in Lebanon

³ South Business Innovation Center; Business Incubation Association in Tripoli

⁴ With the support of the UNDP SME unit

⁵ These units are: the SME Observatory, a National Taskforce on SME Development, and an SME Advisory Panel

2.2. Scope of Work and Purpose of this Document

To develop the strategy, a 9-step approach was adopted as shown in *Figure 1* below, in compliance with the requirements of the Ministry of Economy and Trade / United Nations Development Program stated in the RFP with reference number LEB/CO RFP/96/13 dated November 1, 2013 (please, refer to Scope of Work in the Appendix for details).

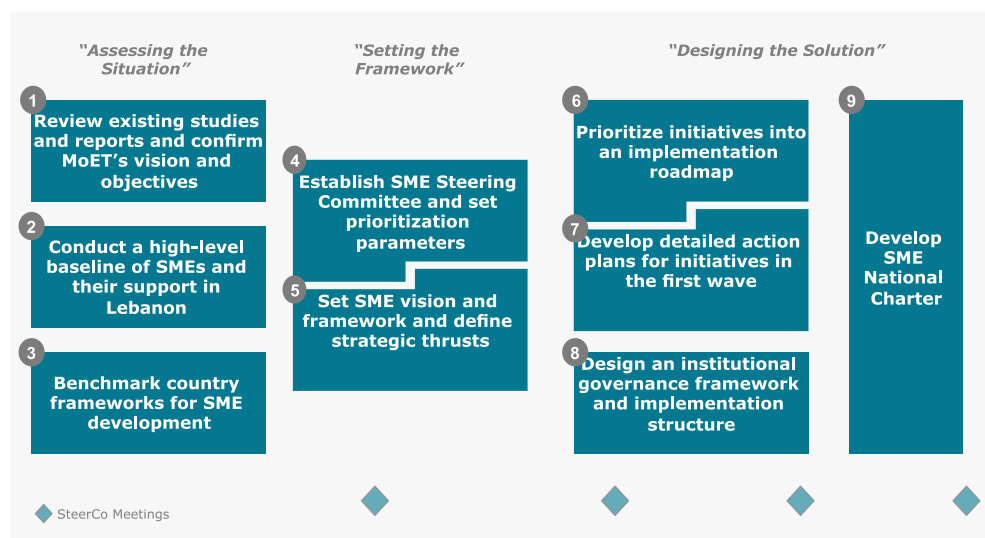


Figure 1: Proposed Approach

The first section of this report summarizes the key findings from the analysis of the existing entrepreneurial and SME landscape. The second section provides a comprehensive strategy with a call for action that encompasses both the private and public sector stakeholders. Overall, the report constitutes one of the few overarching perspectives on the SME and entrepreneurial ecosystem in Lebanon.

As the title indicates, this study is written as a national roadmap to support the success of SMEs and entrepreneurs. The strategy lays down a unified vision and a clear set of objectives for SMEs. It also identifies strategic thrusts that are the foundational drivers for SMEs to thrive and succeed in the country. As such, it should be continually adapted to the realities of challenges and opportunities in the market.

Further details are available in the full extended study accompanying this summary report and submitted to the Ministry of Economy and Trade.

2.3. Framework Definitions

In the assessment of the current situation, two frameworks are adopted that will assist in structuring the analyses. The first defines the essential elements of the ecosystem in which entrepreneurs and SMEs operate. The second defines their evolution from the nascent entrepreneur to the mature owner-CEO. In seeking to be as comprehensive as possible, several frameworks were reviewed, synthesized and amalgamated from other studies (among others, the World Bank's Doing Business, World Economic Forum's Global Competitiveness Report, the Global Entrepreneurship Monitor, and WEF/Booz & Company's Accelerating Entrepreneurship in the Arab World) in order to arrive to the ones proposed here.

2.3.1 The SME / Entrepreneur Ecosystem

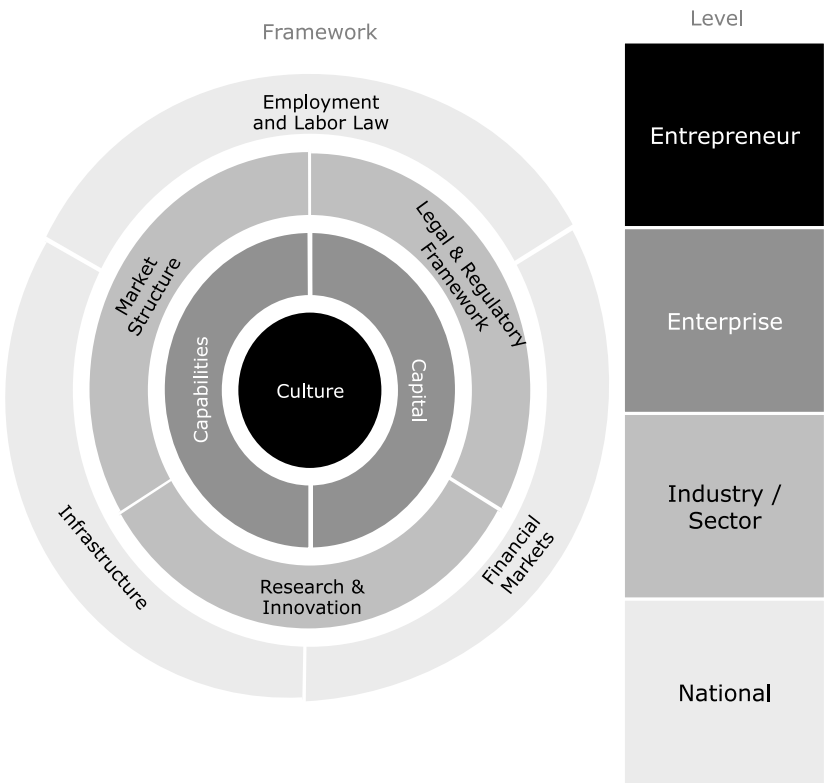


Figure 2: SME Ecosystem and Assessment Framework

SMEs operate in a complex ecosystem of interrelated elements spread across four levels, each building on the other (*Figure 2*). These impact the ease and speed at which entrepreneurs and SMEs can establish new ventures and scale them into sustainable and competitive businesses.

At the Entrepreneur level, culture is of primary importance. In the assessment, the characteristics of entrepreneurs and readiness for risk taking were identified. In addition to the institutionalization culture of business owners and the availability of support mechanisms including mentors, incubation environments, etc.

At the Enterprise level, Capital and Capabilities are the key elements. In terms of Capabilities, the availability and adequacy (quality/quantity) of human capital (including formal education levels, managerial, technical skills, etc.), as well as the level of productive knowledge in the economy were assessed. As for Capital, the access and depth of equity (angel, VCs, etc.) and debt capital and financial support (grants, government subsidized preferential loans, etc.) were evaluated. In addition to the adequacy of funding instruments available to SMEs and entrepreneurs.

At the Industry/Sector level, three main elements emerge: Market Structure, Research & Innovation, and the Legal & Regulatory Framework including tax regime. In the assessment of Market Structure, the SME access to local and regional/global markets, its size and competitive landscape, and level of development of the supply chain for input factors were reviewed. As for Research and Innovation, the adequacy of support and funding for R&D and the level of innovation were evaluated. For Legal and Regulatory Framework, the availability of sector and industry specific regulations (anti-trust, protectionism, etc.), the adequacy of legal framework (commercial laws, etc.), judicial procedures and contract enforcement, as well as licensing, permitting and taxation regimes were reviewed.

Finally at the National level, Employment and Labor law, Financial Markets, and the national Infrastructure and Enablers were reviewed. For Employment and Labor law, the ease of hiring and firing employees, and the access to immigrant workforces were gauged. For the Financial Markets, the breadth and depth of equity and debt capital markets were evaluated. Finally for Infrastructure and related enablers, the availability and quality of the country's infrastructure necessary to support the operations of SMEs (including public utilities, transportation networks and ICT) were assessed.

2.3.2 From Nascent Entrepreneur to Mature Owner-CEO

When examining these elements, one should be cognizant of differences between fledgling entrepreneurs and established business owners. To the extent possible, the differences between the different stages of evolution of enterprises and entrepreneurs were highlighted in the analysis (*Figure 3*). For simplicity, an entrepreneur is any person in the seed or early stage, and business owner any person in the growth or maturity stages.

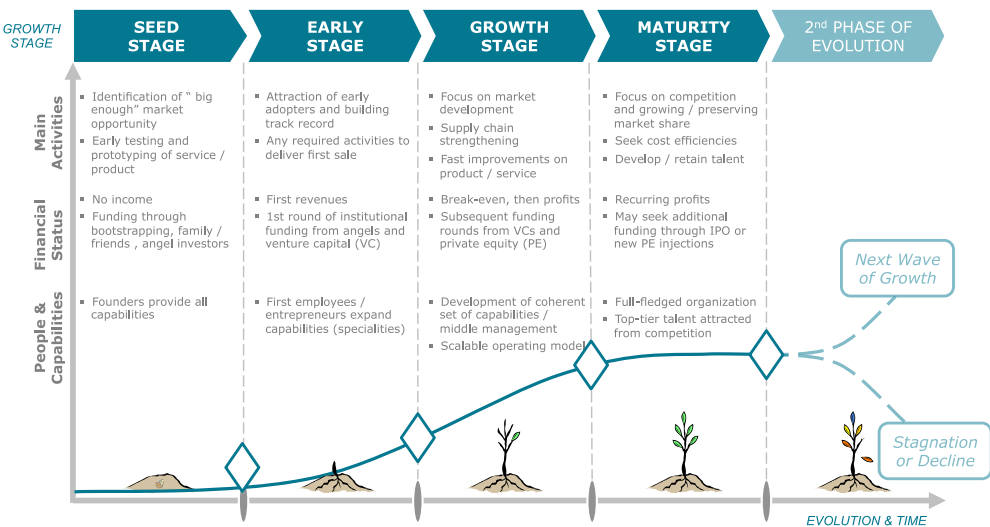


Figure 3: Development Journey of Enterprises and Entrepreneurs

2.4 SME Definition

Historically, Lebanon lacked a formal unified definition of small and medium enterprises. Public and private sector entities developed definitions that suited their requirements.⁶ This technical shortcoming in definition has often been used as a scapegoat for inaction. In order to address this issue, this study recommends the adoption of a unique and simple definition.

Generally, a standard definition for SMEs is an important component in developing a national strategy and is typically devised to achieve one or several objectives, including:

- Statistical data analysis of the country's economic structure and development of associated strategies
- Directing state aid to specific tranches of enterprises (e.g., the Kafalat programs)
- Defining thresholds for regulatory and administrative facilitation and exemptions from a broad range of obligations (e.g., simplified tax procedures)
- Targeting policy measures to take advantage of qualities specific to SMEs
- Provision of quotas for government contracts and procurement

Traditionally, SME definitions have been set by using the number of employees as an indicator. Today, most benchmarked countries use a combination of financial indicators and employees. For instance, the European Union uses a combination of headcount and either of annual turnover or assets on the balance sheet. The United States adopted a more elaborate statistical approach that takes into account industry specificities and standard sizes within each. Examples of both models are shown in Figure 4.

Figure 4: SME Definition Examples⁷

- EU example -				- USA example -		
Category	Headcount	Annual Turnover	OR Balance Sheet	Sector	Headcount ¹	Turnover ¹
Micro	<10	≤ €2M	≤ €2M	Manufacturing and Mining	≤500	
				Buildings/Heavy Construction		≤33.5\$ M
Small	49- 10	≤€10 M	≤€10 M	Retail Trade		≤19\$ M
				Wholesale	≤100	
Medium	249- 50	≤€50 M	≤€43 M	Farming		≤0.75\$M
				Services		≤14\$ M

⁶ E.g., Banque Du Liban defines SMEs as enterprises with less than LBP 15 billion in annual turnover, while Kafalat defines SMEs as having less than 40 employees

⁷ US thresholds are based on medians of industries; sub-industries may differ

Moreover, it is noteworthy to highlight that SME definitions vary among countries, with typically higher thresholds set in more developed countries (*Figure 5*), owing to the naturally larger enterprises.

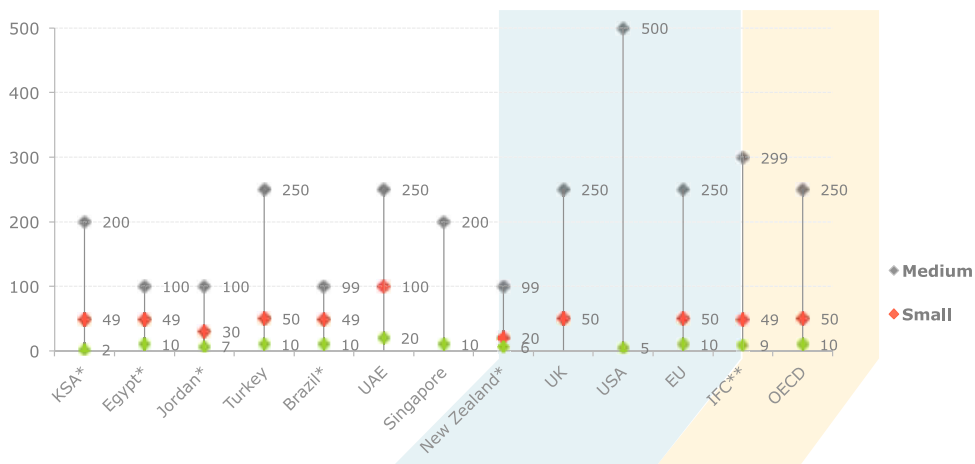


Figure 5: SME Definition across Different Countries - Headcount Perspective

2.4.1 Proposed SME Definition and Current Statistics

A benchmark review indicates that the SME definition should be tailored to the Lebanese market structure primarily, acknowledging that some industry specificities may need to be taken into account. In this context, the analysis of over 70,000 active enterprises in Lebanon was undertaken based on data from the Ministry of Finance, with caveats for under reporting and the informal sector. Reconciliation with other data sources such as the National Social Security Fund are currently impractical; however, it is recommended in the future.

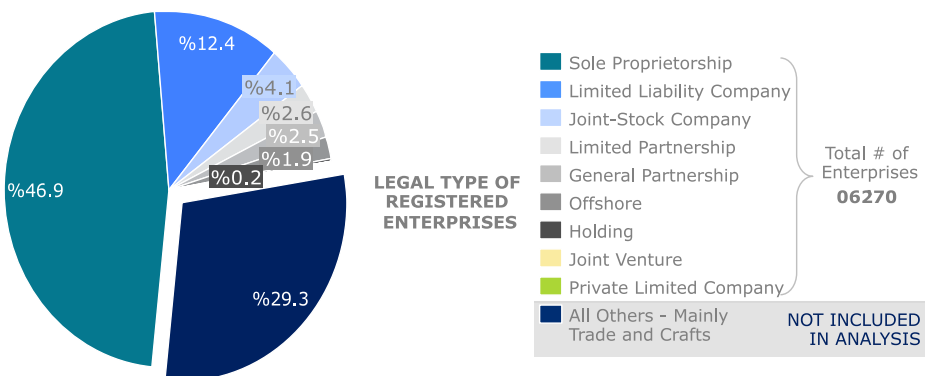


Figure 6: Selected Entities from Registered Enterprises

In developing the SME definition for Lebanon, one needs to account for a simplified approach that takes into account several considerations and constraints including:

- Underreporting of employees and/or financials implies a combination of both may provide stronger definition than a single measure
- Availability of coherent, comprehensive historical data on SMEs is limited in order to tailor thresholds by industry
- Taxation data is currently the most reliable information available to the government
- A simplified definition is easily verifiable and easily understood by both SMEs and policymakers
- Accurate financial statements may not be easily available for SMEs to use asset based data

As such, a simple approach to define SMEs based on annual turnover and number of employees is proposed. It is also recommended to revise periodically the validity of thresholds set in this definition in order to ensure it still serves the purpose for which it was set.

From an annual turnover perspective, the recommended thresholds for Micro, Small and Medium sized enterprises are LBP 500 Million, 5 Billion, and 25 Billion respectively.

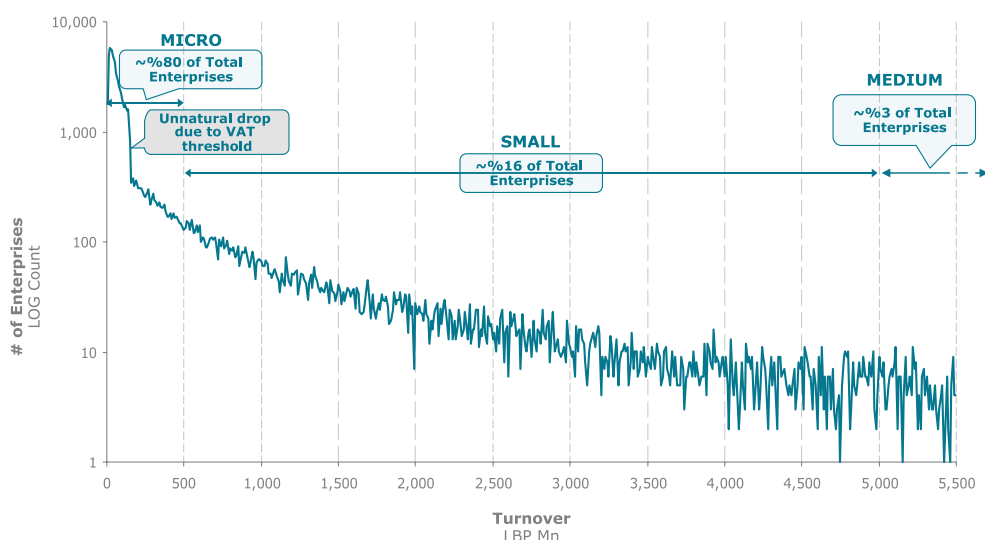


Figure 7: Distribution of Enterprises by Turnover Bracket (May 2014)

A high-level regional and sectorial analysis (*Figure 8, Figure 9*) of Lebanese enterprises according to these recommended thresholds highlights that Mount Lebanon and Greater Beirut account for ~80% of registered enterprises and that trade, manufacturing and real estate activities also account for ~80% of registered enterprises.

More interestingly, comparing across regions and sectors, the same distribution pyramid in terms of count and turnover were noticed. This indicates that despite the aforementioned concentrations, from a policy targeting perspective, there are no apparent advantages to any region or industry. Thus SME policies have the potential of benefiting the entire country and all industries.

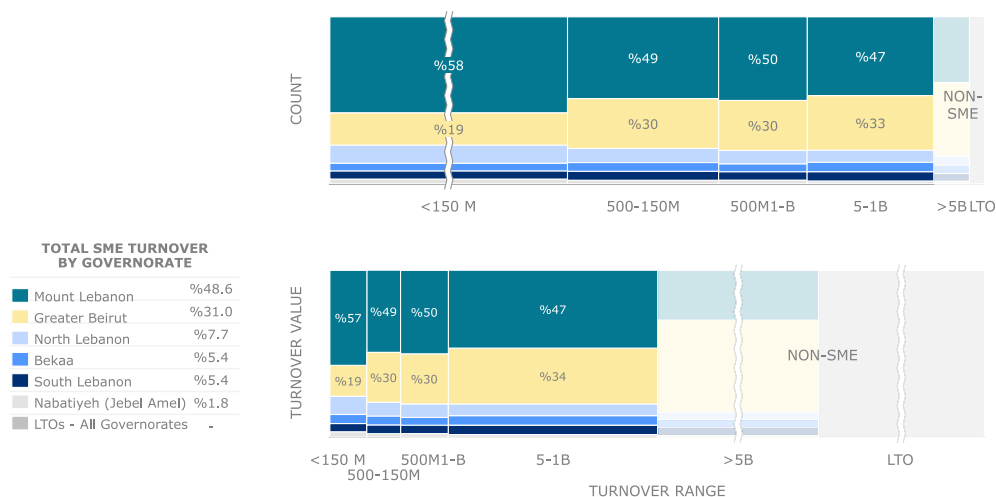


Figure 8: Regional Distribution by Count and Turnover ⁶

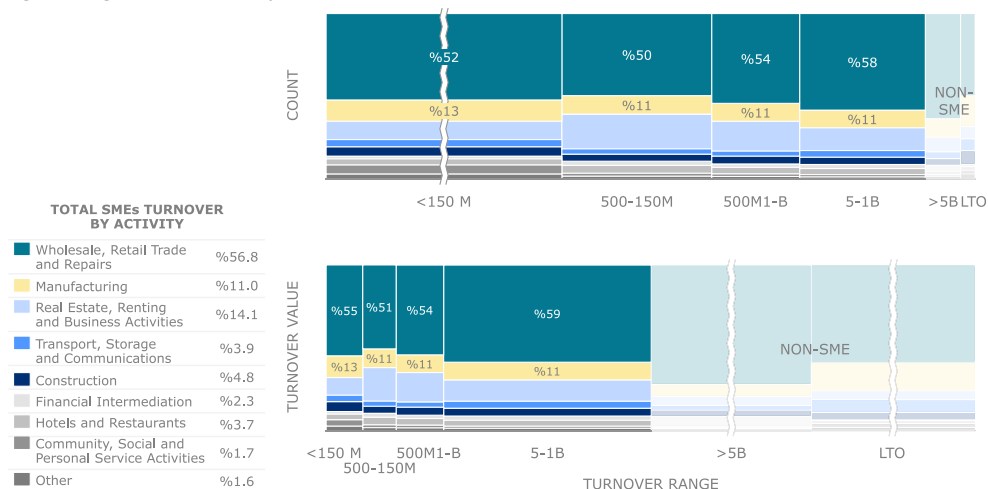


Figure 9: Sectorial Distribution by Count and Turnover ⁷

⁸ Based on MoF – LRD database, 2011 values; LTO: Large Taxpayers Office, entities with large turnovers exceeding LBP 10 billion

From an employee count perspective, the recommended thresholds are 10, 50 and 100 employees for Micro, Small and Medium enterprises respectively. Based on these thresholds, SMEs employ roughly half of the employees declared to the Ministry of Finance.

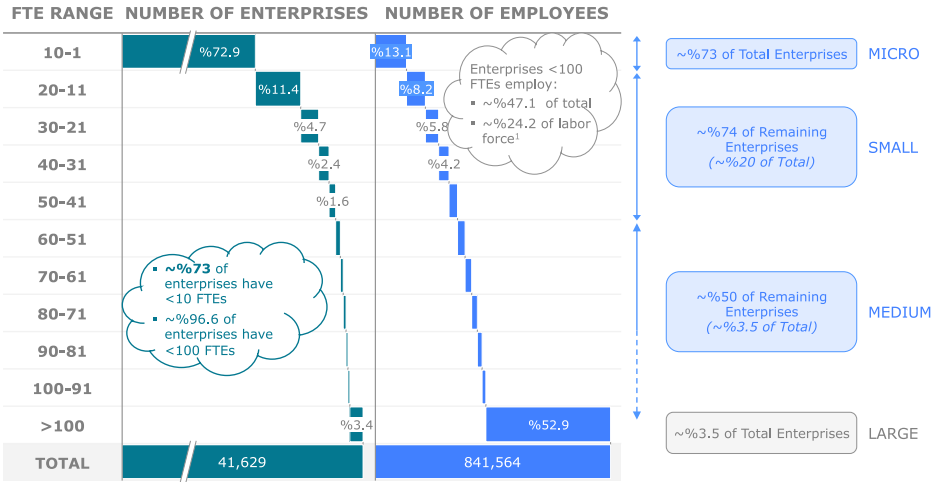


Figure 10: Enterprise Distribution by Employee Bracket (May 2014)

Combining both dimensions, *Figure 11* below proposes the recommended standard definition of the thresholds between the different sizes, namely Micro, Small and Medium enterprises. The definition assumes that an enterprise must meet both Turnover and Employee thresholds in order to be considered in a particular category. For instance, a medium enterprise should simultaneously have between 50 and 100 employees AND an annual turnover between LBP 5 and 25 billion. Exceeding either of these thresholds would lead to recognizing enterprises in the next category.

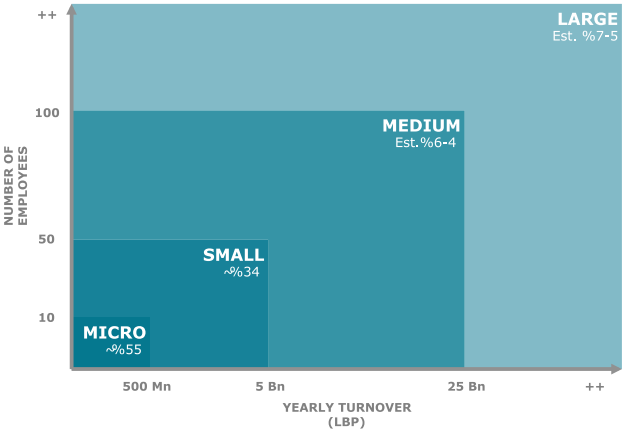


Figure 11: Proposed SME Definition for Lebanon

Adopting this definition, SMEs in Lebanon constitute ~93-95% of the population of enterprises in the country.

03.

Status of the Lebanese SME and Entrepreneurship Ecosystem

To drive the strategy, it is necessary to build a solid understanding of the ecosystem in which SMEs and entrepreneurs operate. This section analyzes the different elements highlighting advantages to build upon, and challenges that need to be addressed.

3.1. Entrepreneur Level

It is known that Lebanon is considered a forming ground of entrepreneurs in the region. In fact, according to the Global Entrepreneurship Monitor, Lebanon boasts a high rate of early-stage entrepreneurial activity reaching ~15% of the working-age population. This may be attributed to the country's tradition of liberalism and private sector domination.

In most countries with similar economic development, these high levels of entrepreneurial activity are typically driven by necessity. The need to earn an income is the main motivation leading entrepreneurs to establishing businesses with low contribution to economy (e.g., corner shops, handy work).

However, unlike these countries, ~82% of Lebanese entrepreneurship is opportunity-driven. Rather than being forced, Lebanese entrepreneurs actually seek to exploit business opportunities they have identified. These businesses are typically high-growth and have high-employment potential. Building on this advantage, Lebanese entrepreneurship can become an essential lever for economic development and the fight against unemployment. This finding is further reinforced by the fact that Lebanese entrepreneurs and SME owners are 2-4 times more likely to be highly educated persons who already have jobs, a pattern generally quite different and unseen in other MENA countries (Figure 13, Figure 14).

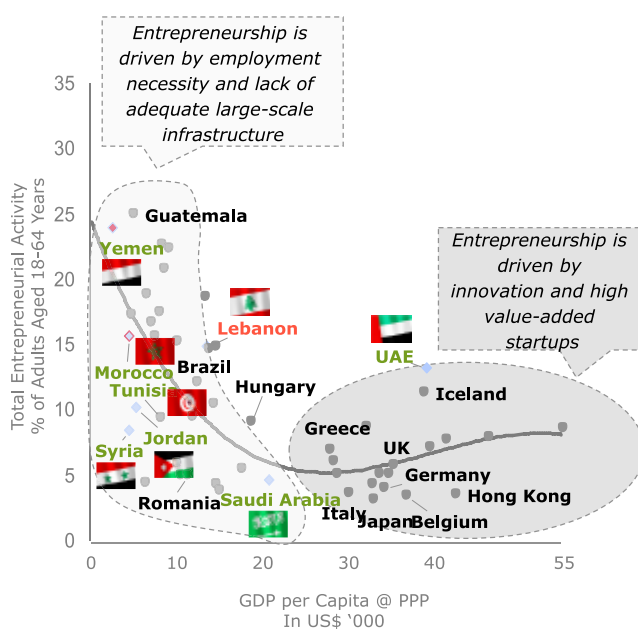


Figure 12: Early Stage Entrepreneurial Activity vs. GDP/Capita

TOTAL ENTREPRENEURIAL ACTIVITY
% of Adults Aged 18-64 Years by Education Level

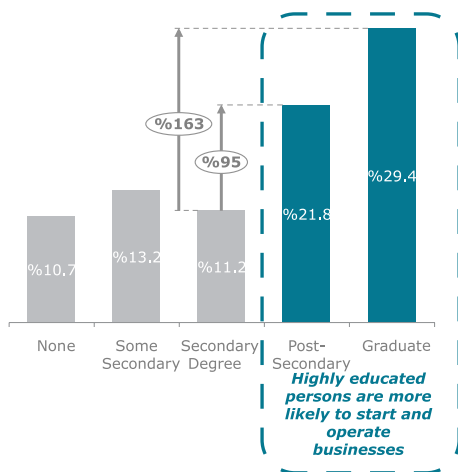


Figure 13: Entrepreneurial Activity by Education Level

TOTAL ENTREPRENEURIAL ACTIVITY
% of Adults Aged 64-18 Years by Work Status

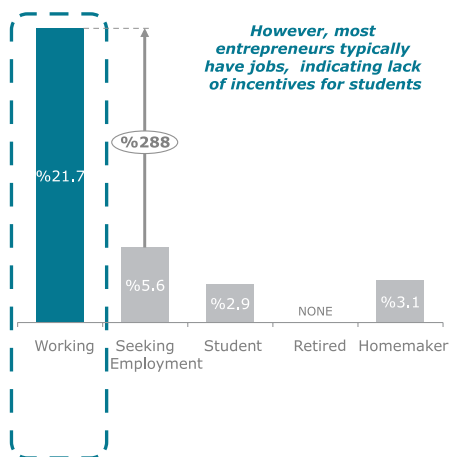


Figure 14: Entrepreneurial Activity by Status

Moreover, Lebanese entrepreneurs are typically successful in building sustainable businesses that persist beyond the early difficult foundational stages. In fact, according to the Global Entrepreneurship Monitor, Lebanon has one of the highest densities of established business owners, not only in the MENA region, but even globally, across all countries covered in the report (16% of the adult population).

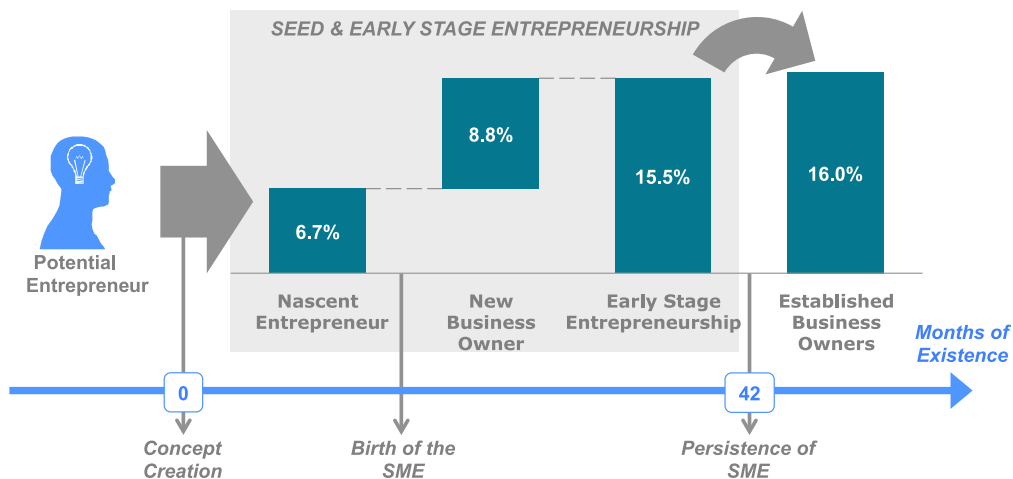


Figure 15: Distribution Across Entrepreneurial Stages

Typically, Lebanese entrepreneurs are twice more likely to be in consumer-oriented industries (retail, hospitality, etc.) as compared to any other sector. The remainder is more likely to be in business services and transforming sectors (manufacturing, construction, distribution). Overall, they also tend to have a higher degree of international orientation as compared to other MENA countries.

However, several challenges impede the development of entrepreneurs and SME owners to the next stages of evolution.

The Everlasting Owner-Manager

Lebanese entrepreneurs have shown relatively limited readiness to institutionalization and preparedness for transition from the model of owner-manager run businesses to long-term sustainable organizations with professional management. Additionally, there is limited effective use of corporate governance, with too few, if any, independent directors, and where boards functions mostly as a “rubber stamp” (Figure 16).

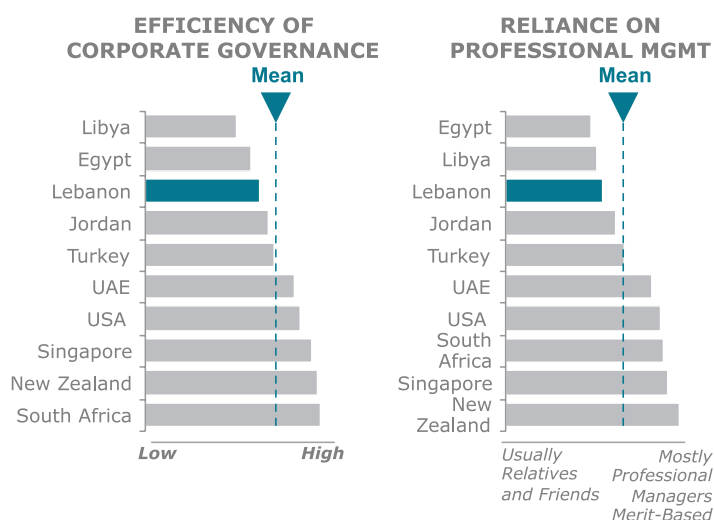


Figure 16: World Economic Forum Indicators (2013-14)

Family First and Ownership Control

Lebanese SMEs have significant hereditary and a family-centered approach to owning and managing businesses. Moreover, business owners often value unrestricted control over their companies more than they do higher profits and finding the least expensive form of finance (e.g., cheaper capital in the stock market). As such, many SMEs keep their capital based closed and remain forever small family-run businesses rather than large family-owned corporations.

The 2nd two-million

Lebanon's track record of SMEs indicates a low participation of women in SME leadership positions, especially in stages beyond startups (*Figure 17*). While a decline may be explained by the natural evolution of young women into motherhood and its requirements, this is also stemming from a continuing patriarchal culture and inadequate supporting environments. In fact, women entrepreneurship in Lebanon tends to peak between the ages of 35-44, a full decade after men. Moreover, unlike their men counterparts who are relatively evenly distributed, women entrepreneurs and business owners tend to come from upper-third household income, indicating a relative financial comfort in their family thereby lowering the risks of launching their businesses. However, some initiatives have been launched to promote more women participation and

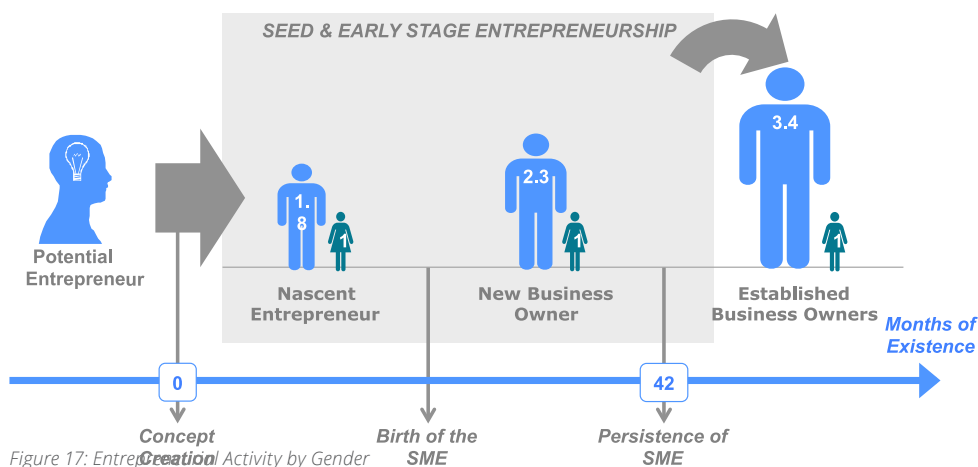


Figure 17: Entrepreneurship Activity by Gender

address some of the issues they face (e.g., W.E. initiative).

From a support perspective, multiple initiatives have been successful in assisting the launch and growth of entrepreneurs and SMEs. A robust, yet nascent, environment of incubators and entrepreneurial support organizations exists in Lebanon:

- Seed-to-early stage incubators and accelerators (e.g., Berytech, Speed@BDD, BIAT, etc.)
- Early-to-growth stage support entities and initiatives (e.g., Bader, Endeavor, Lebanon for Entrepreneurs LFE, Wamda's Mix-n-Match, Mowgli, etc.)
- Entities supporting institutionalization of SMEs (e.g., LCGT, LTA, etc.)⁹
- Competitions promoting entrepreneurial culture across various sectors (e.g., MIT Arab Business Plan Competition, Grow My Business, ArabNet competitions)

Moreover, Lebanese universities have recently launched several entrepreneurial and SME programs that help foster capabilities and promote culture; however their success is yet to be determined (e.g., AUB's Center for Innovation Management and Entrepreneurship, LAU's Institute of Family & Entrepreneurial Business, BAU's Center for Entrepreneurship).

⁹ LCGT: Lebanese Corporate Governance Taskforce; LTA: Lebanese Transparency Association

3.2. Enterprise Level

3.2.1 Capabilities

Access to capabilities constitutes the lifeblood of any enterprise, small or large. Capability systems that companies develop over time essentially define how they can play in any particular market. Together with their external positioning, if orchestrated into a coherent strategy, companies earn the “right to win”. While large enterprises face difficulties in getting the right talent, SMEs face an even more difficult challenge in attracting capabilities given smaller resources and budgets, and limited brand equity.

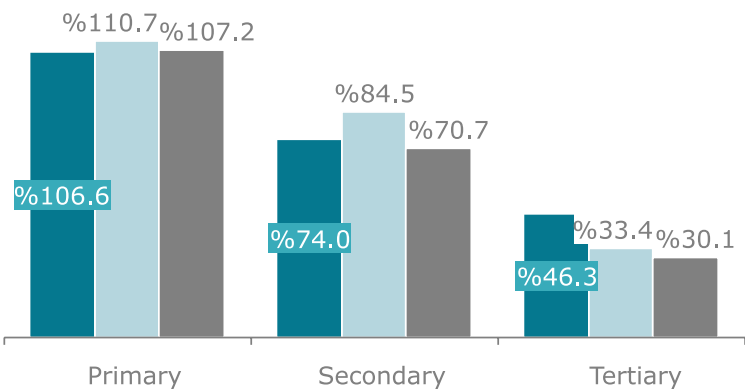


Figure 18: Enrollment Rates in Educational Institutions (%)

At a country level, and from a traditional capability perspective, Lebanon SMEs have access to a highly educated workforce that exceeds the average Upper Middle Income countries, according to the World Bank (*Figure 18*).

However, the usefulness of knowledge at an individual level is limited. In fact, a recent joint study by Harvard and MIT¹⁰ showed productive knowledge, a measure of the collective explicit and tacit knowledge a society amasses over the course of its evolution, to be significantly correlated to a country's income level.

Indeed, productive knowledge builds on the diversity in knowledge domains and linkages between them through teams and organizations to generate a fertile ground for the development of a diverse set of unique and sophisticated products and services.

¹⁰ The Atlas of Economic Complexity: Mapping Paths to Prosperity, Hausmann and Hidalgo

These are the differentiating capabilities that allow organizations, including SMEs to be truly competitive.

To measure productive knowledge and hence a nation's capabilities, the aforementioned study suggests the analysis of the composition of its outputs (namely exports) which are an expression of the capabilities required to produce them – thus, the Economic Complexity Index measures the nature of a country's exports through two main dimensions:

- Diversity of products, to indicate the variety and broad base of available capabilities
- Ubiquity of products, to indicate the level of uniqueness of capabilities, and implicitly competitiveness

High economic complexity reflects the ability of a society to hold and put to use a larger amount of productive knowledge. In Lebanon's case, despite its small population, the increasing Economic Complexity Index (*Figure 19*) indicates a positive evolution of the country towards more varied, unique and complex set of capabilities, and hence an increase in overall competitiveness.

With adequate coordination and facilitated access, Lebanese SMEs and entrepreneurs can benefit from capability systems already built to further advance and develop new ones. Implicitly, this would set apart Lebanese SMEs on the basis of product and services attributes as well as optimized processes which eventually lead to quality and price differentiation.

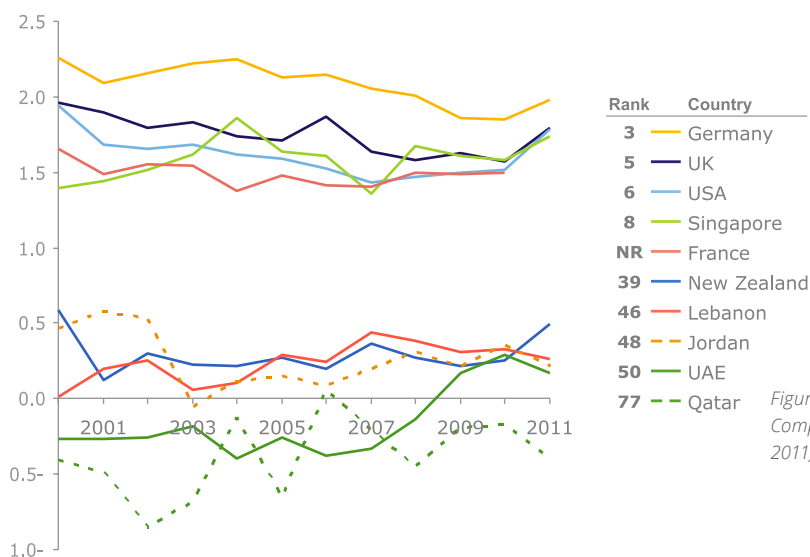


Figure 19: Economic Complexity Index (2000-2011)

Lebanon's main capability challenges have not been a lack of "raw material" – human capital, knowledge potential, educational institutes are all available – but rather developing, fostering and retaining these unique differentiating capabilities has not been systemic. Below are the most salient challenges:

The Middle Management Gap

Lebanon faces a gap in middle management characterized by the scarcity of educated and experienced mid-level managers and leaders (~3-10 years of experience) with adequate business and management capabilities (*Figure 20*). This has been due to waves of emigration driven by unfavorable socio-economic conditions and poor talent retention ability (e.g., glass ceiling in family businesses, unclear career path, and uncompetitive pay). Economically, this anomaly leads to stagnation in the growth of companies: managerial pyramids that allow delegation are weak and knowledge of a particular company's business intricacies is lost with the forgone talent; both of which require efforts and resources to rebuild.

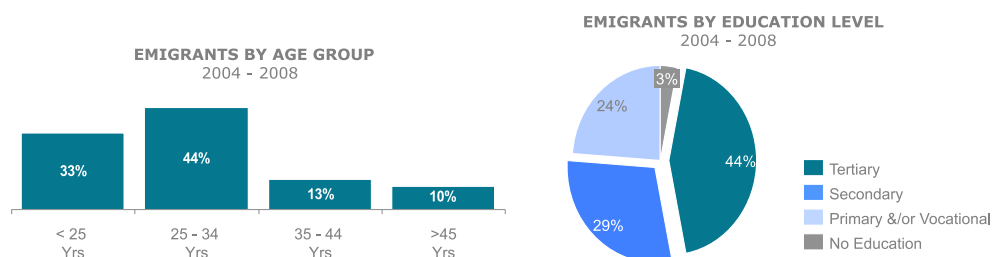


Figure 20: Profile of Lebanese Emigrants

An Ephemeral System of Capabilities

Capabilities, organizational and individual, are not systemically developed and leveraged to provide the country's SMEs with a competitive advantage. To a large extent, the challenge has been attributed to limited coordination and planning. This is especially apparent in Lebanon's product space – essentially a map that shows the different industries, highlighting ones where Lebanon has a comparative advantage as measured by exports above its "fair share" of global trade. Linkages between industries on the product space map represent the transferability of knowledge and capabilities among them. A case in point for the ephemeral system of capabilities in Lebanon resides in the industry of garments, textiles and fabrics which all require interrelated capabilities (shown in dark green on the right side of *Figure 21*).

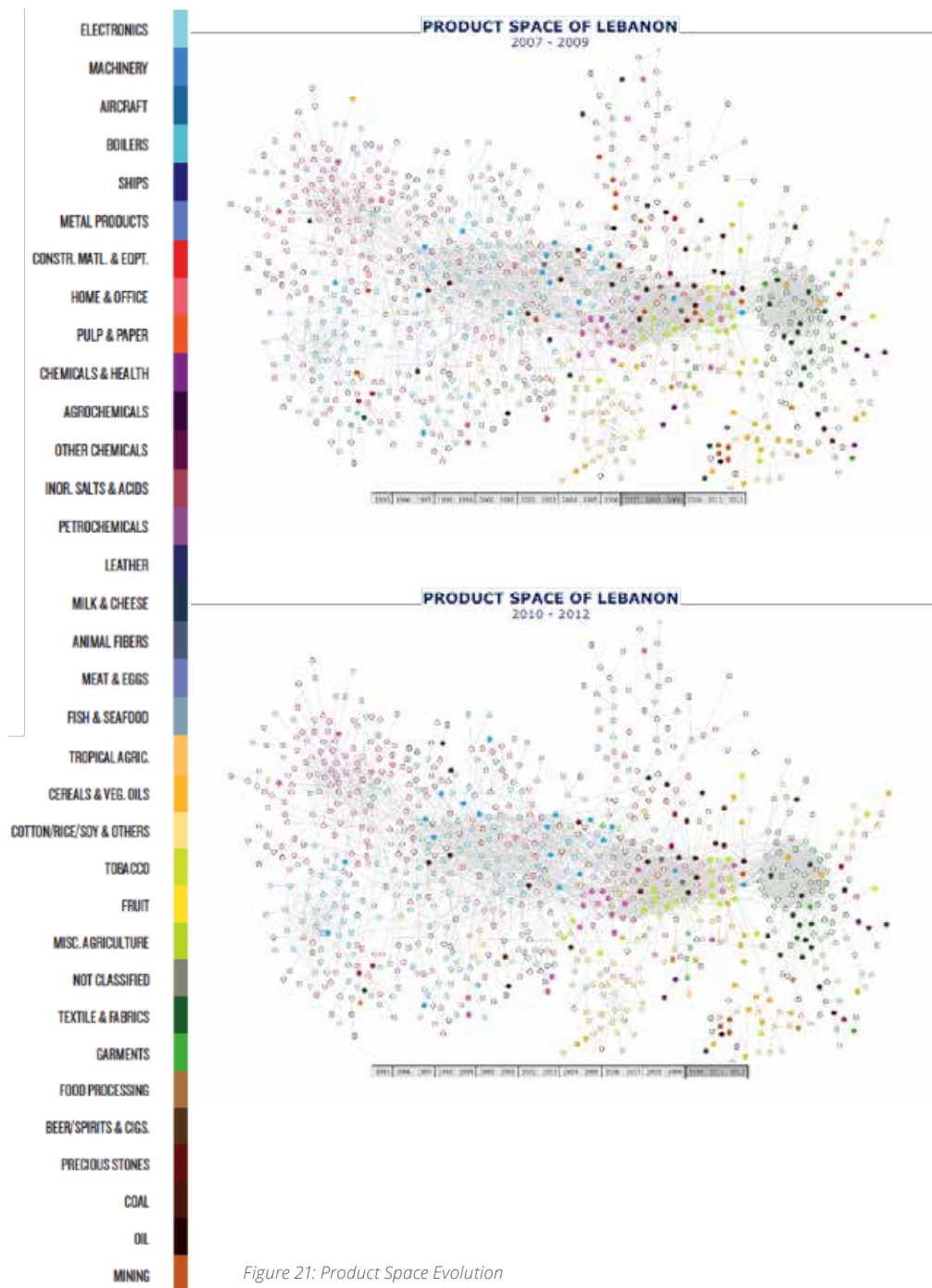


Figure 21: Product Space Evolution

A Mismatch in Demand and Supply of Capabilities

Limited understanding of future market requirements has led to a mismatch in human capital supply. Specifically, formal education and professional training remain traditional and focused on generalists and theoretical learning methods, while the technical formation of specialists and skilled workforce is weak (in quantity and quality) beyond a few sectors. This is apparent in the shortage of vocational programs and highly technical specializations, as well as in the gap between the skills of the new entrants to the labor force and the labor market needs.

3.2.2 Capital

The landscape of capital available for SMEs evolved significantly over the past fifteen years. The turn of the millennium was heavily geared towards debt financing, with a majority in the form of subsidized loans shouldered by the Lebanese government. The middle of the past decade witnessed the entry of a handful of mostly private sector equity investors, especially early stage venture capital. More recently, facilitators such as incubators and entrepreneurial support organizations reinforced the environment by acting as mediators and creating the links between SMEs and investors (*Figure 22*).

Looking further into the Lebanese track record, it should be noted that the volume of debt capital far outweighs institutional equity (<1% of the debt volume). Indeed, some equity investors faced challenges in sourcing quality deal flow to warrant their activity (e.g., Riyadh Enterprise Development, which targets growth SMEs, made a sole investment and recently wound down its operations in Lebanon), spurring the introduction of several incubators and accelerators. However, it is still early to gauge the success of these facilitators, with some of the most publically known still trying to find the optimal format to support startups.

From a transaction perspective, most equity investments were for seed/angel and early stage SMEs, with very limited activity in the PE and growth capital stages. While these investments targeted several sectors, most of the funded businesses had a significant ICT component in their value proposition (*Figure 23*).

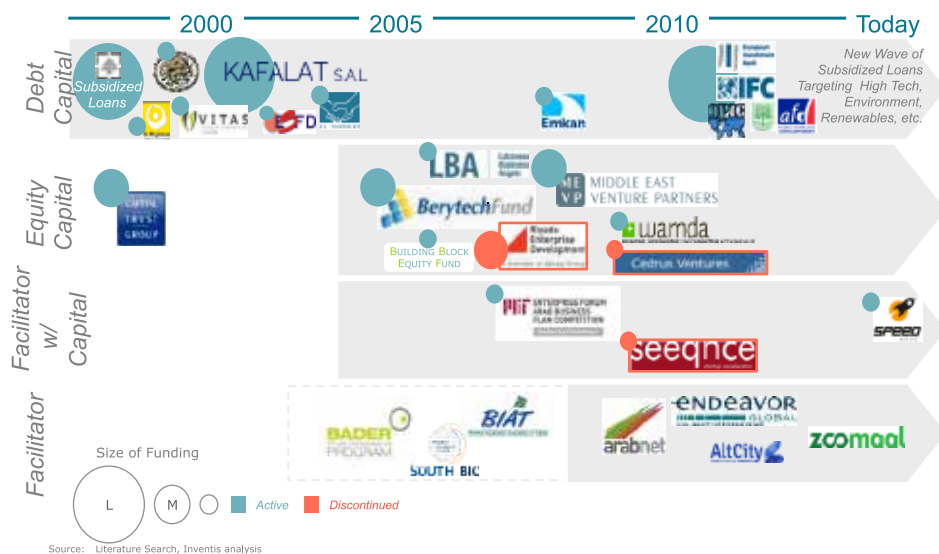


Figure 22: Evolution of Funding Landscape

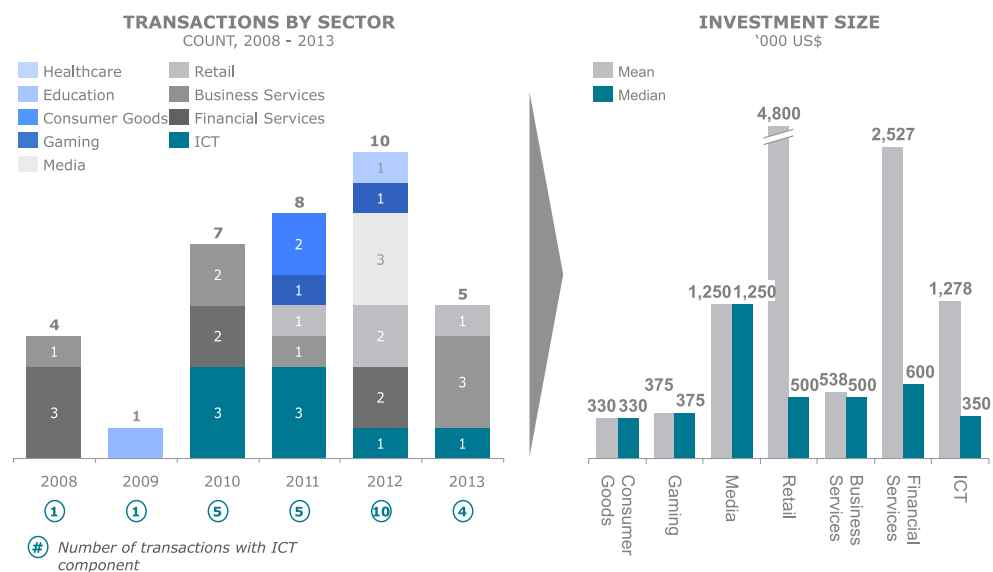


Figure 23: PE and VC Transactions in Lebanon ¹¹

¹¹ Zawya Private Equity Database, MEVP and Berytech websites, literature search, Inventis analysis

In this context, three dominant challenges for Lebanese SMEs transpire from the current situation.

Distorted Cost of Capital Leading to Weak Capital Bases

Considering typical sources of capital, a similar trend is seen across early stage entrepreneurs and more mature SMEs: both rely on significant proportions of debt capital to fund their businesses.

The former typically bootstrap their companies with personal savings and from family and friends, and rely on subsidized loans in lieu of equity. While in the latter case, SMEs rely heavily on short-term debt from banks (e.g., credit lines rolled-over annually) complemented with long-term shareholder loans which effectively are quasi equity.

Indeed, taxation policies (e.g., on dividends and capital increases) and government subsidies despite their benefit somehow distort real cost of capital and could have encouraged debt financing and shareholder loans at the expense of equity, especially in selected industries. This leads to weak capital bases unsuited for fledgling SMEs looking to grow their businesses.

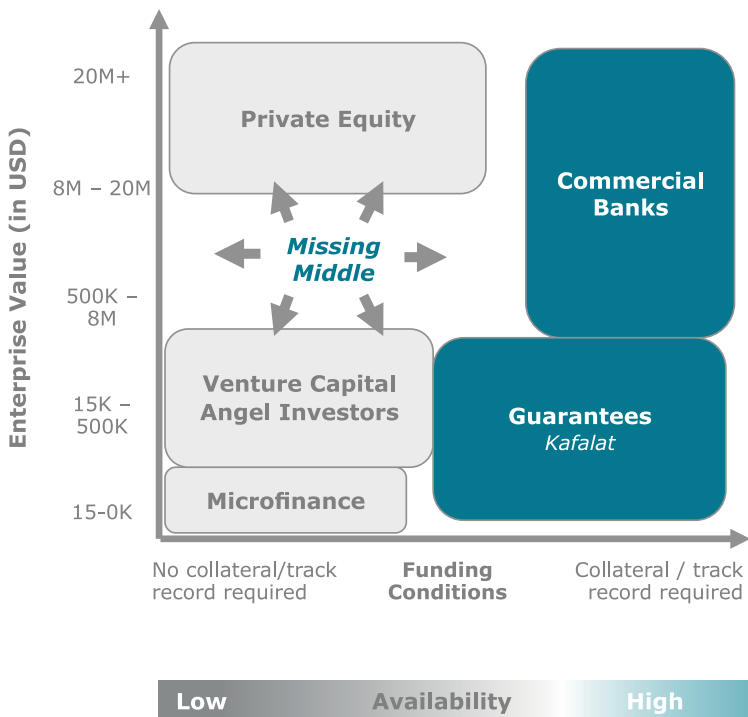


Figure 24: Missing Middle - The Gap in Supply-Demand for Capital

Capital Mismatch

Despite a globally recognized well-developed financial sector, Lebanon remains similar to the region's nascent funding landscape – a heavily debt driven market. Indeed, there is a clear mismatch in target, type and quantity of capital supply and demand from SMEs (*Figure 24*).

Today, commercial banks dominate the funding scene for mature SMEs with (costly) highly collateralized debt. At ~16% of the total loan portfolio, SME lending in Lebanon is among the highest in the MENA region, yet still half of the 30% target set by banks. Moreover, SME loans for investment purposes are still estimated at a 25-30% of the SME loan portfolio. Several challenges hinder banks from reaching their stated target including limited financial transparency coupled with weak credit coverage and creditor rights, improvements needed in SME management skills, and high collateral requirements. A partial solution has been made available with the introduction of Kafalat which pushed the boundaries of commercial lending to earlier stage enterprises (in selected industries) by reducing the risks taken by banks.

However, more suited early and growth-stage equity is still limited in volume and value. While funds increased both in volume and range of investment size, total dry powder is still meager compared to the demand in the economy (*Figure 25*). In August 2013, the central bank of Lebanon issued Circular 331 which attempts to address this issue. This new circular issued in August 2013 introduced new schemes to encourage the financing of startups, accelerators, and incubators through banks and financial institutions. Banks will be allowed to invest as much as 3 percent of their own funds in startup companies, accelerators, and VCs. Banks wishing to finance such companies will benefit from interest-free loans from the Central Bank, guaranteeing up to 75% of banks' investment for a maximum period of 7 years. While it is still too early to see results, this initiative may have significant potential for SMEs if managed by investment professionals.

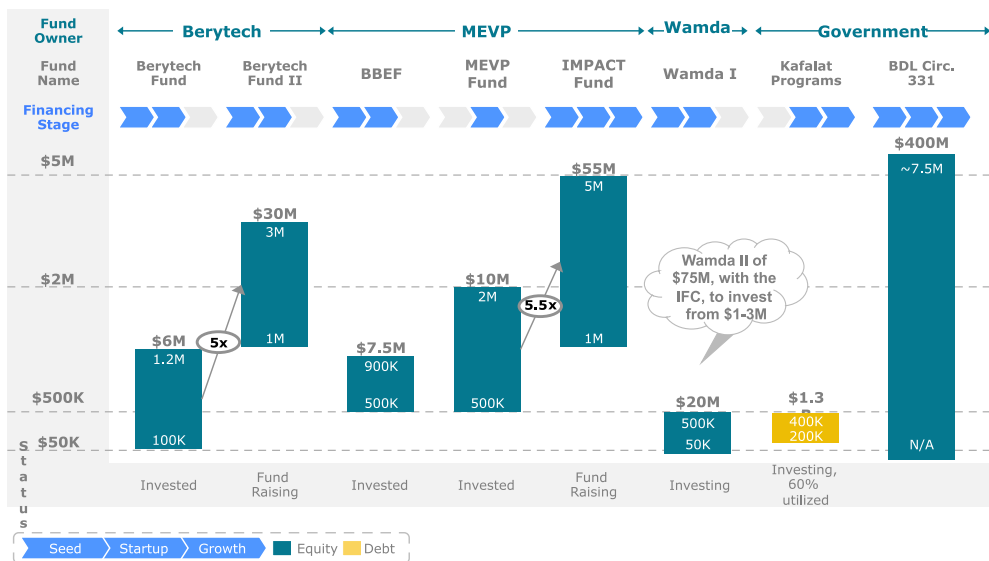


Figure 25: Sample of Equity Capital Evolution

Limited Appetite for Outside Investors

In the same vein as the cultural aspect of family control, some of the challenges faced by professional investment companies revolve around the fact that Lebanese SME owners have low appetite for “outsider” institutional / active investors and fear loss of control. Indeed, most companies prefer to maintain the business within their families, even at the expense of growth. This challenge is exacerbated by the limitations of financial instruments available for investors and owners, which, if made available, may overcome some of these constraints. For instance, except for banks, preferred shares and convertibles are not available to SMEs. Tools such as warrants and options or preferential terms can go a long way to mitigate some of the risks and apprehensions of both owners and investors, and as such, open the arena to more equity investment.

3.3. Industry Level

3.3.1 Market Structure

Lebanon is a small primarily consumer market dominated by services and trade and a high dependence on imports. Nominal GDP in 2012 reached US\$ 42.9 billion of which almost three quarters was in the tertiary sector (trade and services). Private consumption exceeded 75% compared to 52% and 64% for other Upper-Middle and Lower-Middle Income countries. Lastly, the import-export balance has been negative for the past years (*Figure 26*).

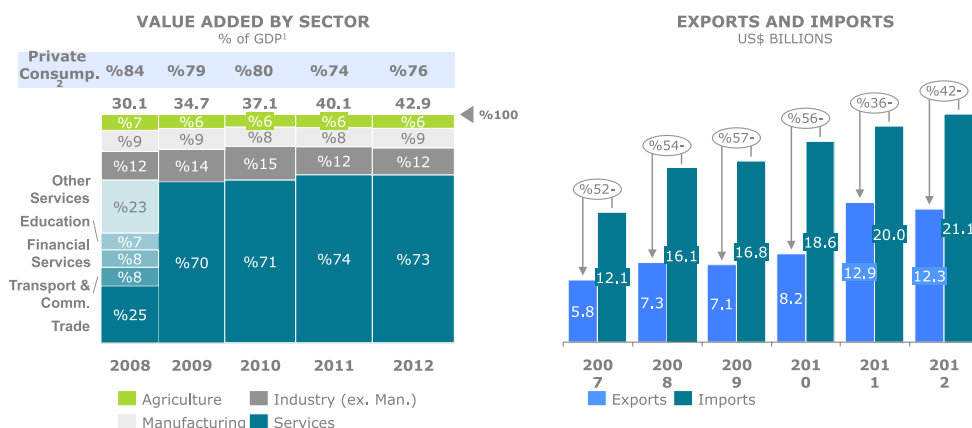


Figure 26: Sample of Equity Capital Evolution ¹²

This situation points to the fact that SMEs have to ultimately orient themselves to external markets and rely on global supply chains to conduct their business. To support them, some efforts are noted including:

- MoET's Internationalization Support initiative to subsidize participation of Lebanese firms in global fairs, and IDAL's support to Agricultural and ICT firms through its sponsorship of local producers in global fairs as well as its Agri Plus and Agro Map Programs
- The Qualeb project with the European Union to improve quality standards through trainings and workshops

More progress is required to support SME growth as they still face unlevelled playing fields and several trading inefficiencies.

¹² World Bank Database 2014, IMF: Lebanon real GDP Growth Analysis 2010

Unleveled Playing Field

Non-competitive structural challenges stemming from exclusive agencies, de-facto oligopolies and yet to be implemented antitrust laws and authorities are stifling the development of SMEs. Some 250 exclusive agencies protected by the 1967 commercial representation law limit the ability of SMEs to enter Lebanese markets where dominant competitors already hold an advantage. Moreover, Lebanon has been an observer of the WTO since 1999, with very little progress achieved in implementing the required reforms. Fortunately, a draft competition law, along with a dedicated national competition authority, has been proposed to ensure fair competition, prevent monopolies and exploitation of market dominance and anticompetitive practices. However, it has yet to be ratified and implemented.

Trading Inefficiencies

The relatively small local market and largely consumer economy has been a major driver for export and import activity. Despite this vital element of SME's value chains, trading remains a lengthy and tedious process – a fact that is especially felt by SMEs with their small organizations which do not have the depth and capacity to handle this complexity as compared to larger players. Indeed, Lebanon ranked 97 in the “trading across border” dimension of the 2014 Doing Business report by the World Bank.

More interestingly, since 2000, Lebanon has steadily grown its exports to the African continent to ~25-30% of total exports (almost US\$ 1 billion in 2013). Yet, in several of the African destinations, no trade agreements or double taxation treaties exist to further encourage such activity (*Figure 27*).

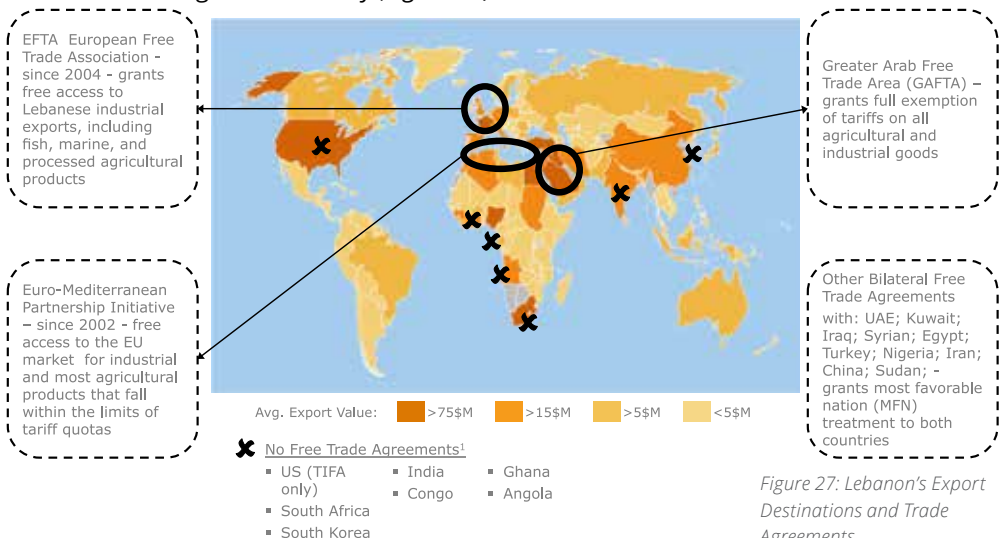
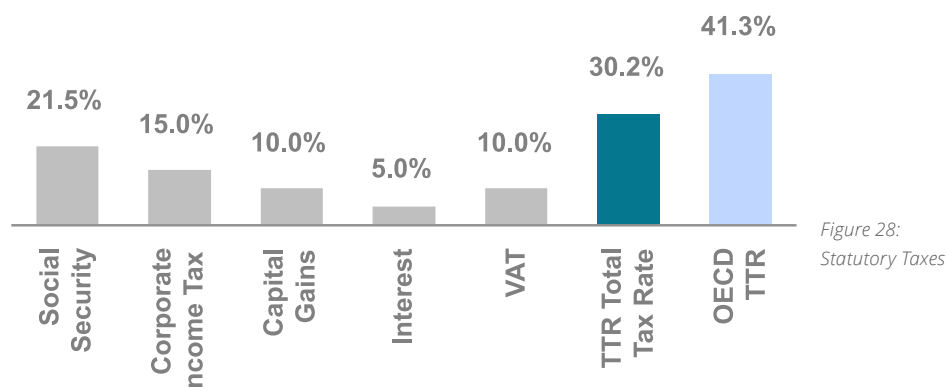


Figure 27: Lebanon's Export Destinations and Trade Agreements

3.3.2 Legal, Regulatory and Taxation

The Lebanese legal framework is based on civil law, inspired by the French system, with disputes typically resolved through a three-tiered court (first instance, appeal, and cassation). For SMEs, an efficient legal and judiciary system underpins business friendly environments by increasing trust, decreasing informal relationships and reducing risks between parties. However, Lebanon's judicial system is plagued by slowness, shortage of judges and inappropriate structures. Moreover, the legal framework has several critical laws that still require updating, are yet to be ratified, or are poorly enforced (e.g., competition law, code of commerce, insolvency law).

From a regulatory perspective, Lebanon's free market economy and strong laissez-faire tradition has set minimal restriction and safeguards, except for a few industries. Lastly, taxation is primarily fixed at a total tax rate of ~30% for all companies alike – including SMEs.



Given the government's strong ability to impact these areas, it is critical to improve the long-term sustainability and growth of SMEs, by addressing several of their inherent challenges:

Legal Enforcement vs. Contractual Goodwill

The inefficient judicial system results in costly and lengthy contract enforcement, especially for SMEs. With an average cost of ~30% of the claim and almost 2 year procedure, SMEs cannot afford to get entangled in legal pursuits to enforce their contracts' clauses thereby reducing their effective utility. To address this issue, the Lebanese Arbitration Center was established in 1995 to facilitate dispute resolution. More recently, efforts have been made to introduce private sector mediation (e.g., USJ,

Bank BEMO). However, neither of these avenues is sufficiently leveraged.

Weak Creditor Protection

According to the most recent Doing Business Report, resolving insolvency in Lebanon is a lengthy process (~3 years) and has poor recover rates (32.4 cents on the dollar). Indeed, current practices have neither protected business owners nor creditors effectively. A draft law to update the 1949 bankruptcy law is still pending approval. This has led to low rates of restructuring, high collateral requirements for SMEs and stifling of the overall economic cycle.

One-Size Fits All Taxation

The current tax and tariffs regime in Lebanon lacks sufficient differentiation for SMEs. Some regulatory fees and tariffs may be prohibitive for SMEs. The Lebanese government has developed tax incentives and exemptions for specific sectors/geographies (e.g., 6-10 years income tax breaks for rural industrials, draft law for tax reduction on profits of industrial exports of Lebanese origin). However, adoption and utilization of these incentives is still low, prompting further action by the government.

Persisting Red Tape

Lengthy and costly regulatory and setup processes are often marred by corruption and bureaucratic inefficiencies. For instance, obtaining a construction permit in Lebanon is costly relative to benchmarks and requires, on average, a lengthy 246 days to obtain. Whereas these shortfalls might not be significant to their larger competitors, given their small scale, SMEs can ill-afford these systemic deficiencies which cost them precious capital and time.

Companies in Perpetual Limbo

As in all economies, statistically some SMEs are bound to fail. However, in Lebanon, the enduring cultural stigma of failure is further aggravated by lengthy and costly processes to close a business. What remains is small teetering SMEs where entrepreneurs are stuck, instead of a more healthy system that allows these same entrepreneurs to learn

from their failures, shut down, and build new stronger enterprises.

3.3.3 Research and Innovation

Ranked 75th in the 2013 edition of the Global Innovation Index, Lebanon boasts a strong mix of human capital, academic and research institutions, as well as market and business sophistication. These key ingredients have the potential to truly catapult Lebanon into the highly coveted knowledge economy.

However, research and innovation in Lebanon lags its potential and is still under developed. Three main challenges seem to endure:

Untapped Innovation Potential

Despite an average of ~440 registered inventions or industrial designs submitted per year, innovation efficiency shows that Lebanon is performing below-par (*Figure 29*). The country has average innovation inputs (including research institutions, human capital, infrastructure), and a low yield in innovation outputs (quantity and quality of knowledge, technology and creative outputs) when compared to other Upper Middle Income countries.

Indeed, private higher education institutions (e.g., AUB, USJ), public entities and institutes (e.g., CNRS, LARI, IRI¹³) have small and limited budgets, despite some having highly regarded research facilities. This can be traced to the lack of long-term sponsors from either the private or the public sector, which leads to short-duration programs

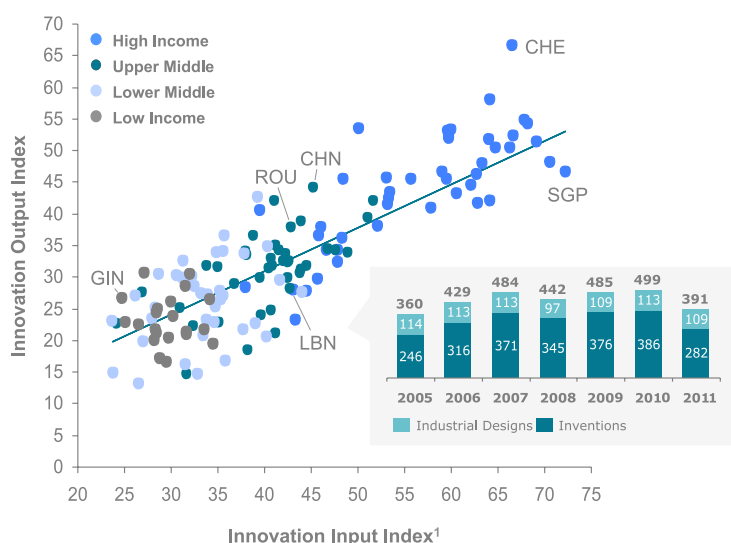


Figure 29: Innovation Efficiency & Patent Track Record

¹³ CNRS: Conseil National des Recherches Scientifiques; LARI: Lebanese Agricultural Research Institute; IRI: Industrial Research Institute

with limited impact and the persisting predominance of traditional industries.

Nascent IP Protection

The Patent Law (2000) and MoET Intellectual Property Protection Office (IPPO) are first steps towards improving Lebanon's intellectual property rights environment and enforcement. Yet, patent awards in Lebanon are based on a deposit system with limited examination, which significantly reduces the application worthiness.

This nascent intellectual property framework is creating disincentives for SMEs to develop new technologies and technical innovations in Lebanon, further anchoring the economy in traditional industries.

Poor Market Research

To compound the problem, SMEs face serious challenges in acquiring reliable, accurate and recent market information. Among others, the main sources for information on the Lebanese economy include the Central Administration of Statistics, the central bank, and a few other public and private institutions (mostly banks). Irregular and poor market intelligence, driven by the small budget allocations of these research and statistical institutions, has led to weak business planning for existing SMEs and poor market sizing for entrepreneurs.

3.4. National Level

The three main elements constituting the ecosystem at the national level were reviewed. From an Employment and Labor Law perspective, Lebanese SMEs benefit from a sizable labor force of ~1.6 million, relatively flexible hiring and firing practices with low redundancy costs equivalent to ~8.7 weeks of salary. Since 2012, minimum wages have increased to US\$ 450 per month. Addressing labor issues has been primarily driven by the public sector. For instance, the government has established an employment bureau, the National Employment Office, to match job seekers with enterprises. International organizations are also lending a helping hand, such as the IFC support in drafting new employment and foreign workers laws.

Turning to financial markets, several measures have been taken. The Beirut Stock Exchange was re-launched in 1996 with upgraded trading systems and support from the Bourse de Paris after a long hiatus during the civil war. To accompany this revival, a new Capital Market law was passed and a new Capital Market Authority was established in 2011. From an SME perspective, access to fresh capital to continue their evolution and growth has been encouraged by the government through tax incentives on dividends (50% reduction) and income tax breaks (2 years if 40% of shares are listed) when listing. Despite these efforts, Lebanese capital markets never really took off and remain largely nascent today.

Lastly, from an infrastructure perspective, several improvements were completed to key elements of the Lebanese infrastructure including the rehabilitation of Beirut's port and international airport, and the introduction of new generation mobile networks, albeit with significant delay to global deployments. Moreover, the government established several economic zones where it focused on particular aspects of infrastructure. For example, the recently launched Beirut Digital District is slated to be equipped with state of the art ICT infrastructure. Free Zones were set up in the vicinity of the ports of Beirut and Tripoli granting established enterprises direct access to this vital supply chain infrastructure. Nevertheless, beyond these sporadic patches, Lebanon still suffers from an overall poor infrastructure setup.

To allow SMEs to thrive, the government has a critical role to play to address some challenges in each of these elements.

Informal Workforce Market

With a perceived high total compensation cost (contributions to the National Social Security Fund amount to 21.5% of wages), SME owners tend to resort to freelance contracts, underreporting of employees, or other means to lower their fixed costs. The lack of SME-specific incentives for formal job creation has led to a sustained informal labor market.

Hurdles for Foreign Skilled Labor

Because of a protectionist policy, foreign workers¹⁴ face several restrictions on type of jobs and industries in which they can engage. Unlike many other countries which have sought to encourage the value-adding individuals, no special provisions for highly-skilled foreign labor as a method of transferring knowledge. Indeed, the process is cumbersome for SMEs and entrepreneurs to seek and hire highly skilled foreigners.

Shallow Capital Markets

At ~US\$ 11 billion capitalization, Lebanese equity capital markets are shallow and illiquid with very low trading volumes on the Beirut stock exchange. Despite aforementioned incentives and the low effective barriers to entry, no IPOs have been witnessed since 1999. In fact, the public stock market is essentially composed of the banking sector and Solidere (*Figure 30*). Among other reasons, the limited appetite of SME owners to list could be attributed to the lack of large institutional investors, and the unwillingness of family enterprises to lose control.

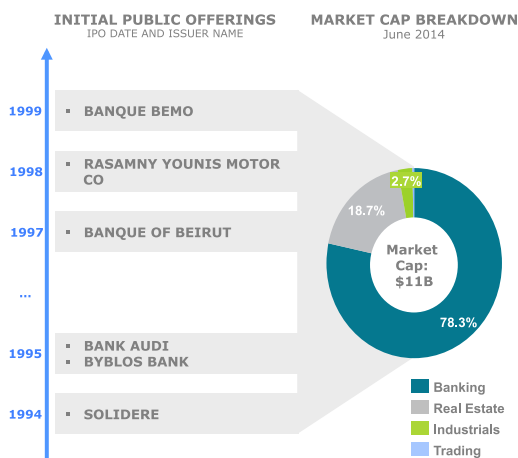


Figure 30: Beirut Stock Exchange Listing

¹⁴ Excludes domestic helpers who are exempt from the Code of Labor; foreign specialists fall under Memo # 99/2 (1999)

Infrastructure Patches

Poor infrastructure increases the costs of SMEs and their ability to operate across the Lebanese territory (poor quality of roads, costly and subpar ICT, challenges in supply of electricity, etc.). More importantly, the state of the development of the infrastructure reduces competitiveness of SMEs, especially when compared to neighboring Arab countries (*Figure 31*). While a complete infrastructure overhaul is beyond the capacity of the government's current tight budget, the adopted strategy of improving patches of infrastructure (free and economic zones) misses on the network effect that could be generated across the country.



Figure 31: Quality of Infrastructure 2013-2014

3.5. Overarching Perspective and Status of Support

The three main elements constituting the ecosystem at the national level were reviewed. From an Employment and Labor Law perspective, Lebanese SMEs benefit from a sizable labor force of ~1.6 million, relatively flexible hiring and firing practices with low redundancy costs equivalent to ~8.7 weeks of salary. Since 2012, minimum wages have increased to US\$ 450 per month. Addressing labor issues has been primarily driven by the public sector. For instance, the government has established an employment bureau, the National Employment Office, to match job seekers with enterprises. International organizations are also lending a helping hand, such as the IFC support in drafting new employment and foreign workers laws.

Beyond individual elements of the SME and entrepreneurial ecosystem, enterprises in Lebanon face today serious challenges that stem from the entire ecosystem in the current conjuncture.

The Growth Barrier

The combination of lack of cultural readiness to corporatize, limited penetration of equity funding, market inefficiencies and other elements have contributed to erecting a tremendous hurdle: today, most Lebanese SMEs face significant challenges in breaking the barriers of next stages of growth and a high risk of long-term sustainability, especially beyond 2nd generation for family businesses. As the statistics show, most remain micro and small enterprises.

A Lingering Old Economy

Limited leveraging of coordinated capability systems, at both the individual and organization levels, combined with meager research and innovation investment and efficiency have slowed the transition from the old traditional economy to the new “knowledge” economy – one based on higher value-adding differentiated capabilities that systemically build upon each other and have the potential to sustainably improve the global competitiveness of Lebanese SMEs.

Changing Business Environment

Lebanese SMEs operate in an ever more challenging business environment stemming from heavy competition from small and large rivals both locally and globally, empowered customers with more complex demands and minute profiles, hindering infrastructure, and fast-changing technologies disrupting existing business models.

Let alone the geopolitical context, Lebanese SMEs which are not nimble enough to morph with these changing demands are likely to wither over time.

Economic Uncertainty and Cash Stressing

The current economic uncertainty and the slowing of business activity have dimmed future prospects of SMEs. This situation, together with the current collateral-backed financing schemes available in the market, is severely stressing cash flows cycles and adding unenviable pressures on SMEs – pressures which are likely to halt the activity of otherwise successful SMEs that have operated for a long time and generated several employment opportunities.

Uncoordinated Institutional Setup and Initiative Inertia

Historically, the SME banner lacked a nationally recognized bearer. Multiple entities have made significant contributions to promote and develop these enterprises; however limited concerted efforts encompassing all stakeholders can be noted. This was due to the absence of an adequate institutional setup and coordination of SME support and development, compounded by limited reach and impact of initiatives, and rigidity in the face of an evolving landscape of needs.

3.5.1 Current State of SME and Entrepreneurial Support

Turning to support, over 100 private sector and some 45 public sector initiatives and programs have been identified and reviewed.

Of the public sector efforts, almost half are in the government's pipeline pending approvals and implementation. Ongoing initiatives have been noted to mainly focus on four key areas: legal and regulatory framework improvements, capabilities building, market structure development and access to capital. By design, these efforts target all of the territory and many of them cater for all sectors, with noticeable focus on Agriculture, Industry and ICT. Given the nature of public support, several of these initiatives tend to revolve around policies and laws that are meant to create the nurturing environment.

In contrast with the public sector, most of the private sector efforts were channeled in longer term active programs, with several NGOs taking prominent positions in delivering support directly to SMEs and entrepreneurs. The overwhelming majority has been focused on providing capital, developing capabilities and to some extent promoting the entrepreneurial culture.

While all support efforts are welcomed and needed, the difference between seed-to-early stage entrepreneurs and growth-to-maturity stage SMEs is stark (Figure 32). In line with the global hype around entrepreneurship in the past few years, most of the support efforts to date, both private and public, have focused on the developing new entrepreneurs and establishing new businesses. However, this should go hand-in-hand with ensuring that these businesses thrive in the longer term in order to preserve and indeed consummate the benefits of these young enterprises – hence, the need to further address the challenges of SMEs.

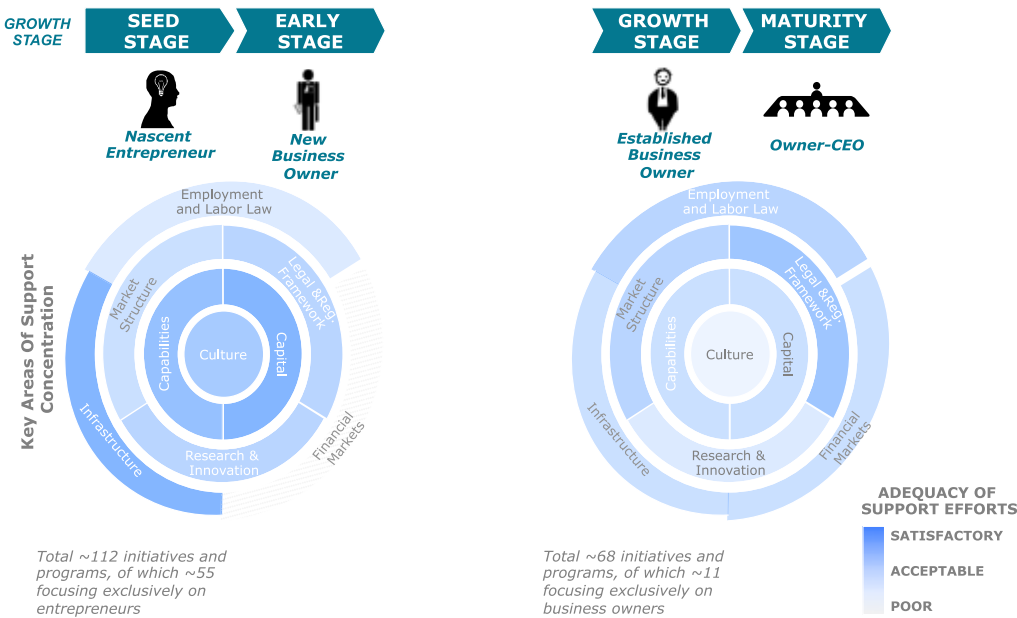


Figure 32: Areas of Support Concentration

04.

Proposed Way Forward: Lebanon's National SME Strategy

As noted in the assessment of the situation, SMEs in Lebanon face a variety of challenges and often have insufficient support across the various dimensions of the ecosystem and different stages of enterprise evolution. Putting things into perspective, while the overall efforts are commendable, the analysis (Figure 33) highlights few areas where support falls short of covering the challenges. These evolving gaps from entrepreneur to SME owner are still problematic and call for future focus of stakeholders.

Going forward, support efforts should continue to focus on the provision of capital, developing capabilities, and addressing the legal and regulatory framework, as well as research and innovation dimensions for start-ups and early stage companies.

As companies evolve into SMEs, these gaps effectively broaden across most of the ecosystem. Indeed, as SME owners experience greater challenges and yet have less available support. As such, increased attention should be given to SMEs, while maintaining the current level of support to early stage entrepreneurs.



Figure 33: Current Gaps in Challenges and Support for Entrepreneurs & SMEs

To address these gaps, a comprehensive end-to-end approach to SME support should be adopted to maximize effectiveness of the strategy. Moreover, while varying degrees of focus can be made to each element of the SME framework, a minimum working level should be ensured across all elements in order to improve likelihood of success. It is thus crucial to develop an end-to-end support of entrepreneurs and SME owners across different stages of evolution, ensuring adequate hand-over mechanisms between each stage:

- Individuals should be encouraged to embark on the entrepreneurial process;
- Entrepreneurs who develop ideas into concepts should be assisted in finding appropriate funding and setting up their businesses;
- Small business owners should be guided into the first steps and subsequent growth of their companies.

Furthermore, best practices reveal that concerted efforts and coordination is paramount to the success of any SME strategy, especially given the multitude of parties typically involved. As such a coordination mechanism should be in place with an overview over the entire process.

4.1 Vision, Mission and Objectives

Lebanon’s National SME Strategy is driven by an ambitious strategic vision of **“SMEs as key economic engine for growth and job creation”**. To achieve this vision, the strategy defines a mission for all stakeholders that calls for **“fostering the creation of vibrant and globally competitive SMEs that contribute to employment opportunities and high value-added economy”**.

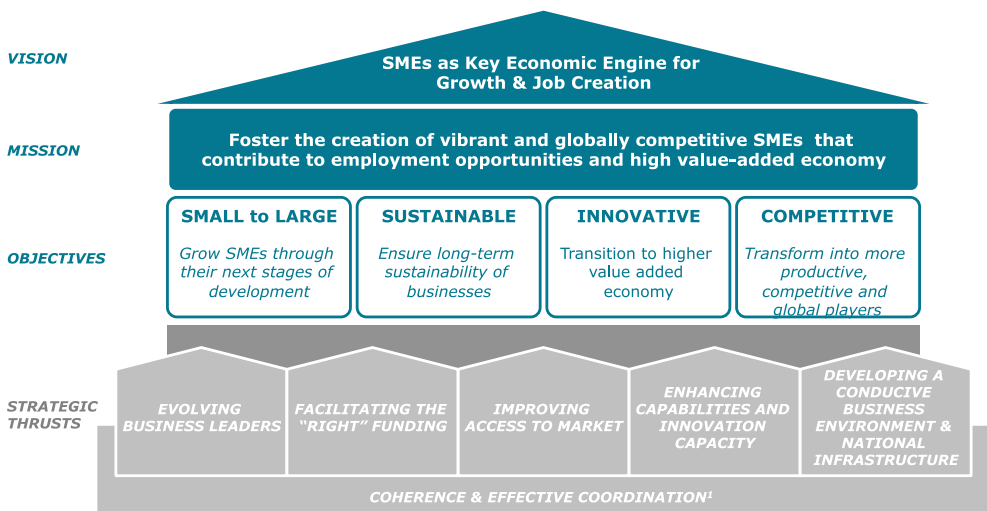


Figure 34: SME National Strategy Framework

The SME strategy (*Figure 34*) further identifies a clear set of strategic objectives that aim towards growing SMEs, enhancing their sustainability, and improving innovation and competitiveness.

A. SMALL to LARGE

The strategy should focus on initiatives that allow small companies to effectively overcome growth hurdles, including access to growth capital, corporatization, and access to markets in order to transition to larger businesses which create jobs and contribute to Lebanon's economic growth.

B. SUSTAINABLE

The strategy should ensure long-term sustainability of SMEs beyond their early entrepreneurial stages and original founders, and secure efficient market structures with levelled playing fields which allow SMEs to thrive.

C. INNOVATIVE

Building on Lebanon's highly educated and talented workforce, the strategy should aim at the transition to a higher value-added economy by fostering innovative and creative activities of SMEs, which create knowledge-based employment opportunities.

D. COMPETITIVE

The strategy should lead to the transformation of SMEs into truly global and agile players with higher productivity and improved resiliency, allowing them to compete effectively in the global economy.

4.2 Key Strategic Thrusts and Proposed Initiatives

Achieving these objectives rests upon six strategic thrusts¹⁵ that are effectively the pillars of Lebanon's National SME strategy:

- 1. Evolving Business Leaders**
- 2. Facilitating the “Right” Funding**
- 3. Improving Access to Markets**
- 4. Enhancing Capabilities and Innovation Capacity**
- 5. Developing a Conducive Business Environment and National Environment**
- 6. Ensuring Coherence and Effective Coordination**

These strategic thrusts are each further divided into a set of initiatives which collectively constitute the strategy. Each strategic thrust and related initiatives are described below. It should be noted that the initiatives are the result of the aggregation and rationalization of initiatives previously collected by MoET, or identified during the baseline of Lebanon's SME support ecosystem, as well as successful initiatives seen during the benchmarking analysis.

1. Evolving Business Leaders

The first strategic thrust aims at assisting SME owner-managers in evolving their corporate culture, professionalizing management, developing new leaders, and transitioning to real effective corporate governance. Five initiatives were identified:

1.1 Develop Mentorship Networks

Match promising high-growth potential SMEs with mentors from a local network of successful CEOs who can counsel the entrepreneurs, provide locally relevant advice, impart best practices and introduce them to SMEs local business network.

1.2 Launch Entrepreneurship & Family Business Center at the Lebanese University

Establish in the Lebanese University, the educational institution with the largest graduate student class every year, a center for Entrepreneurship and Family Business

¹⁵ Strategic thrusts are the high-level actions or broad drivers that summarize families of initiatives

studies similar to ones in the American University of Beirut and the Lebanese American University in order to develop emerging entrepreneurs and train future CEOs of family businesses; establish linkages between the Entrepreneurship & Family Business Center and the regional BDCs to help SME development post-graduation and provide feedback to curricula.

1.3 Provide National Recognition for SME Role Models

On an annual basis, identify and award top performing SMEs recognizing the important aspects through a clearly defined set of criteria (e.g., job creation, value added, capital structure, corporate governance, innovation, international footprint, etc.); develop a broad-based campaign to increase awareness and ensure top-level recognition (e.g., President or Prime Minister).

1.4 Develop a Second-Launch Restructuring Program

Assist in the restructuring and re-launching of SMEs in financial distress (e.g., cash crunch, late payments) to improve the viability of companies, and protect jobs; create an awareness campaign to help eliminate cultural taboos linked to failure or restructuring. Initiative in conjunction with insolvency law (initiative 5.3)

1.5 Establish Women-Friendly Business Environment

Support development of women-led businesses through dedicated and supportive policies and incentives, specialized training, women-to-women support networks and mentors, and backing of private sector initiatives and donors (e.g., WE Initiative, IFC).

2. Facilitating the “Right” Funding

The second strategic thrust aims at encouraging SMEs to strengthen their capital structures for growth and resiliency, ensure availability of adequate sources of funding adapted to SME needs and provide a supporting framework to match smart VC/PE capital to entrepreneurs and business owners.

2.1 Attract Top-Tier VC/PE Firms and Angel Investors

Encourage the entry of top-tier international firms and professional investors by providing them with anchor funding (e.g., by leveraging BDL Circular 331) and facilitating their partnership with local players with a healthy pipeline; seek to transfer their equity investment know-how, advanced value creation plays and access to an international network of partners, suppliers and clients.

2.2 Broaden BDL Circular 331

Expand the scope of BDL's Circular 33116 to allow equity funding targeting a broader range of sectors based on Lebanon's economic priorities and revise investment delivery mechanism to strengthen the participation of investment professionals accustomed to equity risk.

2.3 Improve Access to Debt Capital

Reduce collateral requirements (cash and immovable assets) by introducing the draft Secured Lending law (i.e., new registry for moveable assets) and improving financial reporting and transparency; facilitate new alternative financing tools including cash-flow based financing, mezzanine debt.

2.4 Introduce SME Exchange and Enhance Crowd Funding

Provide SMEs with the ability to tap into new sources of equity funding by establishing an SME-dedicated stock exchange with simplified listing procedures and easier requirements; enhance crowd funding programs for startups by adapting legislation to international standards and practices (e.g., reviewing limits for investment and fund raising) in order to avoid the flight of SMEs to other friendlier geographies; encourage the setup of a limited number of players only to ensure their success.

2.5 Launch iSME Project

Review and update iSME Project criteria to reflect recent changes in business environment (e.g., Circular 331) and approve law to initiate funding to innovative Startups & SMEs.

3. Improving Access to Market

The third strategic thrust aims at minimizing structural market inefficiencies to improve SME competitiveness, enhancing access to foreign markets and in particular to fast-growing economies and ones where Lebanon has an edge.

3.1 Bridge SMEs to Large Enterprises and Multinationals

Facilitate commercial connections between large purchasers (e.g., government, MNCs) and SMEs. Design and implement schemes and mechanisms including business directories, "meet-the-buyer" events, portals, etc. to help establish these links. Help SMEs identify opportunities, understand purchaser requirements, negotiate capacity

and skills, and overcome their eligibility shortcomings through adequate support including advisory services, training, etc.

3.2 Leverage the Global Lebanese Economic and Diplomatic Network

Leverage Lebanese missions abroad (embassies, consulates, etc.) to draw on voluntary commitments of influential Lebanese in the diaspora and individuals connected abroad to help SMEs achieve growth by leveraging their skills, influence, connections and market intelligence. Facilitate the linkages between SMEs and these individuals; systematically aggregate and manage the intelligence and collected information in a structured repository and provide easy access to SMEs (e.g., US Commercial Service buyusa.gov)

3.3 Activate the Lebanese Export Promotion Agency (LEBEX)

Offer customized assistance to pre-export SMEs and high-potential startups and support in ramping up exports rapidly through promotion and support activities of LEBEX (e.g., trade fairs); provide access to export-ready SMEs to a comprehensive support menu which among others include easy access to export/import finance and insurance, linkage to market expertise and buyers (initiative 3.1), and compliance to standards (initiative 3.4) to expedite internationalization of local services and products.

3.4 Improve Market Competitiveness

Ratify Competition Law and expand its scope to promote SME interests; set up procedures and mechanisms (e.g., competition authority) to ensure public awareness, clarity, transparency and non-discrimination to SMEs (including anti-competitive practices).

3.5 Enhance Standards of SME Products and Services

Improve market standards to meet international criteria and grow trade volumes through the provision of professional training and information (e.g., leveraging the Qualeb program) and enhanced national certification system (SME friendly) in order to implement product quality standards and ensure SME compliance to international standards.

3.6 Strengthen Relationships with New Top Trading Partners

Link Lebanon to new top-trading partners and growth economies (e.g., emerging economies in Africa) through free trade agreements and double taxation treaties in

order to facilitate SME access to these markets and augment current trade volume; review and upgrade Lebanon's participation in existing trade agreements with special consideration to SMEs.

4. Enhancing Capabilities & Innovation Capacity

The fourth strategic thrust is to build Lebanon's core specialized capabilities, to enhance its creative and innovation capacity and to develop supporting framework as well as interdependent networks that build upon Lebanon's differentiated capabilities found in both individuals and organizations.

4.1 Develop Competitive Capabilities Clusters

Develop and foster clusters of companies – SMEs and large – whose edge stems from Lebanon's differentiated high value-added capabilities; secure required structural enablers (including supporting infrastructure, business services, etc.) by developing, retargeting, transforming and expanding existing and new economic zones and ensuring linkages to academia, training and R&D centers.

4.2 Repatriate Lebanese Expat Success Stories

Target Lebanese expats with successful businesses abroad and incentivize them either to relocate /open branches in Lebanon or to establish joint ventures with local SMEs. Establish and promote preferential policies based on provision of superior know-how (e.g., these could include priority treatment with IDAL, targeted tax holidays, etc.).

4.3 Assist SME's Technology Upgrade

Assist SMEs in identifying technology requirements (e.g., management and financial systems, automation, e- and m-services and business) through free or subsidized expert advisory services and provide them with access to attractive financing (e.g., new Kafalat program) and other incentives (e.g., tax credits for selected capital expenditures) for technology upgrades in order to enhance their competitiveness.

4.4 Introduce Apprenticeship Programs

Introduce formal apprenticeship programs ending with certifications (and potential job opportunities) that will improve the supply of skills that match market needs and ensure the effective transfer the large business know-how to smaller enterprises.

4.5 Expand Vocational and Training Programs to Meet Market Needs

Adapt vocational and formal training programs to new capabilities' requirements and encourage BDCs, chambers of commerce, incubators, universities and training providers to increase capacity and footprint; provide accreditation to high impact programs.

4.6 Provide Incentives for Employee Training

Assist SMEs in upgrading their human capital capabilities and skills by providing incentives (e.g., tax credits, vouchers, etc.) for targeted trainings; ensure quality of training providers through improved accreditation with the relevant authorities, and "train the trainer" programs.

4.7 Establish a Commercialization Office

Setup a Technology and Creative Commercialization Office (could be in a public-private partnership or, funded and operated entirely by the private sector) to assist Lebanese creators and inventors with high potential in effectively transforming their intellectual property/creations into viable commercial products/services; link the commercialization office to relevant institutions (e.g., universities and research centers) and trade/interest groups (e.g., design and creative guilds, etc.).

4.8 Link Industry to Academia with Innovation Vouchers

Establish linkages between industry SMEs and universities or other research centers to help target research on commercially relevant areas; reallocate portions of R&D budgets of public agencies and donors to SME benefit by providing innovation vouchers redeemable by SMEs to conduct R&D with participating entities (similar to Singapore's Spring program).

4.9 Optimize R&D Spending On Core Sectors

Optimize and refocus budgets (governmental, international donors, etc.) in Research & Development to further develop the SME capabilities in Lebanon's key core sectors that help create a competitive advantage for Lebanon; promote tighter partnership between academia, public sector and industry to ensure common priorities and maximize the benefit of the limited budgets of R&D.

4.10 Introduce R&D Expenditure Tax Credit

Provide incentives for Startups and SMEs (in addition to industry in general) to invest in R&D by introducing tailored tax credits and tariff breaks; update current proposed draft law to extend coverage to all sectors and lobby for its ratification.

4.11 Assist SMEs in Cleaner Production and Resource Efficiency

Expand the support and assistance provided for SMEs by the Lebanese Cleaner Production Center LCPC at the Industrial Research institute to achieve green economy and sustainable development

5. Developing a Conducive Business Environment & National Infrastructure

The fifth strategic thrust is to address SME-critical elements of Lebanon's business environment focusing on developing SME-friendly employment, legal, regulatory and taxation frameworks, as well as concentrate infrastructure development efforts into coherent and comprehensive sector-focused zones.

5.1 Twin IPPO with an International Counterpart

Twin MoET's IPPO with leading international IP offices to upgrade Lebanon's current Intellectual Property Rights framework, introduce best practices, and enhance the quality and protection of inventions and creations in local and international markets.

5.2 Upgrade IP Framework and Patenting Process

Upgrade IP Framework and enforcement of IP rights by introducing examination stages to current registration process, reducing filing costs for SMEs, adapting the judicial system required for its proper functioning, and accelerating the ratification of relevant laws (Copyrights, e-Transaction, Trademarks, etc.); create awareness about the revised system and the benefits of IP rights to SMEs.

Update, Ratify, and Implement Pending Laws

Introduce or revise legislation, requiring drafting, approval by cabinet and submission to parliament; specifically:

5.3 Code of Commerce:

Ratify updates to Code of Commerce in order to protect potential investors; introduce related laws (e.g., GDR, M&A, preferred shares) and establish proposed simplified legal structures (e.g., SAS1).

5.4 Insolvency Law

Update law to enhance investors' protection; allow firms to close operations efficiently, and viable firms to reorganize operations and restructure debt; publish out-of-court workouts guidelines.

5.5 Public Procurement Law

Endorse the draft public procurement law by parliament to pave the way for the adoption of the necessary measures to support SMEs, and establish a transparent process in which a quota is set to encourage and allow SMEs participation; ensure compliance with law.

5.6 Domestic and Foreign Investment Law

Update law to attract foreign investment in local SMEs; and reflect changes to the business environment.

5.7 Labor Law

Update Code of Labor to formalize hiring of partial and seasonal employees to allow SMEs to adapt their workforce to business requirements; clearly distinguish between skill levels of hires.

5.8 Adapt Judicial System to Meet SME Requirements

Reduce duration and costs of court procedures by providing SME-specific trainings to judges and court staff, increasing capacity, and adapting and simplifying processes and procedures for SMEs; encourage the increased usage of arbitration and mediation as alternative methods for conflict resolution.

5.9 Attract and Facilitate Access to Skilled Labor

Facilitate the recruitment of highly skilled foreign labor through special visas and work permits (e.g., similar to the UK's program); incentivize skilled Lebanese middle management expats to return by introducing a tax holiday to eligible applicants.

5.10 Launch a Job Matching Program

Expand upon New Entrants to Work (NEW) program and setup a 'match-maker' between institutions of higher education and SMEs to better adapt supply-demand of anticipated labor force and provide matching services for job seekers and SMEs.

5.11 Develop Government E-Services

Introduce simplified e-government services and administrative procedures (taxes, registration, commercial register, etc.) for SMES in order to eliminate enduring red tape via straightforward online applications and registration processes, and reduced duplication between different authorities; potentially integrate on Entrepreneurs and SME portals.

6. Ensuring Coherence & Effective Coordination

The sixth strategic thrust aims at developing strong effective coordination mechanisms among public and private sector stakeholders in order to ensure coherence and streamlining of SME support efforts.

6.1 Focus All Efforts on an Industry / City

On a rolling basis, direct all public and private sector support efforts to SMEs of a specific city/ industry for a finite term (e.g., one year) to enhance the SME ecosystem enablers and ensure end-to-end support mechanisms that improve success rates of entrepreneurs and SMEs.

6.2 Establish Regional “SME Malls”

Establish a set of regional centers (e.g., 1 or 2 in each Mohafaza) that aggregate SME and business support services offered by multiple providers in one easily accessible location (including banks, legal advisors, consultants, procedure facilitators, etc.); potentially leverage existing BDCs as nucleus of malls.

6.3 Set Up an SME Observatory

Establish an entity, the SME Observatory, tasked to regularly conduct and publish research (e.g., updating this report), statistical and impact analysis on SMEs and support entities, and maintain a comprehensive database to ensure continuous and effective monitoring of support to SMEs; comply with research requirements of local and international SME initiatives, associations and organizations in which Lebanon participates (e.g., Euro Mediterranean Charter for Enterprise)

6.4 Create/Upgrade a Full Fledged portal for Entrepreneurs and SMEs

Create/Upgrade a Full Fledged portal for Entrepreneurs and SMEs including updated directories, support tools, customized trainings, and e-government services, etc.

4.3 Setting the Institutional and Governance Framework

The assessment of previous efforts to support SMEs in Lebanon highlighted the lack of a national champion that provides strategic direction and support, coordinates, and streamlines ongoing efforts in the Lebanese SME ecosystem. Multiple agencies, including MoET, other sectorial ministries, BDL, Kafalat and IDAL, besides multilateral organizations, NGOs and private sectors, work mostly in isolation, putting efforts and resources to support SMEs with risks of overlap and, in most cases, limited coordination amongst them. As a result, many programs have fallen short of their full potential in supporting SMEs and in creating the necessary impact at the required scale. It is thus necessary to setup a robust institutional framework with strong governance and effective leadership in order to ensure efficient execution of the new SME strategy.

International benchmarks show different alternatives of institutional setups (*Figure 35*). Some countries, such as USA, UK and New Zealand, have established ministries dedicated to SMEs, while others have setup departments within ministries or created independent agencies that coordinate efforts between public and private sector. Certain countries, like the Philippines and Malaysia, have set up dedicated development boards that develop strategies and oversee the execution through a dedicated team.








							
Governance	Reports to Ministry of Trade & Industry	Reports to Prime Minister	Reports to Ex. Council / Dept. of Eco. Development	Reports to Federal Government	Reports to Prime Minister	Reports to Department of Trade & Industry	Reports to Prime Minister
Management	SPRING BoD ¹	Ministry of Business, Innovation & Employment ²	BoD ¹ of Khalifa Fund / Dubai SME	Small Business Administration (SBA)	Department of Business Innovation & Skills	MSMEs Development Council	National SME Development Council
Sample Execution	<ul style="list-style-type: none"> Productivity and Innovation Credit Scheme Market Readiness Assistance (MRA) Grant SME Talent Program 	<ul style="list-style-type: none"> Innovation Capability Funding Business Mentorship Incubator Support Program Job Placement Support 	<ul style="list-style-type: none"> UAE SME Fund Khutwa Microfinance Zeyada Program MBR Award For Young Business Leaders Dubai SME 100 SME Connect Dubai Entrep. Academy 	<ul style="list-style-type: none"> Historically underutilized Business Zones program Women-Owned Small Business Federal Contract program 	<ul style="list-style-type: none"> Regional Growth Fund Local Enterprise Partnerships Growth Accelerator Start-up Loans Enterprise Finance Guarantee 	<ul style="list-style-type: none"> Small Business Corporation Access of Small Enterprises to Sound Lending Opportunity One Town One Product Program 	<ul style="list-style-type: none"> SMEINFO portal; providing support on infrastructure, financing, advisory services, access to market, technology, & Human Capital Various development objectives tasked to public entities

Figure 35: Select Institutional Setup Benchmarks

The global benchmarking analysis shows three possible models for Lebanon's institutional setup (*Figure 36*):

- An independent authority, similar to IDAL
- A dedicated/standalone ministry or a general directorate as an extension of an existing one (similar to the General Directorate of Cereals and Sugar Beets within MoET)
- A development board or council, similar to the Higher Council for Privatization

In the case of Lebanon, establishing a General Directorate under the Ministry of Economy and Trade (MoET) or setting up a Development Board under the Presidency of the Council of Ministers (PCM) seem to be the more viable options. The former is easy to setup and can benefit from existing resources of the ministry; however it will require new legislation and may be hindered by the risk of limited coordination with other ministries. The latter cuts across all sectors and provides high-level positioning and visibility that allow for effective coordination and involvement of various private and public stakeholders; however, it will require the allocation of new resources and capabilities and necessitates strong coordination mechanisms that allow it the enforcement of the strategy.



Figure 36: Institutional Setup Models

In both cases, establishing a public-private SME Board chaired by the Prime Minister is recommended. The SME board will be complemented with the General Secretariat, an executive arm responsible for the execution of the strategy. The General Secretariat can be either within the PCM or under MoET (*Figure 37*). If within MoET and after the law is approved, the General Secretariat would then transition into a General Directorate under MoET, while keeping the SME Board under PCM to continue providing the ministry with effective advice and feedback on the effectiveness of the strategy.

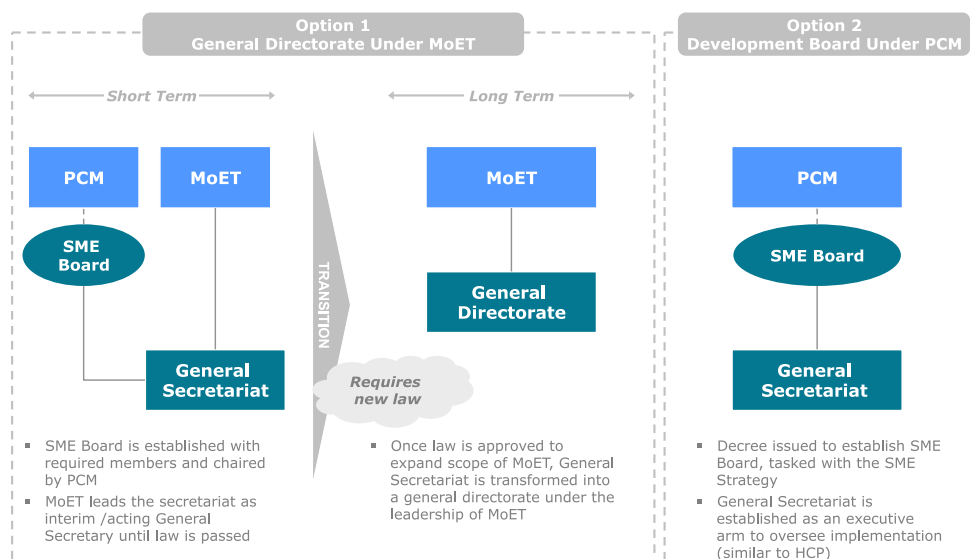


Figure 37: Proposed Institutional Setup Options

4.3.1 SME Board Setup

The SME Board under the Presidency of the Council of Ministers will drive the SME National Strategy with the triple mandate of being the National Strategy Champion, Support Efforts Coordinator and SME Advocate.

As National Strategy Champion, the Board will formulate and set the strategic framework (vision, mission and objectives) for SME development, approve major decisions (e.g., launch of new programs), and oversee achievements of agreed objectives. In addition, the Board will monitor performance of SME contribution to the economy (e.g., GDP and high-value employment).

As Support Efforts Coordinator, the Board will coordinate Inter-Ministerial and Agency efforts, including those from the private sector and NGOs and ensure government and public sector entities and their activities are aligned to SME interests.

Lastly, as SMEs Advocate, the Board will promote and advocate the case of SMEs and related matters locally and internationally.

Board Composition

The SME Board should represent both public and private sectors. It will be chaired by the Prime Minister and Co-Vice Chaired by the Minister of Economy and Trade and a high-level representative from the private sector. It shall be comprised of 12-15 members representing the different sectorial ministries and IDAL, along with broad representation from the private sector (*Figure 38*). These members will be approved and appointed by the government, through a Council of Ministers resolution.

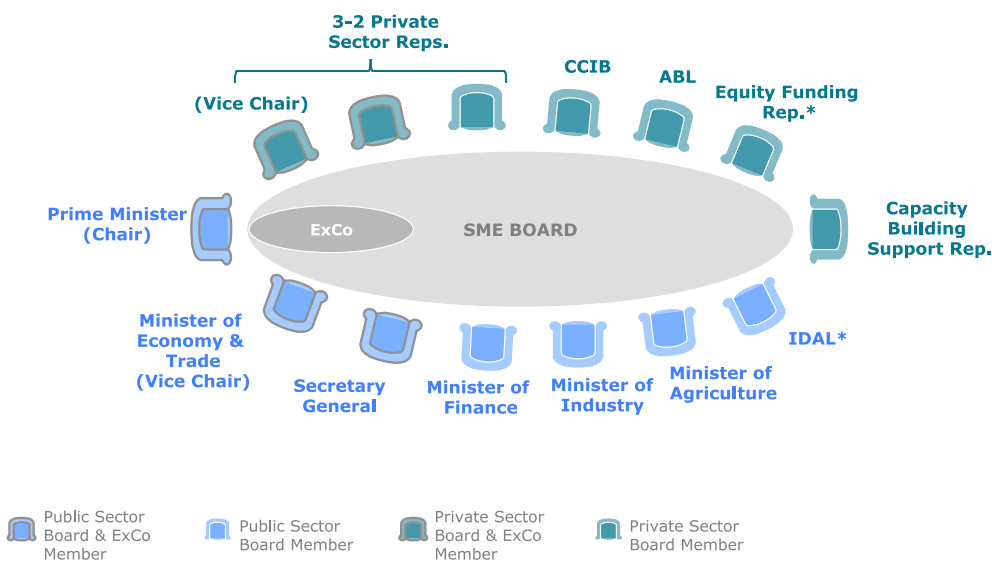


Figure 38: Proposed SME Board and Executive Committee Composition

Board Modus Operandi

The SME Board will act as a supervisory board, in charge of overseeing activities related to the SME support; it coordinates programs and liaises with public and private entities to address the SME challenges. It can appoint committees and task forces dedicated to specific issues (e.g., access to finance). Due to its broad and high-level representation, quorum is not required for meetings to take place, unless there are important decisions to be made. However, balanced representation of both the public and private sector should be ensured at all times.

The Board shall meet on a quarterly basis or upon the request of the Chair. The sessions will be moderated by the Secretary General who acts as the Board Secretary. The Chair presides over meetings and approves agenda.

Executive Committee

The SME Board will also be supported by an Executive Committee of 5 members, 2 of which from the private sector representation, including both Vice-Chairs (*Figure 38*). The Executive Committee will be chaired by the Prime Minister, who could delegate chairmanship to the Vice-Chairs. It will act on behalf of the Board in between meetings, ensuing acts and decisions are later presented for full board review. In addition, the Executive Committee will ensure oversight on the General Secretariat (SG) and provide guidance to its members in performing their responsibilities. The Executive Committee shall meet on a monthly basis or upon request of the Chair.

4.3.2 SME General Secretariat Setup

The General Secretariat under the supervision of the SME Board will lead the implementation of the SME National Strategy along its three mandates as National Strategy Champion, Support Efforts Coordinator and SMEs Advocate.

As **National Strategy Champion**, the General Secretariat will detail the objectives set by the SME Board into strategic thrusts and identify required initiatives. In coordination with the executing parties, the Secretariat will explore, develop, launch and monitor programs to deliver the goals of the initiatives and to help achieve objectives.

As **Support Efforts Coordinator**, the General Secretariat, on behalf of the SME Board, will supervise and coordinate support efforts by public and private providers, measure performance and track progress of support initiatives, and identify synergies among initiatives to streamline efforts.

Lastly, as **SMEs Advocate**, the General Secretariat will act as go-to public entity for SME-related matters, maintain statistics on SMEs in Lebanon (e.g., size, location, birth rate, etc.), issue regular publications and promote SME interests in public venues.

The General Secretariat will be organized into three units (*Figure 39*):

- A Strategy Performance Unit responsible for developing strategies, monitoring performance against implementation of strategy and for maintaining SME-related statistics;
- A Program Development and Delivery Unit organized by strategic thrust to oversee execution of initiatives and coordination with different entities, and;
- An Enterprise Handling Unit responsible for interactions with startups and SMEs, whose teams are organized by region in order to be physically close to the recipients of the support and the executing entities.

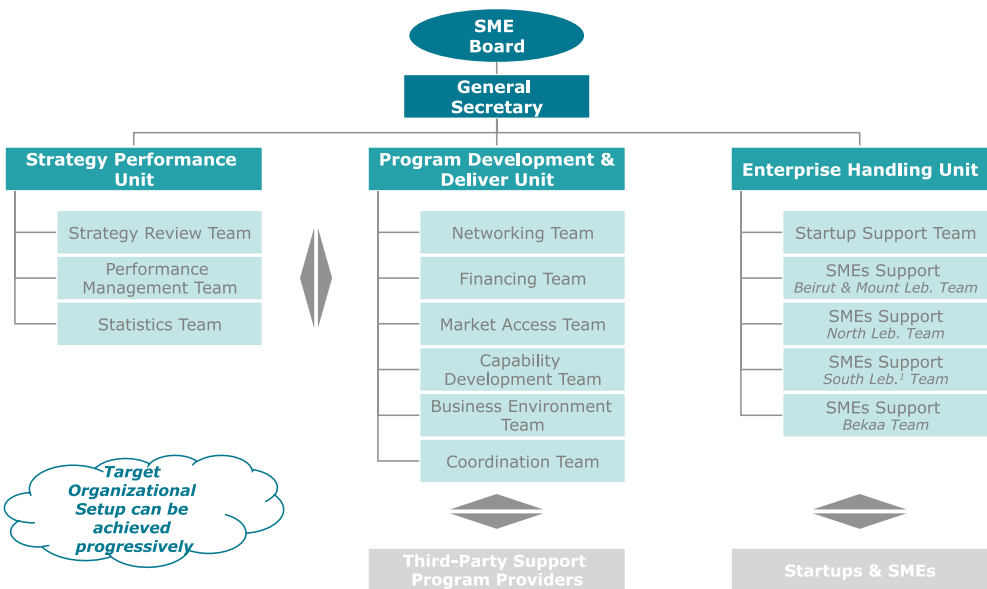


Figure 39: Secretariat Organization Structure

To ensure effective implementation of strategic thrusts and coordination with other entities involved in SME development, the General Secretariat need to appoint and work with champions who effectively become focal points of contact on every strategic thrust (*Figure 40*). Each champion will coordinate with the Secretariat and expand or update its mandate to further support SMEs.

	Strategic Thrusts	Proposed Champion	Rationale
1	Evolving Business Leaders	Consortium of NGOs, Universities, & Chambers	<ul style="list-style-type: none"> Develop business leaders capable of both carrying SMEs to their next wave of growth & adapting to a changing business environment
2	Facilitating the “Right” Funding	Kafalat & BDL	<ul style="list-style-type: none"> Ensure availability of adequate & diverse sources of funding and raise awareness of SMEs on alternatives & suitability
3	Improving Access to Market	MoET & IDAL	<ul style="list-style-type: none"> Ensure fair competition in local market and enhance access to foreign markets
4	Enhancing Capabilities and Innovation Capacity	Business Development Centers	<ul style="list-style-type: none"> Foster provision of effective capability-building efforts and enhance innovation standards & research
5	Developing a Conducive Business & Improving National Infrastructure	PCM w/ IBEL & MoET	<ul style="list-style-type: none"> Improve business environment through appropriate legislation and improve infrastructure in order to provide an enabling environment for SMEs’ needs
6	Coherence & Effective Coordination	SME Secretariat (In-House) <i>Statistics Team under Strategy Performance Unit</i>	

Figure 40: Proposed Champions for Strategic Thrusts

4.4 Lebanon's SME Roadmap

4.4.1 Developing the Roadmap – The Approach

To detail Lebanon's SME strategy and address the identified challenges, a 3-step approach was adopted to identify, prioritize and define the way forward as shown in Figure 41 below.

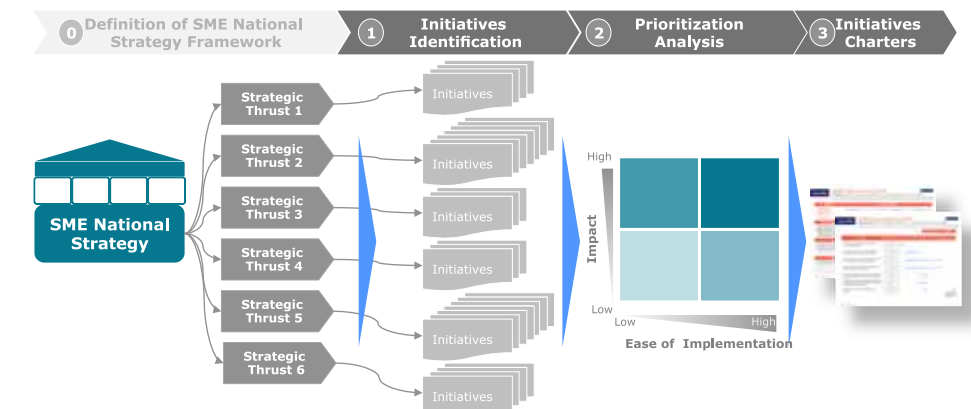


Figure 41: Developing the Roadmap – The Approach

Based on the set vision and objectives, a long list of relevant initiatives was developed and assigned to their respective strategic thrusts as shown in the previous section. Currently existing and proposed initiatives were complemented with new ones identified through a benchmarking exercise. Subsequently the execution of these initiatives was prioritized along two dimensions, namely ease of implementation and impact.

To measure ease of implementation, the below was evaluated to the extent possible:

- Overall time required and level of general acceptance that would facilitate the implementation;
- Dependencies on multiple stakeholders or other initiatives; complexity arising from institutional and bureaucratic constraints;
- Scale and type of the associated costs (one-off vs. recurring) and availability of any offsets (e.g., synergies with other initiatives, donor funding).

As for impact, the below was evaluated:

- Span of impact in terms of target types of enterprises, geographical and sector reach as well as gender bias;
- Economic attractiveness in terms of ability to contribute to the national economy and the creation of employment opportunities (with a preference for high value added / skilled jobs);
- Contribution to advance the four strategic objectives.

The prioritization exercise allows the grouping of initiatives into four groups with different implications on execution (*Figure 42*).

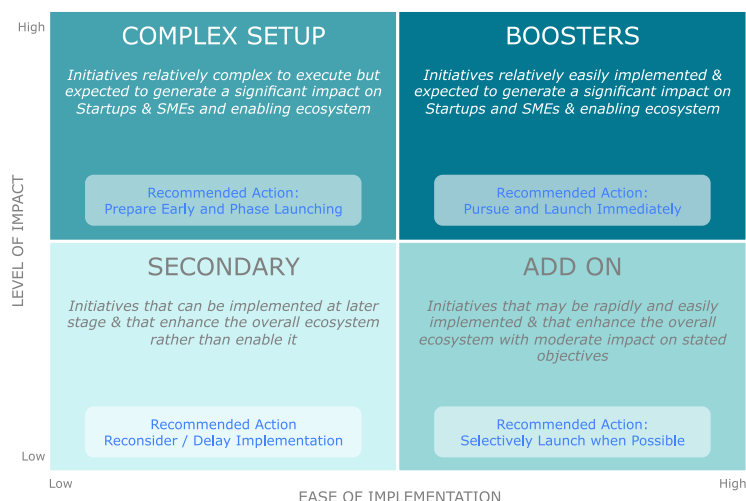


Figure 42: Prioritization Framework

“Booster” initiatives are relatively easy to implement and are expected to generate significant direct impact on startups and SMEs as well as the enabling ecosystem. As such, it is recommended to pursue and launch these initiatives as soon as possible.

“Complex Setup” initiatives are similar to “Booster” initiatives in terms of impact; however their implementation is relatively complex and requires time/effort/capital. To succeed with these initiatives, it is necessary prepare the groundwork early-on. As such, the recommended way forward is to phase their implementation over time, starting immediately with the most promising ones.

“Add On” initiatives are those that may be rapidly and easily implemented and that primarily enhance the overall ecosystem. Again, it is recommended to selectively launch these initiatives over time, pending an opportune time and availability of resources.

Finally, the **“Secondary”** initiatives are those that enhance the overall ecosystem or have a second degree impact, and are often difficult to implement. In this case, it is best to reconsider the implementation of these initiatives at a later stage.

4.4.2 Three Implementation Waves

Based on the outlined prioritization methodology, identified initiatives were all evaluated and assigned to three consecutive waves for the short, medium and long term. To the extent possible, and after several consultations with key stakeholders, an attempt to provide a balanced mixed of initiatives that support the attainment of the stated objectives and fit with the recognized strategic thrusts was made.

Figure 43: Implementation Roadmap

Wave	#	Initiative
I	1.1	Develop Mentorship Networks
	1.3	Provide National Recognition for SME Role Models
	2.1	Attract Top-Tier VC/PE Firms and Angel Investors
	2.2	Broaden Circular 331
	2.3	Improve Access to Debt Capital
	2.5	Launch iSME Project
	3.1	Bridge SMEs to Large Enterprises and Multinationals
	3.2	Leverage the Global Lebanese Network
	3.3	Activate the Lebanese Export Promotion Agency (LEBEX)
	3.4	Improve Market Competitiveness
	3.5	Enhance Standards of SME Products and Services
	3.6	Strengthen Relationships with New Top Trading Partners
	4.1	Develop Competitive Capabilities Clusters
	4.3	Assist SME's Technology Upgrade
	4.8	Link Industry to Academia with Innovation Vouchers
	4.11	Assist SMEs in Cleaner Production and Resource Efficiency
		Update, Ratify, and Implement 1 st Wave of Pending Laws
	5.3	– Code of Commerce
	5.4	– Insolvency Law
	5.5	– Public Procurement Law

Wave	#	Initiative
I	5.10	Launch a Job Matching Program
	6.1	Focus All Efforts on an Industry / City
	6.3	Set Up an SME Observatory
II	1.5	Establish Women-Friendly Business Environment
	4.2	Repatriate Lebanese Expat Success Stories
	4.4	Introduce Apprenticeship Programs
	4.7	Establish a Commercialization Office
	5.1	Twin IPPO with an International Counterpart
		Ratify and Implement 2nd Wave of Pending Laws
	5.6	– Domestic and Foreign Investment Promotion Law
	5.7	– Labor Code
	5.9	Attract and Facilitate Access to Skilled Labor
	6.2	Establish Regional “SME Malls”
	6.4	Create/Upgrade a full-fledged portal for Entrepreneurs and SMEs
III	1.2	Launch Entrepreneurship & Family Business Center at the Lebanese University
	1.4	Develop a Second-Launch Restructuring Program
	2.4	Introduce SME Exchange and Enhance Crowd Funding
	4.5	Expand Vocational and Training Programs to Meet Market Needs
	4.6	Provide Incentives for Employee Training
	4.9	Optimize R&D Spending On Core Sectors
	4.10	Introduce R&D Expenditure Tax Credit
	5.2	Upgrade IP Framework and Patenting Process
	5.8	Adapt Judicial System to Meet SME Requirements
	5.11	Develop Government E-Services

It is critical to stress that achieving the objectives set in the strategy is incumbent upon all concerned parties. The public and private sector have to collaborate in implementing these initiatives. As importantly, entrepreneurs and SME owners have to play an active role in contributing and providing feedback. Indeed, it is the holistic approach that yields the best result. As such, all stakeholders are encouraged to participate in unleashing the potential of this economic engine.

4.5 Conclusion: A Clear Call for Action

Comprising over 90% of the Lebanese registered enterprises and affecting the livelihood of some 50% of the declared employees, setting and implementing the national SME strategy is of paramount importance. Indeed, the numbers show that working towards building strong, sustainable and growing SMEs will help develop the Lebanese economy across industries and regions – a real national priority.

Besides typical hurdles faced by SMEs across the globe, challenges of Lebanese small and medium enterprises are further exacerbated by the local and regional geopolitical context. This study highlights several areas where Lebanese SMEs need help and assistance for them to succeed.

Despite, and perhaps because of, these challenges, the Lebanese public and private sector, and the civil society has mobilized and been active in promoting and developing entrepreneurship in Lebanon. Over the past few years, initiatives and programs have flourished in Lebanon, helping to maintain the country's position as one of the leading entrepreneurially driven societies in the region. While commendable, these disparate efforts to date have fallen short of truly turning around the SME situation in Lebanon due to scale and scope, with most focusing on a narrow portion of early-stage startups.

Going forward, with the limited resources available, it is imperative for all parties, public and private, to work in unison to help the success of Lebanese SMEs. As such, adopting a unified coordinated roadmap and allowing each party to help where best it can is likely to yield a better outcome. The study recommends several initiatives and has prioritized their implementation. Also, the strategy maintains the importance of an end-to-end approach where help is provided from the fledgling entrepreneurs and startups all the way to nurturing the small and medium enterprises, especially ones with high-growth potential. While opinions may differ, this strategy should be considered a first iteration that has to evolve with the prevailing context in which Lebanese SMEs operate.

Practically, next steps include developing the business cases and conducting a detailed design of each initiative, broadening the consultation and outreach process to discuss the strategy with international organizations that can assist Lebanon, and putting this strategy in the national agenda by rallying all stakeholders behind it in order to share a common vision for SMEs.

To be clear, there should be no doubt as to the urgency and importance of SMEs in Lebanon. The country is blessed with most of the right essential ingredients: highly ambitious and educated entrepreneurs, a financial savoir-faire and depth beyond its size, above average capabilities, a global footprint with its diaspora and a traditionally open economy. Under the right direction and with the support of all stakeholders, Lebanon has as tremendous opportunity to drive the renewal of its economy. Let's all act now for it not to continue to be wasted.