



**Youth and Social Entrepreneurship  
in the Middle East**

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## Introduction

The Middle East and North Africa (MENA) has the highest youth unemployment rates of any geographical region in the world. The region has an average youth unemployment rate of over 30 percent and many countries such as Egypt, Yemen, and Iraq suffer even higher unemployment rates. This lack of jobs has created a myriad of problems, not only economically but socially as well. One potential solution to the region's economic problems is the encouragement of social entrepreneurship, especially among youth. This paper raises the following questions. Can the region's economic problems be addressed by promoting youth entrepreneurship? if so, how can this behavior be encouraged? What are the social and political obstacles to doing so?

Lack of economic opportunity in the MENA undermines national and regional political stability. As evidence, one needs look no further than the Arab Spring. The political uprisings which swept across the Middle East were, at their core, spurred by economic interests. Mohamed Bouazizi's self-immolation in Tunisia in late 2010, which sparked the protests which spread across the Arab world, was not brought on by a desire for more representative government, but by his frustration at being unable to operate his merchant stall without interference by the city in which he worked. Bouazizi was himself an entrepreneur, attempting to operate in the informal sector of his country's economy and facing the impediments confronting entrepreneurs across the region. One of the Arab Spring's most popular chants was "aysh, hurriyya, 'adalah ijtimaiyya," which translates, "bread, freedom, and social justice." Notice that bread comes first, a fitting symbol of the movement's economic roots.

This paper is divided into five sections. First, we discuss the importance of entrepreneurship and what it means to be an entrepreneur. Then we use Latin America as a case study to understand just how effective entrepreneurship can be in alleviating the social and economic challenges faced by many countries in the Middle East. Following the discussion of Latin America, we examine the large youth demographic in the Middle East and its potential economic and political ramifications. We then shift our focus from the state of youth in the region to the state of entrepreneurship. Here we discuss the political and institutional context within which the region's youth entrepreneurs operate, as well as examples of successful initiatives. Finally, we discuss the factors which both encourage and prohibit entrepreneurship in the MENA region, and how these issues can be addressed to create a more entrepreneur-friendly environment.

## Importance of Entrepreneurship

Before we begin our discussion of entrepreneurship in the Middle East and North Africa, it is essential to first define what exactly is meant by entrepreneurship. Entrepreneurs are the backbone of the production process. They are responsible for its organization and coordination and serve as a link between capital and labor markets. Most importantly, entrepreneurs are responsible for creating innovations and making them available to the public. They are responsible for what Joseph Schumpeter termed "creative destruction"- the creation of new technologies and production methods that replace the old ones and drive society forward.

Entrepreneurship necessarily involves a certain level of risk. Innovating and creating unique businesses involves a high degree of uncertainty about both the nature of the market and the

productive potential of the respective business. In economic theory, the profits accrued to entrepreneurs are largely a result of this willingness to accept risk.<sup>1</sup> However, at a certain point, excessive risk begins to impede the formation of social enterprises and disincentivizes entrepreneurship. It is imperative that governments do what they can to create an entrepreneurial-friendly business environment by eliminating unnecessary risk. While this undoubtedly offers substantial social benefits, such a policy can be complicated by excessive levels of bureaucracy, high levels of corruption, institutional obstacles, and other political variables which will be discussed in the “Factors” section below.

Social entrepreneurship can be defined as, “engaging in an initiative whose primary aim is to achieve positive social impact and to do so using financially, sustainable methods.”<sup>2</sup> In short, social enterprises operate in the area between purely for-profit and non-profit ventures. This does not mean that a social enterprise cannot be profitable. Rather it only suggests that it has a twin mandate of being both profitable and promoting positive social change. Social entrepreneurship has four central principles<sup>3</sup>: The achievement of a positive social impact, the application of non-conventional ideas to social challenges, financial sustainability, and the possibility of “scaling up” the business or innovation being applied to society. Social entrepreneurship is distinguished from entrepreneurship more generally because the goal is not solely profit maximization but also the creation of positive social change. It should be noted, however, that many of the strategies designed to encourage social entrepreneurship can also benefit entrepreneurship more broadly defined.

Currently, the public sector accounts for most of the employment in the Arab world. These public sector economies developed after “revolutions,” largely by military forces, which involved the nationalization of domestic and foreign banks and industries. To this day the public sector accounts for between 60 and 80 percent of total formal employment in the Arab Gulf states, Egypt, Iraq, Jordan, and Tunisia and constitutes a sizable percentage of total employment. This overreliance on government jobs presents a major problem for economies throughout the MENA region. State finances in the Middle East are increasingly strained and governments are unable to bankroll bureaucratic salaries. At the same time, the state cannot risk scaling back salaries or laying off unproductive employees because of the risk of creating social unrest in what is already a delicate political environment. Meanwhile, bloated public sectors have crowded out private sector employment and reduced regional productivity. Protected public sector firms have little to no incentive to innovate and reinvest in themselves. Additionally, the extensive corruption which characterizes these bureaucracies poses a major problem for private businesses and overall productivity. The large state public sectors and the potential for a secure government job



<sup>1</sup> Eduardo Lora and Francesca Castellani, eds., *Entrepreneurship in Latin America: Ladder?* (Washington, DC: The World Bank, 2014), 19

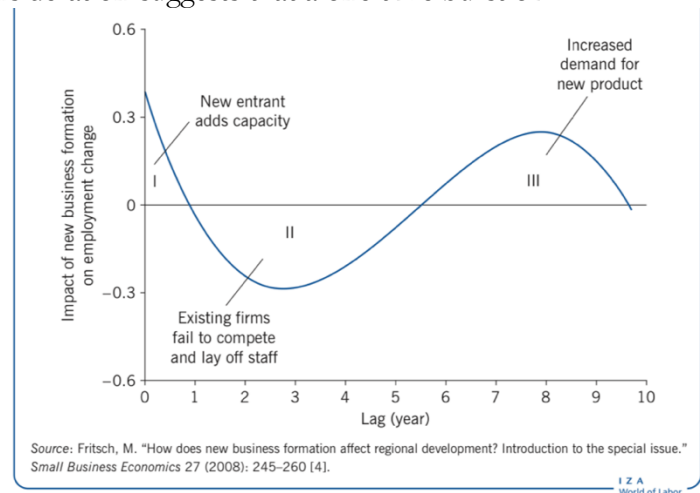
<sup>2</sup> Diana Greenwald, and Samantha Constant. “The Context for Social Entrepreneurship in the Middle East.” *Social Entrepreneurship in the Middle East*, vol. 1, 2015, pp. 39–66., doi:10.1057/9781137395368\_3.

<sup>3</sup> Ehaab Abdou, et al. *SOCIAL ENTREPRENEURSHIP IN THE MIDDLE EAST TOWARD SUSTAINABLE DEVELOPMENT FOR THE NEXT GENERATION*. The Brookings Institution, April 22, 2010, 8, [www.brookings.edu/wp-content/uploads/2016/06/04\\_social\\_entrepreneurship.pdf](http://www.brookings.edu/wp-content/uploads/2016/06/04_social_entrepreneurship.pdf).



creates an incentive for young people to seek or wait for the promised stable wages, benefits, and security of a job in the state bureaucracy rather than seeking or accepting jobs in the private sector.<sup>4</sup>

Entrepreneurship can be a boon to economies suffering from high unemployment. A report by Christopher M. Schroeder and Sherif Kamel of the American University of Cairo found that, for every ten successful enterprises, an additional 2,500 jobs are created. Entrepreneurs provide new job opportunities in both the short and long term.<sup>5</sup> In the short term, they increase employment as a result of new firms entering the market, growing and increasing their labor pool. In the long term, after market shares shift, and entrants unable to compete exit the market, the increased competitiveness of suppliers leads to another set of employment gains.<sup>6</sup> After a period of ten years, the impact of new enterprise formation fades away, although a positive economic impact related to the enterprise's activities may still exist. This consideration suggests that a one time burst of entrepreneurship cannot be a sufficient driver of long-term employment growth. Instead, economies need to cultivate an environment that encourages the consistent formation of SMEs. Here I use the term “economies,” rather than states, because reforms can occur on multiple dimensions, not just on a national level. Entrepreneurship can and should be incentivized on the state level, but also on a local level, by municipal administrators and, perhaps to a lesser extent, on a regional level by intergovernmental organizations (IGOs) and international development groups such as the IMF and the World Bank.



Entrepreneurship promotes the development of new industries and introduces product variation. These innovations in turn lead to increased economic growth. Newer firms are more likely to invest in innovation, and their more dynamic nature allows them to quickly shift course and adapt in ways which larger and more established firms are unable to replicate. The new firms also foster productivity as they displace existing firms which were unable to compete (the medium term in the chart above). As competition increases, existing firms are forced to either become more efficient or shut down in what Schumpeter defined as the process of “creative destruction”. While they have temporary negative employment outcomes, these changes in the market have been shown to have a positive overall effect on productivity in both single country studies and in an analysis of the OECD.<sup>7</sup>

Not only is entrepreneurship beneficial to the economy, but it also empowers the entrepreneur, especially the young entrepreneur. A healthy environment for entrepreneurship

<sup>4</sup> Bessma Momani, *Entrepreneurship: An Engine for Job Creation and Inclusive Growth in the Arab World*. The Brookings Institution, Mar. 2017, [www.brookings.edu/wp-content/uploads/2017/03/entrepreneurship\\_in\\_the\\_arab\\_world.pdf](http://www.brookings.edu/wp-content/uploads/2017/03/entrepreneurship_in_the_arab_world.pdf).

<sup>5</sup> Alexander Kritikos, “Entrepreneurs and Their Impact on Jobs and Economic Growth,” *IZA World of Labor*, 2014: 3-4, doi:10.15185/izawol.8.

<sup>6</sup> Ibid

<sup>7</sup> Kritikos, “Entrepreneurs and Their Impact,” 4

encourages growth in human capital and fosters the development of the next generation of leaders. It offers options to youth who otherwise might not see a bright future ahead of them, especially given the difficult employment situation of the Middle East. Additionally, social entrepreneurship creates a culture of awareness of social issues while encouraging youth to play an active role in their communities. Interest in social entrepreneurship is markedly high in the region, with a poll by Ernst and Young showing that roughly a fifth of entrepreneurs in the Middle East want to effect positive social change through their ventures.<sup>8</sup>

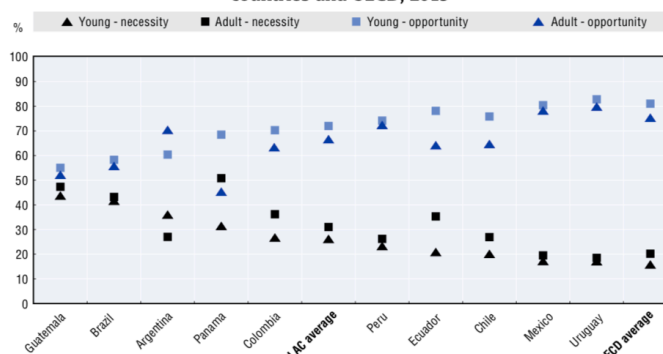
Aside from the more obvious and immediate economic benefits which can be gained from entrepreneurship, social entrepreneurship plays an even greater role in addressing some of the MENA region's most pressing developmental challenges.<sup>9</sup> Social entrepreneurship allows for the creation and testing of innovations which can better address social needs, provide basic services, and achieve equitable development than most public programs. Unfortunately, many states are unable or unwilling to overcome the political and institutional obstacles necessary to achieve these goals.

All of this said, social entrepreneurship cannot exist in a vacuum. Young entrepreneurs require support from both national and local governments, as well as and the private sector, to be successful on a large scale. Unfortunately, the required level of support does not currently exist. As most would agree, the Middle East suffers from a uniquely unstable political environment. As such, it is not enough to simply encourage entrepreneurship in the present. It is also necessary for both public and private sector groups to plant the seeds which would blossom into a healthy and sustainable environment for social entrepreneurship, such as creating an entrepreneur-friendly regulatory environment.

## The Latin American Example

Latin America provides a useful case study the potential effectiveness of entrepreneurship as a tool for economic growth in the Middle East. Latin America faces political and economic challenges comparable to those faced by the Middle East. Corruption and red tape prevent many would-be entrepreneurs from getting their businesses off of the ground. Additionally, the region has faced a significant youth bulge, although that bulge is now in decline and not as severe as it once was. Similar to countries in the Middle East, many Latin American countries rank low when it comes to ease of doing business.<sup>10</sup> Given these similarities, by examining the role entrepreneurship has played in Latin

Figure 1.8. Entrepreneurial motivation in Latin American and Caribbean countries and OECD, 2015



Note: LAC average includes Argentina, Brazil, Colombia, Costa Rica, Ecuador, El Salvador, Mexico, Panama, Peru and Uruguay.

Source: OECD/ECLAC/CAF based on Global Entrepreneurship Monitor individual data 2015.

<sup>8</sup> Kate Moran, "Leveraging the Youth Bulge to Transform the Arab World," *CIPE Development Blog*, Center for International Private Enterprise, February 2, 2016, [www.cipe.org/blog/2016/02/02/leveraging-the-youth-bulge-to-transform-the-arab-world/#.Wn-k\\_LbMzq3](http://www.cipe.org/blog/2016/02/02/leveraging-the-youth-bulge-to-transform-the-arab-world/#.Wn-k_LbMzq3).

<sup>9</sup> Abdou, "SOCIAL ENTREPRENEURSHIP," 29.

<sup>10</sup> "Ease of Doing Business Index." | Data, The World Bank, Last Updated 2017, [https://data.worldbank.org/indicator/IC.BUS.EASE.XQ?end=2017&start=2017&view=map&year\\_high\\_desc=true](https://data.worldbank.org/indicator/IC.BUS.EASE.XQ?end=2017&start=2017&view=map&year_high_desc=true).

America, we can extrapolate information about the potential benefits it would have in the Middle East and North Africa.

Entrepreneurship, and especially social entrepreneurship, developed in Latin America much sooner than it did in the Middle East. The region's social entrepreneurs, "intentionally—and not because of guilt or obligation—take on chronic social ills."<sup>11</sup> Many of the region's entrepreneurs can be described as "necessity entrepreneurs," who launch their own business not out of choice, but out of necessity, due to the fact that no other opportunities were available to them to make a living.<sup>12</sup> According to the World Bank, nearly one out of every three entrepreneurs in Latin America can be characterized as a "necessity entrepreneur."<sup>13</sup> This same model can be applied to entrepreneurs in countries such as Egypt where they face the same situation.

How has entrepreneurial model of economic development proven successful in Latin America? In Mexico, for example, studies have shown that on average, entrepreneurs have higher incomes than non-entrepreneurs. Additionally, they have an increased chance of upward socio-economic mobility, long considered a sign of a healthy economy.<sup>14</sup> The gains from entrepreneurship are often highest at the extreme ends of the socio-economic ladder, allowing previously poor entrepreneurs to join the middle class. Other studies of entrepreneurship have been conducted with similar results in many other Latin American countries.

The spread of entrepreneurship has been heavily encouraged by civil society organizations in Latin America and has had a positive effect on employment growth in the region.<sup>15</sup> The increase in the number and variety of small businesses has led to a growth in job opportunities as entrepreneurs contribute to the region's economic growth by their job creation. Local governments have begun to shift away from the traditional strategy of "attracting a factory that could employ many people," and instead are focusing their attention on promoting entrepreneurship among youth as a formal job creation strategy.<sup>16</sup> The acknowledgement by local governments of the potential benefits of entrepreneurship and the corresponding policy shift in trying to create an environment that is more hospitable to entrepreneurship is essential to the development social entrepreneurship. The attention paid to entrepreneurship by the state in Latin America, and the concerted effort to promote entrepreneurship which follows, is what has allowed entrepreneurship in the region to improve significantly.<sup>17</sup>

Entrepreneurship in the region has also been helped by the state and the private sector which have started incubators and accelerator programs to help develop early stage startups and entrepreneurs.<sup>18</sup> Similar to other developing regions, one of the most difficult challenges facing

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<sup>11</sup> Neela Pal, "Impact Entrepreneurship in Latin America (SSIR)," *Stanford Social Innovation Review*, February 15, 2013, [ssir.org/articles/entry/impact\\_entrepreneurship\\_in\\_latin\\_america](http://ssir.org/articles/entry/impact_entrepreneurship_in_latin_america).

<sup>12</sup> Lora and Castellani, "Entrepreneurship in Latin America," 4

<sup>13</sup> "Entrepreneurship Is the Trend in Latin America," *World Bank*, September 30, 2015, [www.worldbank.org/en/news/feature/2015/09/30/emprender-esta-de-moda-en-america-latina](http://www.worldbank.org/en/news/feature/2015/09/30/emprender-esta-de-moda-en-america-latina).

<sup>14</sup> Lora and Castellani, "Entrepreneurship In Latin America," 82

<sup>15</sup> World Bank, "Entrepreneurship Is the Trend in Latin America."

<sup>16</sup> Ibid

<sup>17</sup> Freddie Dawson, "Growing Entrepreneurship in Latin America," *Forbes Magazine*, July 31, 2014, [www.forbes.com/sites/freddiedawson/2014/07/31/growing-entrepreneurship-in-latin-america/#7de336a81af9](http://www.forbes.com/sites/freddiedawson/2014/07/31/growing-entrepreneurship-in-latin-america/#7de336a81af9).

<sup>18</sup> "Funding Social Entrepreneurship in Latin America," *BlueStar Strategies*, September 30, 2015, [www.bluestarstrategies.com/news/insight-and-analysis/261-funding-social-entrepreneurship-in-latin-america](http://www.bluestarstrategies.com/news/insight-and-analysis/261-funding-social-entrepreneurship-in-latin-america).

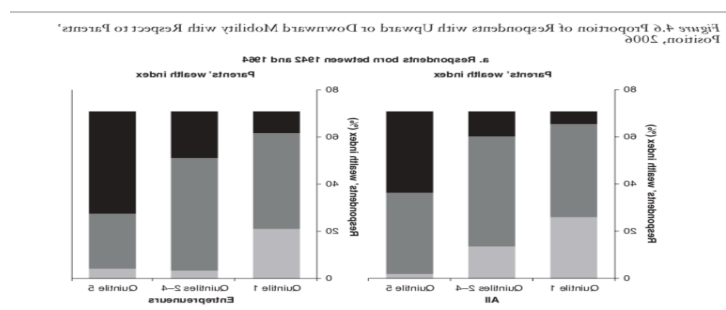


entrepreneurs in Latin America is fundraising. This is especially true for the newest startups because potential investors are concerned by the new businesses' lack of a "track record." These incubators and accelerator programs make it much easier for young entrepreneurs to connect with potential investors and acquire the financial capital necessary to grow their businesses. Many of the largest funders of social enterprises in Latin America are foundations, governments, and multi-lateral organizations such as the Inter-American Development Bank.

Entrepreneurs in Latin America have also faced, and continue to face, similar challenges to those faced by entrepreneurs in the Middle East. Red tape and inefficient procedures inhibit entrepreneurship and make doing business in Latin America extremely difficult. Would-be entrepreneurs also have less formal exposure to entrepreneurship and the business world before starting their own businesses. Entrepreneurs in Latin America also face similar cultural and legal barriers to the ones faced by entrepreneurs in the Middle East such as government corruption, bloated bureaucracies, and difficulty acquiring funding. However, as entrepreneurship becomes more established these barriers have begun to dissipate. Unlike more advanced Western economies, it is incredibly difficult to fail and close a business in both the Middle East and Latin America due to a lack of favorable business laws and regulations, e.g., the frequent absence of protection through bankruptcy laws. Additionally, negative cultural stigmas against risk and failure serve as disincentives towards the creation of small businesses. As one expert puts it, "This aversion to failure is not irrational. It is associated with the fact that it is very difficult to fail and close a company in the region. It is different in the U.S. There, you are expected to fail several times. That's because you learn from those failures so you can improve your business model."<sup>19</sup>

Although many Latin American countries still struggle with economic issues, such as a large informal sector and an over-reliance on natural resources and commodity exports, it is clear that the adoption of entrepreneurship as a means of economic growth by some of the region's nation-states has been a powerful force for socio-economic progress. It has allowed for an increased degree of economic diversification, job creation, and social mobility and has been encouraged by both the state and private organizations alike. Given its political and economic situation, the region's experience with entrepreneurship would suggest that the Middle East, with its similar demographic, economic, and political challenges could replicate this success

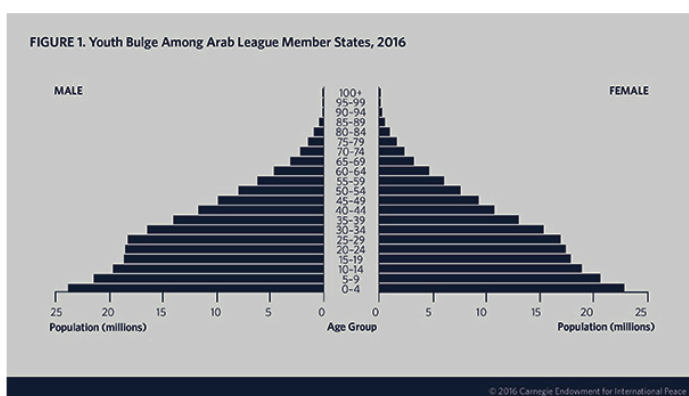
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<sup>19</sup> World Bank, "Entrepreneurship Is the Trend in Latin America."

<sup>20</sup> Lora and Castellani, "Entrepreneurship In Latin America," Figure 4.6 (page 88)

## Youth in the Middle East



Latin America's example is demonstrative of the potential for entrepreneurship in the Middle East. The Middle East is experiencing a huge youth bulge, with 65 percent of the region's population below the age of 30 and more than 28 percent of the population between the ages of 15 and 29. In many Middle Eastern countries, youth constitute an even higher percentage of the population. The current proportion of youth to adults is the highest in the region's history.<sup>21</sup> A youth population this large is an incredible and mostly untapped source of potential economic power. A significant portion of the growth experienced by the "Asian Tigers" is attributed to the fact that they were able to take advantage of the growth in their working age population through human capital development.<sup>22</sup> While a large generation of more educated youth suggests a promising scenario, it comes with potential problems. The youth bulge has resulted in stress on the region's education systems, labor markets, social services, and infrastructure.<sup>23</sup> These problems are in part due to the fact that many states have followed corrupt and nepotistic policies which have limited the expansion of the economy and the ability of social services to keep up with increasing demand.

Exacerbating these problems is the lack of jobs, with youth unemployment rates at 42 percent (2014 World Bank estimate) and in some cases even higher, which makes it exceedingly difficult for youth to become socially and financially independent. The youth unemployment problem is unlikely to go away naturally anytime soon, with a recent World Bank report estimating that the region will need to create 80 million new jobs in the next two decades.<sup>24</sup> In many of the region's countries, it formerly was the case that

Country	Youth unemployment (%)	Female LF participation (%)
Algeria	24.0	15.2
Bahrain	27.9	39.2
Egypt	38.9	23.7
Iraq	34.1	14.9
Jordan	33.7	15.6
Kuwait	19.6	43.6
Lebanon	20.6	23.3
Libya	51.2	30.0
Morocco	18.5	26.5
Oman	20.5	29.0
Palestinian Territories	38.3	15.4
Qatar	1.5	50.8
Saudi Arabia	28.7	20.2
Syria	29.8	13.5
Tunisia	31.2	25.1
United Arab Emirates	9.9	46.5
Yemen	29.8	25.4

<sup>21</sup> Moran, "Leveraging the Youth."

<sup>22</sup> Emmanuel Y. Jimenez and Mamta Murthi, "Investing in the Youth Bulge," *Finance and Development*, September 2006, <https://www.imf.org/external/pubs/ft/fandd/2006/09/jimenez.htm>

<sup>23</sup> Abdou, "SOCIAL ENTREPRENEURSHIP," 5

<sup>24</sup> "Unlocking the employment potential in the Middle East and North Africa - toward a new social contract."

Middle East and North Africa - MENA - Development Report. (Washington, DC: World Bank, 2014), 1

<http://documents.worldbank.org/curated/en/343121468753030506/Unlocking-the-employment-potential-in-the-Middle-East-and-North-Africa-toward-a-new-social-contract>

college educated youth were all but guaranteed a public sector job after graduation. However, the increasing size of the labor force, coupled with a decrease in the relative size of the public sector, makes government employment an increasingly unlikely prospect for new graduates. According to a 2016 report by the UNDP, sixty million jobs needed to be created by 2020 to meet the increased demand from youth entering the labor force, a difficult challenge which the region's economies have been unable to achieve.<sup>25</sup> Unemployment rates are further complicated because formal female labor force participation in the region is strikingly low, despite the fact that, in many Arab universities, women constitute as much as 70 percent of the student body. Many of the young women not counted in the labor force may be engaged in unpaid family work or irregular wage labor in the informal sector of the economy.

Unemployment in the region is often not just a short-term phenomenon. Those who are unemployed often spend several years looking for jobs. The inability to achieve some degree of financial stability causes youth to leave their parents homes later and to put off getting married due to a lack of financial feasibility. This is particularly true for middle and lower class urban youth but these effects extend to rural communities as well. High youth unemployment leads, in turn, to a significant degree of social and political unrest. Indeed, recent social revolutions have been primarily fueled by youth with high levels of unemployment and seemingly perennial economic difficulty as one of the main drivers. In a 2013 Pew survey, an overwhelming number of respondents identified a lack of employment opportunities as a "very big problem"- 60 percent in Egypt, 56 percent in Jordan, 91 percent in Lebanon, 86 percent in the Palestinian Territories, and 90 percent in Tunisia. Widespread dissatisfaction with national economic performance and employment opportunities poses a significant problem for national governments. As we have seen repeatedly in the past, such discontent undermines political stability and has led to mass protests throughout the region.

Many young people who are able to find some form of employment suffer from underemployment, or having to accept jobs below the level of their qualifications due to economic necessity. Another study by the International Labor Organization shows that almost half of employed youth are in jobs that do not match their level of education. The growing frustration as a result of this phenomenon can be seen by the fact that graduates of doctoral and masters degree programs often stage protests against the government. An often seen sign at these protests reads, "Four years Bachelors, three years Masters, four years PhD, and still unemployed!"<sup>26</sup>

Unemployment rates are even higher for young women than for young men. For example, in Egypt the unemployment rate for young women is an astonishing 49.8 percent.<sup>27</sup> Women, especially rural women, are less likely to receive formal education than their male counterparts putting them at a distinct disadvantage when it comes to the job market. Gender discrimination leaves a substantial segment of the potential labor force out of work with few options available to them. Additionally, negative cultural stigmas around women who work still abound in many of the region's countries.

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<sup>25</sup> United Nations Development Program (UNDP), *Arab Human Development Report: Youth and the Prospect for Human Development in a Changing Reality* (New York: UNDP Regional Bureau for Arab States, 2016), 32, available from <http://www.arab-hdr.org/reports/2016/english/AHDR2016En.pdf>.

<sup>26</sup> Adel Abdel Ghafar, "Educated But Unemployed: The Challenge Facing Egypt's Youth." *Brookings.com*, The Brookings Institution, July 2016, 6 [www.brookings.edu/wp-content/uploads/2016/07/en\\_youth\\_in\\_egypt-2.pdf](http://www.brookings.edu/wp-content/uploads/2016/07/en_youth_in_egypt-2.pdf).

<sup>27</sup> Ghafar, "Educated But Unemployed," 5

These attitudes put cultural pressure on women which makes it more difficult for them to achieve gainful employment, especially in the private sector.

The inability to find work has driven many young people into the informal sector. The informal sector refers to firms and workers which are outside of a country's tax and regulatory systems, although the work they are engaged in is not necessarily illegal.<sup>28</sup> In fact, the vast majority of informal businesses sell legal goods and services. In Egypt, the volume of the informal sector is around one-and-a-half-trillion Egyptian pounds, roughly two-thirds the size of the formal economy.<sup>29</sup> Across the region it is estimated that 27 percent of GDP and 2/3 of the labor force exists in the informal sector.<sup>30</sup> Examples of informal businesses can range from private tutors to street vendors to mechanics. The one uniting factor is that their businesses are not formally licensed and so operate outside of the formal regulatory framework. Excessive bureaucracy, difficult registration conditions, and political impediments towards the formation of a business (such as the need for bribes in many countries in order to push paperwork through) are also common reasons why a prospective entrepreneur might choose to operate in the informal sector.<sup>31</sup> Many firms may start out as informal enterprises to avoid political and bureaucratic obstacles to the formation of their business and then become formally registered years later after they are able to create more capital and better establish themselves.

The increase in the size of the informal economy poses several problems. First, it results in the loss of billions of dollars in potential tax revenue, money which could be very beneficial to the region's cash strapped states. Moreover, those who work in the informal sector have little in the way of job security and lack the social and financial benefits of formal employees, such as access to social security and pensions. Creating a friendlier business climate in the Middle East and North Africa could go a long way towards reducing the amount of small businesses operating within the region's informal sector and increase the ability of youth to engage in entrepreneurship.

Creating an entrepreneurial venture is often easier said than done. A recent Statfor study argues that many states in the Middle East and North Africa are unwilling to make the necessary reforms because they fear that doing so will undermine the regime's grip on power.<sup>32</sup> The argument against private sector development is that the dominant social contract in the region, one which developed in many Arab countries after the military's seizure of power established one-party rule, is based on the state providing its citizens with a high standard of living through the public sector

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<sup>28</sup> "Why It's Hard to Reduce Informality in Latin America's Labour Market," *The Economist*, February 15, 2018, [www.economist.com/news/americas/21737088-solving-problem-holds-back-growth-and-productivity-why-its-hard-reduce-informality](http://www.economist.com/news/americas/21737088-solving-problem-holds-back-growth-and-productivity-why-its-hard-reduce-informality)

<sup>29</sup> Doaa Farid, "Informal Sector Volume Records Around EGP 1.5tn: ECES," *Daily News Egypt*, September 23, 2014, <http://www.daily-newsegypt.com/2014/09/23/informal-sector-volume-records-around-egp-1-5tn-eces/>

<sup>30</sup> Diego F. Angel-Urdinola and Kimie Tanabe, "Micro-Determinants of Informal Employment in the Middle East and North Africa Region." Social Protection Paper No. 1201, World Bank, (January 2012): 2, <http://documents.worldbank.org/curated/en/843621468275089806/pdf/665940NWP00PUB0Box365795B0SPDP01201.pdf>

<sup>31</sup> Bringing Light to the Grey Economy," *The Economist*, October 15 2016, [www.economist.com/news/international/21708675-new-technology-may-persuade-informal-businesses-and-workers-become-formal-bringing-light](http://www.economist.com/news/international/21708675-new-technology-may-persuade-informal-businesses-and-workers-become-formal-bringing-light).

<sup>32</sup> "Youth Unemployment: The Middle East's Ticking Time Bomb," Stratfor, February 28, 2018, [worldview.stratfor.com/article/youth-unemployment-middle-east-teen-jobless](http://worldview.stratfor.com/article/youth-unemployment-middle-east-teen-jobless).

economy. This state sponsored standard of living is based on varying combinations of subsidies, public sector employment, and commodity exports. In return, citizens give the state their loyalty and largely forgo any right to participate in politics. However, this social contract has begun to deteriorate as many Arab states have been unable to maintain a high standard of living for their citizens. At the same time, these states are unwilling to alter the status quo by encouraging entrepreneurship and private industry as this may create market forces which they are unable to control.<sup>33</sup>

The lack of opportunity in their home countries often leads educated young people to emigrate and start a life elsewhere in the world, creating a brain drain that perpetuates the region's economic problems. According to the United Nations Development Program, roughly 20 to 25 percent of Arab youth leave the Middle East in search of a "better future"- an almost 100 percent increase since 2012.<sup>34</sup> Over 50 percent of the migrants to OECD countries from Egypt, Iran, Iraq, Lebanon, and Jordan have at least a college education.<sup>35</sup> The flight of well-educated and skilled young Arabs from their home countries reduces the amount of human capital and hinders both entrepreneurship and economic development. Migration of educated youth then exacerbates the problems that incentivized them to leave in the first place, encouraging an even larger brain drain and fomenting unrest among the segment of the population that remains in the country.

For years scholars have been describing the Middle East's youth bulge as a ticking time bomb.<sup>36</sup> Security experts fear that, as young men languish unemployed around the region, the allure of groups like Hezbollah and the Islamic State becomes stronger because they offer them the potential for decent wages and a cohesive source of identity which they are unable to obtain elsewhere.<sup>37</sup> Many analysts believe that the same type of frustrations which lead to the Arab spring could become a destabilizing force and bring about a more negative change in an already volatile region. A study done by Chris Meserole of the Brookings Institution revealed that, "when between 10 and 30 percent of a country's youth are unemployed, there is a strong relationship between a rise in youth unemployment and a rise in Sunni militancy."<sup>38</sup> The region's countries are, unfortunately, well past this unemployment threshold.

The effect of the region's youth bulge does not necessarily have to be a negative one. If youth are provided with the opportunities, and especially economic opportunities, they will be able to shape their futures. Then youth can act as drivers of social change and economic growth—allowing the country to achieve greater success. We have already seen the power of youth in the region to drive political and social change. With the proper assistance from the state and the domestic private sector, this power can be harnessed to produce a positive benefit for both the entrepreneur and the region as a whole. Therefore, policy makers should focus their efforts on

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<sup>33</sup> Stratfor, "Youth Unemployment"

<sup>34</sup> James Reinl, "Arab 'Brain Drain' Accelerates after Arab Spring: UN," *Middle East Eye*, May 9, 2015, [www.middleeasteye.net/news/un-arab-brain-drain-accelerates-after-arab-spring-1752815577](http://www.middleeasteye.net/news/un-arab-brain-drain-accelerates-after-arab-spring-1752815577).

<sup>35</sup> Caglar Ozden, "BRAIN DRAIN IN MIDDLE EAST & NORTH AFRICA – THE PATTERNS UNDER THE SURFACE." *UNITED NATIONS EXPERT GROUP MEETING ON INTERNATIONAL MIGRATION AND DEVELOPMENT IN THE ARAB REGION*, (May 11, 2006): 9, [http://www.un.org/en/development/desa/population/events/pdf/expert/11/P10\\_Ozden.pdf](http://www.un.org/en/development/desa/population/events/pdf/expert/11/P10_Ozden.pdf)

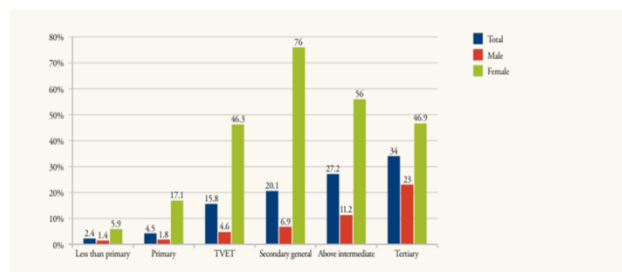
<sup>36</sup> Moran, "Leveraging the Youth Bulge."

<sup>37</sup> Ibid

<sup>38</sup> McCants, William, and Christopher Meserole, "The French Connection," *Foreign Affairs*, April 11, 2016, [www.foreignaffairs.com/articles/2016-03-24/french-connection](http://www.foreignaffairs.com/articles/2016-03-24/french-connection).

creating an institutional framework which would provide opportunities for youth to positively contribute to their communities and their economies.

Youth in the MENA region are generally well educated. Therefore there is a high degree of human capital present in the labor force, indicating that the high levels of unemployment are for the most part due not to a lack of qualifications but to a lack of jobs and opportunities. In fact, a study conducted by the International Labor Organization reveals that unemployment rates actually increase with every additional level of education.<sup>39</sup> The study shows that unemployment rates among college graduates are almost seventeen times higher than those of youth with less than a primary level of education, 34 percent as compared to 2.4 percent. This in turn serves to discourage young Egyptians from pursuing higher education, because the labor market is already saturated with college graduates who are unable to find a job.<sup>40</sup>



Source: ILO 2014

Additionally, the youth literacy rate in the Middle East and North Africa is higher than the adult literacy rate, especially in the lesser developed countries. Some countries in the Middle East (such as Tunisia) have youth literacy rates close to or greater than 90 percent.<sup>41</sup> This is due to the fact that most countries in the region have achieved near universal primary school. Additionally, enrollment in secondary education across the region is at 63 percent, exceeding that of the world average.<sup>42</sup> Enrollment rates in higher levels of education vary across countries. However, the general trend is that much of the region has a high level of educational attainment.<sup>43</sup> While the education systems in these countries are far from perfect, the fact that many youth have achieved some level of education is an encouraging sign of an increasingly qualified labor force.

Clearly, this information would suggest that the staggeringly high unemployment rates are not due to apathy on the part of the region's young people. Youth in the MENA region can be, and are in fact, highly motivated. Many young Arabs dream of being able to start their own business. In fact, one survey of the region's youth showed that, "In 2010, even before the uprisings, 26 percent of youth in the Arab world were planning to open their own business in the next 12 months, versus 4 percent in the United States."<sup>44</sup> Surveys indicate that young people in the region are committed to

<sup>39</sup> Tariq Khokhar, "Chart: Literacy Rates Higher Among Youth than Adults." *The Data Blog*, World Bank, September 7, 2016, [blogs.worldbank.org/opendata/chart-literacy-rates-higher-among-youth-adults](https://blogs.worldbank.org/opendata/chart-literacy-rates-higher-among-youth-adults).

<sup>40</sup> "27، القبس الإلكتروني، البطالة بين شباب الدول العربية 28 %." Apr. 2017, [alqabas.com/387618/](http://alqabas.com/387618/).

<sup>41</sup> Max Roser and Esteban Ortiz-Ospina, "Literacy," *Published online at OurWorldInData.org*, Dataset sourced from the World Bank, Last Updated September 20, 2018, <https://ourworldindata.org/literacy>

<sup>42</sup> Greenwald, "The Context for Social Entrepreneurship in the Middle East."

<sup>43</sup> Mary Kraetsch and Samantha Constant, "Taking Stock of the Youth Challenge in the Middle East: New Data and New Questions." The Brookings Institution, July 28, 2016, [www.brookings.edu/articles/taking-stock-of-the-youth-challenge-in-the-middle-east-new-data-and-new-questions/](http://www.brookings.edu/articles/taking-stock-of-the-youth-challenge-in-the-middle-east-new-data-and-new-questions/).

<sup>44</sup> Dina Sherif, "Entrepreneurship for a Better Egypt," Middle East Institute, February 20, 2014, [www.mei.edu/content/entrepreneurship-better-egypt](http://www.mei.edu/content/entrepreneurship-better-egypt).



making a positive difference and are seeking ways to find greater meaning in their work. In a joint poll conducted by Silatech and Gallup, about 70 percent of youth surveyed around the Arab world responded that they believed that entrepreneurs help create jobs.<sup>45</sup>

This widespread attitude coincides with an uptick in interest in entrepreneurship, with 67 percent of Arab youth believing that their generation was more likely to start their own businesses than previous ones.<sup>46</sup> For youth from around the region, 83.2 percent believe that, “in my country, starting a business is considered a good career choice,” a larger proportion than in all developing regions (70.9 percent) and European countries (62.2 percent) surveyed. The Arab world had the highest percentage of youth in any region who agreed with the statement, “persons growing a successful new business receive high status.”<sup>47</sup> These facts clearly demonstrate that youth entrepreneurship in the Middle East is not only possible but can be highly beneficial and would have a significant amount of local support. However Stanford University estimates that it is 5 to 10 times more difficult for a startup to thrive in the MENA region than in the United States due to the region’s lack of effective property and contract laws and regulations, inadequate infrastructure, and market system which stifles the growth of entrepreneurial ventures.<sup>48</sup> The question which then remains is how can entrepreneurship in the MENA region be developed?

## The Current State of Entrepreneurship in the Middle East

The MENA region appears to be in the midst of what could be characterized as a “startup boom.”<sup>49</sup> Investment into the region is soaring compared to past levels, with annual funding reaching almost one billion dollars as of 2017. However, this investment is not evenly distributed, with most of the funding centered on the United Arab Emirates. At the same time, there is a significant amount of potential in the entrepreneurial environments of other Middle Eastern countries and quite a number of success stories.

The central role youth played in the Arab Spring has likewise motivated them to fight for economic change. A *New York Times* profile of the region suggests that the revolutions which swept across the region were followed by a more subtle, but equally important, entrepreneurial revolution based on the noticeable surge in entrepreneurial activity and the increased presence of groups willing to support such activity.<sup>50</sup> This second revolution is described as being led by a “a very educated and

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<sup>45</sup> “The Silatech Index: Voices of Young Arabs.” *Silatech*, Silatech & Gallup, June 2009, <https://www.silatech.org/en/publication/publication-details/docs/default-source/publications-documents/silatech-index-june-2009>

<sup>46</sup> “Arab Youth Survey 2014,” ASDA’A Burson-Marsteller, (2014): 16, <https://www.arabyouthsurvey.com/pdf/whitepaper/en/2014-AYS-White-Paper.pdf>

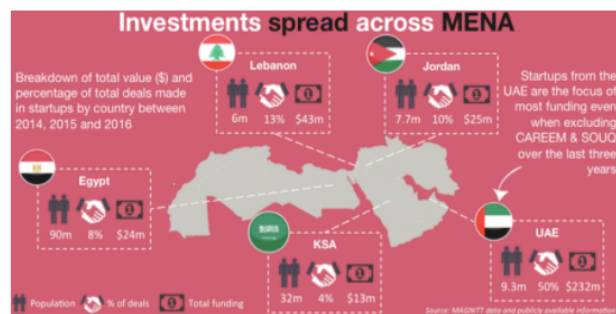
<sup>47</sup> Jacqui Kew et al., “Generation Entrepreneur? The State of Global Youth Entrepreneurship,” Global Entrepreneurship Monitor and Youth Business International, September 2013, 66-67, <http://www.youthbusiness.org/wp-content/uploads/2013/09/GenerationEntrepreneur.pdf>.

<sup>48</sup> Kathleen Bury, “What’s Holding Back Entrepreneurs in the Middle East and North Africa? (SSIR),” *Stanford Social Innovation Review*, August 8, 2016, [ssir.org/articles/entry/whats\\_holding\\_back\\_entrepreneurs\\_in\\_the\\_middle\\_east\\_and\\_north\\_africa](http://ssir.org/articles/entry/whats_holding_back_entrepreneurs_in_the_middle_east_and_north_africa).

<sup>49</sup> John McKenna, “The Middle East’s Start-up Scene – Explained in Five Charts,” *World Economic Forum*, May 17, 2017, [www.weforum.org/agenda/2017/05/what-you-need-to-know-about-the-middle-east-start-up-scene-in-five-charts/](http://www.weforum.org/agenda/2017/05/what-you-need-to-know-about-the-middle-east-start-up-scene-in-five-charts/).

<sup>50</sup> Hannah Seligson. “Arab Spring, Start-Up Summer?” *The New York Times*, July 16 2011, [www.nytimes.com/2011/07/17/business/global/egypts-entrepreneurs-look-beyond-the-revolution.html?\\_r=1](http://www.nytimes.com/2011/07/17/business/global/egypts-entrepreneurs-look-beyond-the-revolution.html?_r=1).

economically conversant, forward-looking group of people,” who are creating a new conversation around economic growth, economic diversification, and a rethinking of the region’s economy. As one entrepreneurs interviewed for the article noted, “The revolution really made my generation believe in ourselves.” This would imply that the Arab Spring revolutions not only led to regime change but also included a degree of “social psychological” empowerment which has produced a less discussed social “revolution” among the region’s youth. This particular entrepreneur had actually been planning on leaving Egypt until the revolution, at which point she decided to stay and try to make a difference in her home country.



As present, there have been successful youth-led entrepreneurial ventures in the Middle East in many different sectors. For example, in the field of mobile applications and communication, one of the most successful ventures is the Egyptian startup, Bey2ollak. Founded by a group of friends in their twenties, Bey2ollak is a mobile app that allows users to share real-time information about Cairo and Alexandria traffic in two of Egypt’s most congested cities. It helps commuters deal with the notorious traffic of Egypt’s cities. The app received over 5,000 users on the first day it was launched and is nearing a million. Bey2ollak received sponsorships from Vodaphone and have worked with advertisers such as Hyundai and FIFA, and is one of Egypt’s most successful startups.<sup>51</sup>

Another example of a successful startup is Karm Solar. Founded in October of 2011 by Ahmed Zahran, Karm Solar is a renewable energy company that offers an important alternative energy option to the significant number of Egyptians who live off of the electrical grid. This alternative sources of energy is especially useful to farmers who are dependent on diesel fuel-powered generators. Karm Solar is currently working on building a village entirely made of earth materials that will totally rely on solar energy.<sup>52</sup> There are other alternative energy startups in Egypt such as Tagaddod and Biodiesel Misr, which make biodiesel from used cooking oil. Both ventures have been able to secure investment and are among the country’s most promising new startups, although neither has been able to achieve the scale of Karm Solar.

As interest in startups has increased among Middle East investors, especially Western investors, a significant amount of local investment capital has begun to take notice, resulting in incubators and startup accelerators being established across the region. Both incubators and accelerators assist entrepreneurs in turning their startups into successful companies, although accelerators normally assist ventures later in their development. One of the largest and most successful is Flat6Labs. Flat6Labs is a regional startup accelerator program which describes itself on its homepage as organization that invests in “bright and passionate entrepreneurs with cutting-edge ideas.” It provides seed funding, strategic mentorship, a workspace, and entrepreneurship-focused business training, and connects startups to partner entities, mentors and investors. It was founded by

<sup>51</sup> Monica Ibrahim and Menan Khater, “Egypt’s young entrepreneurs work to fulfill revolution’s promise,” Public Radio International (PRI), June 5, 2014, <https://www.pri.org/stories/2014-06-05/egypts-young-entrepreneurs-work-fulfill-revolutions-promise>

<sup>52</sup> “KarmBuild | Architecture and Construction,” KarmSolar, accessed January 23, 2018, <http://karmsolar.com/architecture-construction/>

Ahmed Alfi, the CEO of Sawari Ventures. Flat6Labs has two main offices, one in Cairo and another in Jedda, Saudi Arabia.

Even the Occupied Palestinian Territories have their share of startup ventures, especially when it comes to the tech industry.<sup>53</sup> For example, Yamsafar is a Ramallah-based travel booking internet startup which has begun to gain international recognition and has been described as the Middle East's Booking.com. One of the first major investments in the startup came in the form of \$1 million in Series A funding from Sadara Ventures. As the first VC firm targeting the Palestinian tech sector, Sadara Ventures has been a major player in the rise of the West Bank's startup industry.

Despite its small size, the United Arab Emirates is home to arguably the two most successful startups in the MENA region: Souq, an online retailer described as the Middle East's Amazon, and Careem, the Dubai based ride-sharing service. The UAE has secured almost half of all startup funding in the past three years and is arguably the region's leading startup economy. This is in large part due to the UAE having the best business climate in the region, although much of the investment has been in the two major emirates, Abu Dhabi and Dubai. Other countries in the region, such as Qatar and Saudi Arabia, have taken notice and there has been a conscious effort by both governments and the private sector to improve the institutional environment of doing business in the Middle East.

However, the picture in the MENA region is not always a positive one and some countries fare better than others when it comes to entrepreneurship. Some countries, such as Jordan and Lebanon, have a high number of entrepreneurial initiatives per capita, while others such as Kuwait, Algeria, and Egypt lag behind.<sup>54</sup> These lagging countries are often the ones which have the least hospitable business climates and are plagued by excessive corruption and a bloated public sector. In many MENA countries, entrepreneurship is seen as a risky venture given the business climate. This is especially true when compared to a government job, which discourages youth from beginning a startup because they instead elect to wait for a job in the public sector. This problem in turn exacerbates the problem of youth unemployment which the emphasis on entrepreneurship is supposed to assist in eliminating.<sup>55</sup>

Social entrepreneurship as a separate model did not really begin to establish itself in the MENA region until the early 2000s. The concept is still not fully established in the region, with even the precise Arabic terminology still contested.<sup>56</sup> Social entrepreneurship is sometimes referred to as "*riyada al-majtama'iyah*" or alternatively as "*masbarfi ijtima'iyah*." This relative newness presents both an opportunity and a challenge to young entrepreneurs who are interested in engaging in social entrepreneurship. They have the opportunity to shape a new and exciting landscape in the region's economy and contribute to a process which can contribute to long-term economic development. At the same time, it is more difficult to create and operate social enterprises within an environment

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<sup>53</sup> Yadin Kaufmann. "Start-Up Palestine." *Foreign Affairs*, July 15 2017, [www.foreignaffairs.com/articles/israel/2017-06-13/start-palestine](http://www.foreignaffairs.com/articles/israel/2017-06-13/start-palestine).

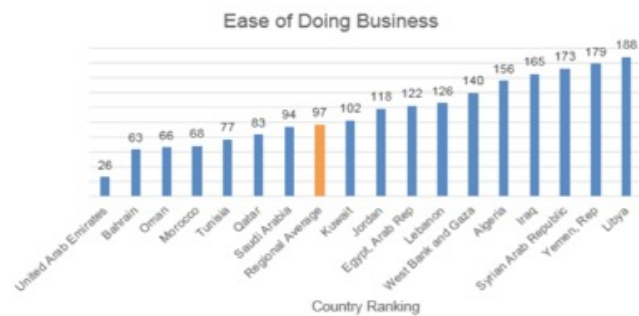
<sup>54</sup> "Accelerating Entrepreneurship in the Arab World," World Economic Forum and Booz & Company, (October 2011): 20, [http://www3.weforum.org/docs/WEF\\_YGL\\_AcceleratingEntrepreneurshipArabWorld\\_Report\\_2011.pdf](http://www3.weforum.org/docs/WEF_YGL_AcceleratingEntrepreneurshipArabWorld_Report_2011.pdf).

<sup>55</sup> Kraetsch, "Taking Stock of the Youth Challenge in the Middle East: New Data and New Questions."

<sup>56</sup> Greenwald "The Context for Social Entrepreneurship in the Middle East."

which is just being introduced to this type of business activity and a domestic institutional framework which is not yet equipped to accommodate it.

Often, prospective entrepreneurs find themselves facing a system which seems to make things unnecessarily difficult for them. As seen in the graph below, many countries in the region are exceptionally difficult to conduct business in. A higher numerical score on the index indicates a regulatory environment that is less conducive to business operation. The poor performance of MENA countries is due to the fact that they have neither the legal nor the institutional structure necessary to support social entrepreneurship. The high levels of bureaucracy, coupled with a lack of government and private support, creates unnecessary barriers for would-be entrepreneurs. This is an issue that must be remedied if the region's economies wish to take advantage of the clear entrepreneurial potential of their youth populations.



Source: World Bank Doing Business Report (2017)

Another major impediment to entrepreneurship in the MENA region is that many startups find it difficult to hire qualified employees. A Wharton School study found that, while many people saw startups as a good career move, few were willing to take the risk to work at one. One reason for this is that wages at a new startup are generally less than they might be at a larger and more established public or private sector corporation. While there is a general consensus that having a substantial portion of the population reliant on public sector employment is unsustainable, many people still prefer the relative security of a government job. It is also often difficult for entrepreneurs to know how to locate talent and thus there is often a disconnect between the employer and the potential employee.

## Factors Influencing Entrepreneurship

Promoting an environment which is conducive to the growth of social entrepreneurship should be a priority for both the state and civil society. As already noted, much of the private investment in the region has been in the United Arab Emirates which has the most-business friendly in the Arab world. Why has the UAE's experience not been replicated in other Arab Countries? In practice, it is not possible to apply a "one size fits all" model to the Arab world. Entrepreneurs and the startups that have created are extremely heterogeneous in nature and thus delineating specific ways to promote entrepreneurship can be an elusive task. That being said, there are general principles which can be pinpointed as ways to help entrepreneurs across the region. I've divided this section into three different parts, each focused on a specific factor: bureaucracy, the legal system, and civil society.

## The Legal System

The legal system in countries such as Egypt makes it difficult to develop a small business. According to a 2009 Gallup Poll, youth consider an excessively complicated bureaucracy to be the

greatest impediment to entrepreneurship in Egypt. The World Bank lists a slew of major impediments to the development of small businesses in Egypt. These include: macroeconomic instability, the operation of businesses in the large informal sector resulting in illegal competition, corruption, regulatory policy uncertainty, tax rates, cost of financing a business, tax administration, and labor regulations. To encourage youth entrepreneurship, the legal system relating to business enterprises in the MENA region must be reformed.

One very telling example of the issues with the legal system in the MENA region is the basic bankruptcy law just enacted by the Egyptian government.<sup>57</sup> Before 2018, Egypt had no such law, meaning that if a person started a business and failed, the entrepreneur would likely end up in debtor's prison. The lack of such a basic business law makes starting a business a much riskier venture and severely disincentivizes entrepreneurship. This legal impediment is especially important considering the fact that at least 30 percent percent of start-ups globally are forced to liquidate their assets and at least 70-80 percent fail to meet their projected return on investment.<sup>58</sup> Without a legal safety net which reduces the disincentives of failure, would-be entrepreneurs are increasingly unlikely to attempt to establish a startup. The new law was incentivized by Egypt's loan agreement with the IMF. In return for a 12-billion-dollar loan in 2016, the IMF demanded that Egypt make significant economic reforms. This type of pressure from international organizations can be invaluable in pressuring regimes into policy change and economic liberalization.

In many Arab countries, the legal system is outdated and has not kept up with the times, making it extremely difficult to engage in business activities which are common practice for startups elsewhere in the world, such as compensating employees with stock options.<sup>59</sup> Where they do exist, labor laws make it an arduous process to hire and fire employees- a necessary function of any business, especially one which is just establishing itself. For example, hiring a foreign-born employee, or contracting with a foreign firm, requires an immense amount of paperwork and jumping through a myriad of bureaucratic hoops. In addition to making it difficult to establish and operate a business, this type of legal framework incentivizes entrepreneurs to operate within the region's vast informal sector, where they can avoid these impediments - to the detriment of the economy as a whole.

A problem also exists when it comes to the enforcement of laws. Many Arab economies suffer from poor contract enforcement, an inability to obtain and follow up on government issued permits, and issues arising from cross-border trading.<sup>60</sup> Although there has been an effort to liberalize the regulatory environment for private enterprise, when those laws are not enforced, it is impossible to have real economic change. Part of the reason for this lack of enforcement is that many of the region's countries have an incentive to stipulate legal reform on paper, so that they

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<sup>57</sup> 14, مصراوي عيد " قانون الإفلاس يرى النور أخيراً.. ما أهميته للاقتصاد المصري؟". Jan. 2018,

[www.masrawy.com/news/news\\_economy/details/2018/1/14/1241597\](http://www.masrawy.com/news/news_economy/details/2018/1/14/1241597)

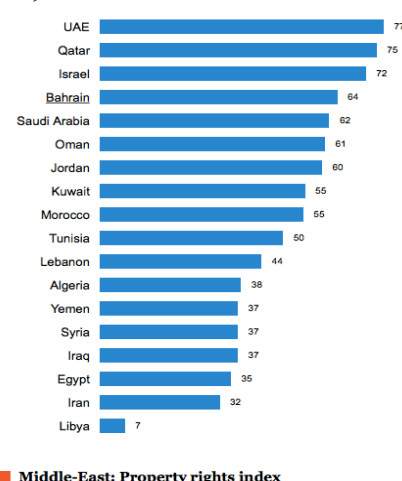
<sup>58</sup> Carmen Nobel, "Why Companies Fail-and How Their Founders Can Bounce Back." *HBS Working Knowledge*, Harvard Business School, March 7, 2011, [hbswk.hbs.edu/item/why-companies-failand-how-their-founders-can-bounce-back](https://hbswk.hbs.edu/item/why-companies-failand-how-their-founders-can-bounce-back).

<sup>59</sup> "Startups in the Arab World." *The Economist*, January 12, 2017, [www.economist.com/news/middle-east-and-africa/21714335-arab-entrepreneurs-could-help-many-regions-problems-too-many](http://www.economist.com/news/middle-east-and-africa/21714335-arab-entrepreneurs-could-help-many-regions-problems-too-many).

<sup>60</sup> "Business Reforms Pick Up in Middle East and North Africa, Despite Conflict, Says Doing Business Report," World Bank, October 27, 2015, <http://www.worldbank.org/en/news/press-release/2015/10/27/business-reforms-pick-up-in-middle-east-and-north-africa-despite-conflict-says-doing-business-report>.

appear to be modernizing in the eyes of the international community, without applying these laws and regulations in practice. When the existing legal infrastructure is not enforced, it becomes much harder to do business, especially for small and medium size enterprises which lack the resources and connections to overcome such obstacles. Therefore, another way that Arab states can encourage entrepreneurship and the creation of small businesses is by ensuring that the existing legal infrastructure is actually enforced for all businesses, regardless of their size. For this practice to take hold, it would have to come about as a result of either domestic pressure or pressure from international institutions, most likely as a precondition for loans and financial aid. Additionally, the international community, and especially international development organizations such as the IMF and World Bank, must continue to hold MENA region states accountable for the implementation of reforms.

Property rights, both intellectual and physical, are an essential component of an economic environment which incentivizes entrepreneurship. Without strong property rights, there is little incentive for potential small business owners to create and invest, as the threat of having their assets seized with little to no legal recourse to recover them always looms over their heads. As the chart to the right indicates, Arab countries where property rights are more secure, such as the UAE and other Gulf countries, are also the ones which offer the most secure business environment and consequently receive the vast majority of investment in their startup sector.<sup>61</sup> Stanford University points to the MENA region's lack of enforcement of property laws as one of the main reasons that entrepreneurship is significantly more difficult in the Middle East than it is in developed economies in other parts of the world.<sup>62</sup> Physical and intellectual property rights can only meaningfully exist in a context where the state is willing to enforce them and has the power to do so. There also has to be a meaningful commitment to the development of the private sector. Property rights cannot exist if the public sector is bloated or government entities have significant control over the economy and are willing to seize private property for their own gain.



Another legal obstacle to social entrepreneurship in the region is the business tax code. In countries with both for-profit and non-profit sectors, the tax burden is invariably different between the two. Since social entrepreneurs lie somewhere between the two business models, they are unable to function with the limitations placed on non-profit enterprises. They are forced to accommodate the for-profit level of taxation which in turn creates an environment in which it is much more difficult for them to be successful. Therefore, a more flexible tax code must be established, one which allows social entrepreneurs to take advantage of their ventures' social impact but taxes them at a fair rate.

In addition to tax codes, social entrepreneurial ventures generally follow the same regulatory laws as their purely for-profit counterparts. This status creates unique challenges for social enterprises which have a second and equally important goal of creating positive social change and thus may necessarily have to utilize a different business structure. Some countries with more

<sup>61</sup> Figure: <http://www.globalpropertyguide.com/Middle-East/property-rights-index>. Sourced from the Heritage Foundation and the WSJ

<sup>62</sup> Kathleen Bury, "What's Holding Back Entrepreneurs."



developed economies, such as the UK and France, are actually creating new legal codes for those ventures which seek both profit and to promote social advancement.<sup>63</sup> However, these options do not yet exist in the MENA region, where, as a result of decades of single party rule, civil society organizations were kept under a tight leash. Indeed, many countries don't even have distinct non-for-profit sectors. Even in Tunisia, which has perhaps the most robust civil society in the region, NGOs and non profits often face harassment by the state. This forces social entrepreneurs to adopt a legal structure that was developed for firms which only have a tangentially related purpose. Such a legal regime makes starting and running social entrepreneurial ventures to be much more difficult than a traditional for-profit business which does not have the dual mandate for social change. If MENA region states were to reform their business codes to be more accommodating towards entrepreneurs, especially social entrepreneurs, it would go a long way towards making entrepreneurship a more attractive option for the region's youth.

## Civil Society and the Private Sector

Financing and raising capital is seen by many would-be entrepreneurs as a major obstacle to establishing new ventures. The difficulty in gaining access to finance and investments is one of the main factors limiting the growth and development of entrepreneurship in the MENA region. Banks often see startups as too risky, making traditional loans difficult to obtain. Instead, most of the loans go primarily to the public sector and secondarily to large and established private firms, many of which have connections to the lender.<sup>64</sup> Furthermore, bank loans are often difficult for the region's young entrepreneurs to obtain because of the high interest rates and steep requirements for collateral which disadvantage younger bank clients.<sup>65</sup> A study conducted by the World Bank revealed that only about 8 percent of bank loans in the region have been allocated to SME's. This number is especially low in the Gulf states where, despite the friendlier regulatory environment, it is about 2 percent, and somewhat higher (but still worryingly low) in North Africa and the Levant where it hovers right around 13 percent. By comparison, the average middle-income country averages 16 percent, while high-income countries generally average 22 percent.<sup>66</sup> If the MENA region's governments incentivized banks to lend more to SME's, perhaps through some form of tax incentive or quota system, then obtaining the necessary financial capital to start a business could be significantly easier.

Crowdfunding and venture capital have only recently become an option and there are state-funded resources such as the Egyptian Social Fund for Development which was established in 1991 with a mandate to reduce poverty. Since then the Fund has disbursed about 2.5 billion dollars, much of it in the form of microloans and infrastructure development.<sup>67</sup> Such resources are available to

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<sup>63</sup> "Social Enterprise in Europe: Developing Legal Systems Which Support Social Enterprise Growth." *European Social Enterprise Law Association*, October 2015, 22-29, [esela.eu/wp-content/uploads/2015/11/legal\\_mapping\\_publication\\_051015\\_web.pdf](http://esela.eu/wp-content/uploads/2015/11/legal_mapping_publication_051015_web.pdf).

<sup>64</sup> Momani, "Entrepreneurship: An Engine for Job Creation."

<sup>65</sup> Ibid

<sup>66</sup> Roberto R.Rocha, Zsolia Arvai, Subika Farazi, "Financial access and stability: a road map for the Middle East and North Africa," (Washington, DC: World Bank, 2011): 105, <http://documents.worldbank.org/curated/en/343771468052798123/pdf/649370PUB0Fina00Box361550B00Public0.pdf>

<sup>67</sup> Hala Abou-Ali, et al. "Evaluating The Impact Of Egyptian Social Fund For Development Programs." *Policy Research Working Papers*, (July 2009): 2, doi:10.1596/1813-9450-4993

entrepreneurs but are increasingly difficult to access. Instead, many of the region's entrepreneurs rely on funding from international donors. The downside is that many of these grants are hyper-focused and earmarked for specific uses, making it difficult to raise the funds required for core operations and activities. Furthermore, this funding is often short-term, making long term planning and sustainable management difficult.

MENA states should create incentives for banks to provide a larger percentage of their loans to entrepreneurs, particularly those whose projects qualify as social entrepreneurship and would provide a net social benefit, distinct from those of the average business. For example, several years ago, Lebanon launched a four-hundred-million-dollar incentive package for just this purpose. This project, known as Circular 331 and sponsored by the Lebanese central bank, guarantees banks who loan money to startups a 75 percent reimbursement on their loan should the investment fail. Such a model could be applied in other MENA countries as well. States should also allow sources of venture capital and other alternative funding mechanisms to expand their work in the region.

As for the funding sources, it is important that they be willing to provide capital to a wide variety of projects. It is often easier for entrepreneurs engaging in specific sectors which are considered more profitable to find investment capital than it is for entrepreneurs engaging in less traditional businesses. For example, there is often much more funding available for high-tech startups than there are for startups in still important sectors such as manufacturing and agriculture. This is especially a problem for social entrepreneurs who, in order to affect their desired social impact, often pursue this type of non-traditional business model. Rather than just investing in one or two key industries or sectors, efforts should be made to deliver funding to ventures in what are considered less traditional sectors.

Where they exist, civil society organizations must make resources available to guide youth through the process of creating and registering their businesses. Additionally, more financing and development resources, such as startup accelerators, should be made widely known and easily available to entrepreneurs. In a survey of the region's youth, one of the main factors cited as preventing them from being able to open their own businesses was a lack of counseling and business information.<sup>68</sup> The availability and ease of access of these resources is essential to developing a healthy entrepreneurial environment.

Local private enterprise and civil society organizations should be encouraged to set up programs to foster entrepreneurship in the MENA region. Local organizations understand the regional political and economic environment and the difficulties that local entrepreneurs confront in a way that foreign based organizations are unable to comprehend. However, a majority of the major institutions supporting social entrepreneurs in the Middle East are based in Western countries. This support structure poses a number of obstacles for local entrepreneurs. For example, the application processes for these organizations often require proficiency in English, thereby excluding a significant proportion of the population and limiting the ability of these organizations to promote entrepreneurship among those who need their assistance the most.<sup>69</sup> Nevertheless, as already demonstrated, there is evidence of a growing number of grassroots social entrepreneurs in the Middle East, many of whom are supported by local civil society organizations and private startup

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<sup>68</sup> Bury, "What's Holding Back Entrepreneurs."

<sup>69</sup> Abdou, "SOCIAL ENTREPRENEURSHIP," 42

accelerators. This development is an encouraging trend in the region and demonstrates that social entrepreneurship is beginning to take root and carve out a place for itself in the MENA region's business environment.

One example of an organization that is focusing on planting the seeds of entrepreneurship as a method of promoting economic growth is the Syrian Economic Forum (SEF).<sup>70</sup> Of MENA region countries, Syria may be facing one of the most difficult roads ahead (second only to Yemen) in terms of revitalizing economic growth and catering to its large youth population. The SEF has partnered with local businessmen, as well as humanitarian organizations such as the IYD and the Assistance Coordination Unit, to work with both Syrians inside of the country and within the broader Syrian diaspora to provide young Syrians with the tools and skills necessary to be successful entrepreneurs within a post-conflict Syria.<sup>71</sup>

Aside from just technical training and funding, a concentrated effort should also be made by domestic and international investors to further develop the MENA region's human capital.<sup>72</sup> As mentioned earlier, the region's youth population is relatively well educated. That being said, the skillset needed to pursue entrepreneurship is often not received through formal education. Developing entrepreneurs' human capital involves not just training in the technical aspects of running a business or specific industries, but also developing leadership qualities and other essential interpersonal skills important for entrepreneurship. This type of human capital development provides a significantly potent advantage for regional entrepreneurs. For example, the Mowgli Foundation's mentoring program claims an 890 percent return on investment to their programs in the Middle East.<sup>73</sup>

## Bureaucracy

According to World Bank estimates, public sector bureaucracies in the MENA region are larger than anywhere else in the world. Some Arab countries employ up to 40 percent of the formal labor force.<sup>74</sup> Not only are these bureaucracies excessively large, they are notoriously inefficient, with many bureaucrats taking advantage of the lack of performance monitoring to do little or no work. This lack of monitoring is partially a result of the way public sector jobs are used to "buy off" the middle classes and reduce possibilities of political unrest and opposition. These jobs come with a high degree of job security and better benefits than employment in the private or informal sector. The state's political calculation is that, when you rely on the government for your income, you are less likely to oppose it. However, this policy results in a bloated and poorly functioning set of government institutions which impede the country's ability to develop. The bloated nature of the MENA region bureaucracies is so well-known and pervasive in the region that they often appear in pop-culture, such as the hit film "*al-Irhab wa-l-Kabab*" (*Terrorism and Kabab*), in which the protagonist

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<sup>70</sup> Moran, "Leveraging the Youth Bulge."

<sup>71</sup> "طردوس... هل هي العاصمة الاقتصادية القادمة؟" [www.syrianef.org/home/](http://www.syrianef.org/home/).

<sup>72</sup> Bury, "What's Holding Back Entrepreneurs"

<sup>73</sup> Ibid

<sup>74</sup> Lida Bteddini, "Governance and Public Sector Employment in the Middle East and North Africa," *Voices and Views: Middle East and North Africa*, September 21, 2012, [blogs.worldbank.org/arabvoices/governance-and-public-sector-employment-middle-east-and-north-africa](http://blogs.worldbank.org/arabvoices/governance-and-public-sector-employment-middle-east-and-north-africa).

finds it so impossible to complete the required government paperwork, that he unwittingly creates a hostage situation. To create a more hospitable business climate and encourage entrepreneurship in the region, excessive state bureaucracy needs to be pared down and streamlined to improve the business climate. Corruption, especially on the local administrative level in both urban and rural areas, must be combatted to ensure an even playing field and an efficiently functioning economy. Some MENA region states have already begun to enact such reforms. Egypt recently passed a set of laws which include public sector job announcements, and civil service tests, while Iraq has recently intensified efforts to weed out corruption in its bureaucratic ranks.



Additionally, the regulatory system needs to be reformed in order to encourage the formalization of businesses so that informal and illegal enterprises can become legitimate businesses and drivers of economic growth. One important step in this direction is to pare down excessive regulation. Excessive regulation of entry into the formal economy is associated with unofficial economies.<sup>75</sup> To avoid having to negotiate myriad regulations and bribes to register and operate their businesses, entrepreneurs are more likely to become part of the less regulated informal sector and only officially register their businesses when it becomes absolutely necessary.

The restrictive bureaucratic and regulatory environment present in many MENA region countries often make it difficult for entrepreneurial ventures to get started. Once they do become established, they still face challenges when it comes both to continuing business and scaling up. Excessive bureaucratic impediments means that even simple tasks can take years and likely involve mountains of paperwork. Even when that paperwork is completed, it is notoriously difficult to have the paperwork approved. Often the process requires bribery, intermediaries, or both. In Egypt, starting a business can require permits from up to seventy-eight different government agencies.<sup>76</sup> Even large companies find it difficult to navigate the vast bureaucracies of the MENA region. It took Uber, the ride-sharing giant, an extraordinarily long time to obtain the approval needed in order to become licensed to operate in Egypt, now one of its fastest growing markets. By comparison, in economies where there is a greater emphasis on encouraging entrepreneurship, registering a business is often as easy as submitting a form online.

Nor is the approval process for creating a new startup cheap. Even in the relatively business friendly Arab Gulf countries, it can cost between \$5,000 and \$15,000 to properly complete the process of formally registering a business.<sup>77</sup> Clearly this is an incredibly large sum, especially for the region's large cohort of unemployed youth. Additionally, governments often require that an

<sup>75</sup> Simeon Djankov, et al. "The New Comparative Economics." *Journal of Comparative Economics* 31, no. 4, (2003): 611, doi:10.1016/j.jce.2003.08.005.

<sup>76</sup> "Aiwa (Yes) Minister," *The Economist*, The Economist Newspaper, November 14, 2015, [www.economist.com/news/middle-east-and-africa/21678243-regions-countries-desperately-need-reform-their-public-sectors-aiwa-yes](http://www.economist.com/news/middle-east-and-africa/21678243-regions-countries-desperately-need-reform-their-public-sectors-aiwa-yes).

<sup>77</sup> Noor Sweid El-Solh, "Bureaucracy Is Stifling Small Business In The Middle East," *Forbes*, May 15, 2012, [www.forbes.com/sites/85broads/2012/05/14/government-fees-are-stifling-small-business-in-the-middle-east-and-north-africa/#3290177243d2](http://www.forbes.com/sites/85broads/2012/05/14/government-fees-are-stifling-small-business-in-the-middle-east-and-north-africa/#3290177243d2).

entrepreneur have a specified amount of shareholder capital before they will allow them to formally start a business. The required amount of money becomes an insurmountable obstacle for a large percentage of the region's potential entrepreneurs. For comparison, the average income per capita in Egypt is roughly \$3,500, in Tunisia it is \$3,700, while in Iraq it is \$4,600. In addition, yearly licensure fees of approximately \$10,000 are often required to keep a business registered. This is especially difficult for new businesses which are potentially unable to turn a profit in their first few years. In regions with more developed startup economies, such as Hong Kong, Australia, and Silicon Valley, these fees are closer to a few hundred dollars.

Additionally, Middle Eastern bureaucracies usually suffer from rampant corruption and crony capitalism. Large firms are able to leverage political ties with their respective governments to create situations which are favorable to them and to reduce competition, putting small and medium sized enterprises at a disadvantage. This power imbalance helps to explain why large enterprise only accounts for roughly 10 percent of all firms but 70 percent of all private sector employment in the region.<sup>78</sup> This in turn creates a situation where entrepreneurs who have yet to establish themselves and their businesses are unable to carve out a space in the market for themselves.

Streamlining the state bureaucracy can save entrepreneurs endless troubles and create an environment which is much friendlier to small business creation and social entrepreneurship. Nation-states in the MENA region should simplify registration procedures, perhaps by creating "one stop shops" where entrepreneurs are able to complete all registrations and other regulatory procedures in one office, rather than having to go through innumerable government agencies. States should also work to reduce expenses to levels similar to those countries which have more competitive business environments. Pressure from development agencies has succeeded in pushing through reforms in the recent past, and agencies like the International Monetary Fund could make such a fee structure incumbent on receiving a loan from the organization. Government jobs should be based on merit as opposed to political connections. Additionally, MENA region states must clamp down on corruption and institute performance reviews to ensure that public sector employees are both doing their jobs and doing them properly.

## Conclusion

While obviously not a panacea for the region's socio-economic struggles, social entrepreneurship can be very beneficial to the MENA region. It could potentially be a boon to the economies of the region and go a long way towards combatting their extraordinarily high youth unemployment rates. Numerous successful startups have demonstrated that many of the necessary conditions required for a successful culture of entrepreneurship already exist in the MENA region. However, the need to provide social entrepreneurs with the resources required to help them get them off the ground and for the region's states to create policies which foster entrepreneurship still remains.

In the long run, MENA region state must develop broader policies designed to encourage the formation of small businesses. Such policies would require reform of bureaucracies and legal

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<sup>78</sup> Sahar Nasr and Douglas Pearce, *SMEs for Job Creation in the Arab World: SME Access to Financial Services* (Washington, DC: World Bank, 2012), 5, <http://www.ifc.org/wps/wcm/connect/1115c70045539e51af04afc66d9c728b/SMEs+for+Job+Creation+in+the+Arab+World.pdf?MOD=AJPERES>

systems and an institutional shift on the part of both the public and private sectors which facilitated a more hospitable environment for entrepreneurship throughout the region. Implementing these reforms represents an incredibly complicated process as every country's economic and political situation is different. The resources and human capital available are varied and, as a result, the startup industries in each country will be different and have different needs. While it is impossible to create a "one size fits all" policy which applies to every country, I have identified certain problems which must be addressed if the economies of the MENA region are to experience economic growth. The state's failure to take entrepreneurship, especially among youth, threatens to further increase political turmoil in what is already the most unstable region of the world.



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