



ESCWA



Distr.
LIMITED
E/ESCWA/ECRI/2008/2
24 December 2008
ORIGINAL: ENGLISH

Economic and Social Commission for Western Asia (ESCWA)

REPORT

OF THE EXPERT GROUP MEETING ON STRENGTHENING PRIVATE SECTOR RESILIENCE UNDER CONFLICT: LESSONS LEARNED AND THE WAY FORWARD BEIRUT, 11-12 NOVEMBER 2008

Summary

The Economic and Social Commission for Western Asia (ESCWA) region continues to suffer from the backlash of conflict and political tension. This situation poses great challenges to ESCWA member countries as they strive to meet their development goals, including the challenges of unemployment and poverty.

The instability and protracted crises experienced in the Western Asia region call for development policies and interventions that are resilient to conflict and political tensions.

Strengthening the private sector and its capacity to operate, thrive and survive in conflict-affected countries is increasingly regarded as a potential driver for development, mainly due to the essential role played by the private sector in generating income, creating jobs and mitigating the impact of conflict on socio-economic development, as well as an effective tool for peacebuilding.

The Expert Group Meeting, organized by ESCWA in collaboration with the Lebanese Economic Association and Marker Global, tackled the issue of private sector resilience in the context of conditions faced by ESCWA member countries. The meeting also considered the viability of the private sector as an actor of development, the challenges facing the sector in the region and the financial and technical dimensions of private sector interventions in support of development objectives. A number of recommendations aimed at ensuring a greater role for the private sector in development efforts were formulated by the meeting.

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Introduction

1. The Economic and Social Commission for Western Asia (ESCWA) region continues to suffer from the backlash of conflict and political tension. This situation poses great challenges to ESCWA member countries as they strive to reach development goals, including the challenges of unemployment and poverty. The instability and protracted crises experienced in the Western Asia region call for development policies and interventions that are resilient to conflict and political tensions.
2. Such policies and interventions are urgently needed as disputes in the region have tended to spillover into other countries, creating negative socio-economic effects for the region as a whole.
3. Strengthening the private sector and its capacity to survive and operate in unstable and volatile national contexts is increasingly regarded as a potential driver for development, mainly because of the important role the private sector plays in generating income, creating jobs and mitigating the impact of conflict on socio-economic development, as well as an effective tool for peacebuilding.
4. This report takes stock of the presentations and deliberations of over 20 experts and decision makers who participated in an Expert Group Meeting on “Strengthening Private Sector Resilience under Conflict: Lessons Learned and the Way Forward”. The meeting was organized by ESCWA in collaboration with the Lebanese Economic Association and Marker Global.

I. THE PRIVATE SECTOR IN CONFLICT-AFFECTED COUNTRIES: AN AGENT OF DEVELOPMENT?

5. The Western Asia region has been beset by conflict and political instability in recent decades and has, on average, experienced a major war every 10 years. Numerous Arab-Israeli conflicts, the ongoing Palestinian crisis and three major wars in the Arab Gulf, have all negatively affected the development potential of the region. The Western Asia region is also subject to political tensions driven by local and international interests, the presence of numerous geographic flash points, and the scourge of terrorism and ethnic and sectarian tension which threaten the stability of a number of countries, if not the entire region.
6. National, political and socio-economic systems and local socio-economic performance have historically been weak in the Western Asia region. This is compounded by the absence of robust reform processes and competing international, regional and local interests. In consequence, the region has experienced an increase in illegal migration, capital flight, negative economic growth, burgeoning ethno-sectarian tensions and religious extremism. Remedies to address these problems have been few and far between and the scarce resources that could be used to address urgent development needs are being allocated to military and security budgets.
7. Conflict-affected countries in the region are characterized by, among others, centralized decision-making processes dominated by political and security considerations; inefficient public institutions and services; outdated administrative practices; and a dysfunctional relationship between the public sector and key stakeholders, for example the private sector. As a result, national political-economic systems are unable to address local political discord or socio-economic grievances, thereby increasing the likelihood of instability and even civil strife, which in turn feeds into negative socio-economic performance and exacerbates poverty and unemployment.
8. Regional conflict patterns have changed in recent years, and traditional forms of warfare have been replaced by protracted local conflicts. These conflicts pose formidable challenges to local populations as they go about trying to secure their livelihoods. In the light of these realities, there is an urgent need for development interventions that are resilient to conflict and political instability.

9. The potential role of the private sector as a vehicle for development, peacebuilding, conflict mitigation, promoting productivity, economic growth and job creation has received considerable attention in recent years. The private sector has a vested interest in maintaining security and the administrative efficiency of State institutions and public services, and is increasingly being seen as an important interlocutor by development actors because of its economic weight, influence and political contacts, as well as its abundant financial resources, skilled workforce and the pivotal link it provides between different levels of society.

10. Further analysis is needed on the contribution that the private sector can make to development in unstable contexts, as well as the potentially negative role that businesses can play in conflict settings. The political economy that emerges during periods of conflict or instability can sometimes benefit certain private sector actors; and some of those actors indulge in corruption and rent-seeking activities, and impede efforts to introduce greater transparency, accountability and good governance. In some conflict scenarios certain sections of the private sector have even gone so far as to act as spoilers in the peacebuilding process, derailing State consolidation, institution-building and socio-economic development initiatives. The private sector has also been known to finance certain conflicts. One example of the negative role that the private sector can play in conflict situations is illustrated in the case of the Lebanese civil war, where some business elites opted to postpone resolving outstanding political and economic challenges, which greatly weakened the State and eventually led to the outbreak of the conflict.

RESILIENT SECTORS

11. Some private sector activities can have a positive impact on conflicts, but can also be affected by them to different degrees. Strongly capitalized businesses with flexible management structures offering vital services are more resilient to the negative economic impact of conflict. Furthermore, small and medium-sized enterprises (SMEs), the self-employed and those who work from home, enjoy higher survival rates.

12. Enterprises active in telecommunications, food and other vital consumer products, banking and finance and in conflict-related sectors, such as arms manufacturing and security, have been the most resilient in conflict situations. For example, Iraqi engineers were able to rebuild the country's telecommunications network despite ongoing violence and the telecommunications sector now employs about 100,000 people. Between 2002 and 2007 market penetration rates in Iraq grew by 270 per cent, and by 2013 the country is expected to have one of the highest penetration rates among all emerging market countries. Another example is the banking sector in Palestine, where private sector deposits increased by 133 per cent to US\$ 2 billion between 1996 and 2000. The conservative lending policies adopted by banks in Palestine has resulted in non-performing loans representing only 9 per cent of assets; Palestinian banks have also experienced relatively low withdrawal rates, partly due to consumer confidence in the sector. Banks were able to show a degree of flexibility during periods of conflict by, among others, staying open for business when curfews were lifted. Banks in Lebanon also continued to service their clients during the 2006 Lebanese-Israeli war.

13. Among the sectors that struggle to survive during periods of conflict are the tourism, export/import, real estate and construction and non-vital consumer goods sectors. The survival rate of these sectors, however, greatly depends on a number of variables, such as location, incentives to take risks for profit, and the nature and intensity of the conflict. Human factors, such as the vital need to earn a living, also play an important role.

14. The informal sector plays a significant role in the economies of conflict-affected countries as it tends to perform better than the formal sector in crisis situations because of its greater flexibility and tendency to grow during conflicts. Between 1998 and 2005, the formal sector in Bosnia and Herzegovina employed 60,000 people, while the numbers of those employed in the informal sector increased from 200,000 to 500,000 over the same period. In many cases, the growth of the informal sector in conflict-affected

countries can represent the first step towards recovery, but this presents challenges to both socio-economic development and peace consolidation. However, the development of the informal sector is not entirely beneficial as it is poorly regulated and workers are poorly protected, have no job security, and can easily fall under the control of militias and criminal elements.

II. CHALLENGES FACING CONFLICT-AFFECTED COUNTRIES IN WESTERN ASIA

15. The private sector and, for that matter, most of the socio-economic structure in countries with abundant natural resources, such as Iraq and the Sudan, remain greatly dependent on oil and the State. In Iraq, efforts to introduce economic reforms aimed at creating a more conducive business environment and a more diversified economy are expected to take some time because of security considerations, the need for further reconciliation, weak State institutions, and the long history of the centrality of the State. In the Sudan, there is also a need to reduce reliance on public sector employment and explore the different avenues that exist for the private sector to accommodate the demand for jobs. Greater diversification away from resource-based economic sectors is also vital for further economic growth in the Sudan. Improving education and linking supply with demand in the job market are central issues that need to be tackled, particularly as better qualified and skilled human resources in the public and private sector would ultimately contribute to employment generation and poverty eradication.

16. In Palestine, the private sector is operating amidst a widespread economic crisis, resulting from the demolition of vital infrastructure and restrictions on the free movement of people and goods. The legal framework governing private sector operations in Palestine has yet to be finalized and this along with a weak judiciary, limited financial intermediation and a narrow range of enterprise support services place constraints on the capacity of the private sector to kick-start a stagnant economy.

17. Retention of investment is one of the key challenges facing the private sector in Palestine. Local and foreign investors in Palestine face a number of constraints, such as accessing raw materials; contracting overland transport services at reasonable prices; coping with customs and overland transport procedures; and the absence of dispute settlement mechanisms. Paradoxically, a majority of Palestinian enterprises stated that they were satisfied by the availability of external finance at reasonable terms; their principal concern revolved around ensuring that existing production levels could be maintained. The business development needs of investors included: access to external finance; training of local staff; good relations with the Government; ensuring further foreign direct investment (FDI) inflows; improving the quality of products; and increasing access to markets.

18. Investors in Palestine are also concerned about growth dynamics at the macro level; the absence of a well articulated development strategy; the weak legal framework; and inadequate trade-related infrastructure. An examination of the dynamics of Palestinian industry revealed that most enterprises belong to sectors with poor technological capacities, and that they lacked the required know-how to choose technologies, adapt imported technologies to local needs and assimilate more complex technologies through product development. However, the most persistent impediment to enterprise development was the preoccupation with survival and the distraction of having to focus on day-to-day problems, which left little time to explore longer term opportunities.

A. CORRUPTION

19. An important challenge facing the private sector in conflict-affected countries is the absence of good governance within the public sector. Although this phenomenon is not unique to the Western Asia region, corruption remains a widespread phenomenon and represents an obstacle to smooth business operations in the region. On average, 35 per cent of firms in developing countries pay bribes to facilitate business transactions.

20. It should be noted that corruption does not necessarily mean negative economic growth. High growth rates have been achieved in countries where corruption and bribery is known to take place within the public sector. However, the additional cost of doing business and the diversion of fiscal revenues has a negative effect on socio-economic development and the consolidation of peace. Corruption creates additional costs to doing business and bars many economic actors from entering the market and potentially contributes to income disparity and production distortion. In addition to paying bribes to facilitate transactions, some firms in the region evade taxes by paying bribes, which in turn leads to lower revenues to finance public sector reforms and marginalizes entrepreneurs who cannot afford pay-offs.

B. THE FINANCIAL SECTOR

21. The financial sector plays a critical role as a facilitator for private sector resilience, particularly in the light of the tremendous growth experienced by this sector in recent years. The rapid structural changes seen in global financial markets are providing considerable benefits to users of financial services as the cost of financial intermediation has fallen dramatically and also because it is now easier to manage and hedge financial risks.

22. Nonetheless, financial innovation has also produced new challenges, particularly as banks are increasingly dependent on capital markets and sustained market liquidity to hedge risks. This places additional pressure on the robustness of financial market infrastructure to handle large changes in trading volumes and to cope in periods of market turmoil and strain.

23. Greater integration of world capital markets means that a major financial problem is more likely to spread quickly across borders. A number of oil-rich countries in the ESCWA region have in recent months injected liquidity into the markets to counter the effects of the financial meltdown; however, it remains to be seen how this will affect their ability to pump much needed liquidity, not to mention aid, into conflict-affected countries. While the global financial turmoil has to date had little effect on the Middle East, overheating is still a major concern. Real gross domestic product (GDP) growth in Middle Eastern countries is projected to weaken modestly during 2008-2009, and fall from 6.5 per cent to 6 per cent (International Monetary Fund estimate). Inflation is soaring in different Arab countries, but sizeable FDI inflows are boosting activity.

24. Arab sovereign wealth funds are playing an increasingly important role in global financial markets and have grown by 24 per cent over the past five years (Global Insight, 2008). As of April 2008, the total assets held by Arab sovereign wealth funds exceeded US\$ 1 trillion, and are projected to reach US\$ 12 trillion by 2015 (Morgan Stanley, 3 May 2007). Arab sovereign wealth funds are exposed to companies and financial firms in the United States, and some of them invested more than US\$ 40 billion to bail out a number of foreign-based global financial banks during the subprime mortgage crisis in 2007 (Global Insight, 2008).

25. Islamic banking has assumed a prominent role in the world of finance and attracted a growing number of investors and clients. Islamic banking institutions have succeeded in establishing a presence in Lebanon and in a number of other Arab countries. One such institution, the Arab Finance House, managed to develop its activities in Lebanon because it was willing to take risks during periods of political instability.

III. RESPONDING TO CHALLENGES FACING THE PRIVATE SECTOR IN ADVERSE ENVIRONMENTS: FINANCIAL SCHEMES

26. The International Finance Cooperation (IFC) has developed a model for public-private partnerships (PPPs) that addresses development needs in conflict-affected settings. Countries experiencing conflicts are often plagued by weak Government control and rapidly changing security, political, social and business environments and have to face urgent humanitarian needs and resource constraints. As is often the case in such situations, the State and donors have many priorities and limited resources. The private sector is often more agile in such circumstances and can mobilize more rapidly, and in most cases is better equipped to

assess and address risk. Moreover, the private sector can be more cost efficient and manage resources more effectively.

27. Partnerships between the public and private sectors are aimed at delivering a project or service traditionally provided by the public sector. In this model the public sector specifies requirements and has oversight responsibilities over the project, while the private sector builds facilities and runs support services. In such partnerships, the private sector aims to both recuperate its investment and make a profit, while the State seeks to ensure that the private sector is not given any unfair advantages.

28. The IFC model seeks to capitalize on the efficiency gains arising from private sector participation. PPPs have positive aspects, namely that they are subject to a competitive process, they increase transparency, promote private sector efficiencies and innovation, incorporate well-designed risk allocation and transfer of project risk to the private sector, help to improve service levels and enhance revenues. Some of the negative perceptions of PPPs are that they are overly complex, have high transaction costs, that the cost of borrowing is higher than public financing, and that public assets are being controlled by the private sector.

29. PPPs are increasingly becoming more important in the light of the: (a) reduced availability of public funding due to deficits or prudent fiscal management; (b) reduced availability of private capital as investors are increasingly more risk averse and less willing to take risks in emerging markets; and (c) huge levels of financial resources needed for infrastructure, education and health care projects.

30. Conflict-affected economies can benefit more from PPPs because, unlike other countries, their basic and strategic infrastructure has to be repaired, Governments are burdened with huge fiscal burdens, their access to finance is reduced and they have important reconstruction and rehabilitation needs. In addressing these challenges, the IFC can assist in securing global resources to enable a quick recovery and encourage the private sector to enter these economies. Partnerships between the State and the private sector can result in greater expertise in managing infrastructure projects, access to finance and enhanced leverage of investments and work.

31. The Multilateral Investment Guarantee Agency (MIGA) is also structured to assist the private sector in responding to the challenges associated with conflict and instability. MIGA promotes FDI by providing non-commercial risk insurance (guarantees) for investors and lenders, dispute mediation services, assists in removing obstacles to current and future investment, and provides information on investment opportunities and operating conditions in developing countries.

32. MIGA's insurance coverage addresses currency transfer restriction and inconvertibility, expropriation, breaches of contract and business interruption. Significantly, MIGA's insurance coverage also includes protection against losses arising from damage or disappearance of tangible assets during revolutions, insurrections, coup d'états and acts of sabotage and terrorism. In order to be covered by MIGA's insurance coverage scheme, these acts must be intended to achieve political objectives.

33. An example of a local insurance coverage scheme is Kafalat, a Lebanese company that offers loan guarantees to SMEs in marginal areas of the country that are usually not targeted by commercial bank lending. Kafalat provides insurance coverage in a number of sectors such as agriculture, information technology, tourism and industry. In case of default, Kafalat covers up to 90 per cent of the amount of the loan owned to the bank. During the 2006 Lebanese-Israeli war, Kafalat supported SMEs by rescheduling debt and granting grace periods to private sector enterprises. The percentage of defaults has historically not exceeded 2-3 per cent of the total portfolio.

34. The economies of Lebanon and most non oil-producing countries in the region are closely tied to those of the GCC countries, which are in turn directly linked to global markets. Given these close links, the effects of the global financial crisis are expected to be significant on both oil and non-oil producing countries. Arab stock markets registered losses estimated at about US\$ 460 billion and declined by 35 per cent by October 2008. Significantly, the economies of non oil-producing countries in the region are directly linked to oil-producing countries.

35. Expatriate remittances represent a major source of funds in Lebanon and have contributed greatly to the resilience of the Lebanese economy over the past few decades. The flow of remittances into Lebanon and other countries are not tied to political risk; however, the global financial crisis is likely to result in reduced flows. In the case of Lebanon, remittances on average grew by 20 per cent between 2003 and 2007. Although remittances are expected to keep flowing, the financial crisis will undoubtedly lower remittance growth rates, which in turn will have an impact on economic activity in Lebanon and other countries in the region.

36. The financial situation in Iraq is marked by high capital outflows and availability of internal sources of finance, including microfinance programmes supported by the Ministry of Planning. The lack of investment and weakness of private sector enterprises is due to, among others, high interest rates and high inflation and not the lack of finance.

37. SMEs have a very important role to play in conflict-afflicted countries. In Iraq, further efforts need to be made to promote and support SMEs because of their operational flexibility and their capacity to absorb unemployment and fight inflation. SMEs would also benefit if they could have access to suitable financing mechanisms, such as microfinance.

38. The new Iraqi State has an important role to play in fostering a healthy and resilient private sector. It is the role of the State to guarantee peace and security, which are essential conditions for the development of the private sector, as well as to ensure that Iraqi citizens have opportunities to support themselves and their families. The State has an essential role to play in supporting the private sector. To this end, it needs to develop a clear framework and objectives and identify gaps or areas of improvement. Cooperation arrangements, such as PPPs, do not undermine the role of the State. On the contrary, they boost performance through enhanced efficiency. Regulatory authorities can provide useful support to the State in overseeing the implementation of PPPs and similar contracts. State intervention is necessary during crises and conflicts in order to provide guidance and support to the private sector, and further attention needs to be given such interventions in the region.

39. Not all crisis-affected countries face difficulties with regard to access to financial services. Access to funds is not a major problem for the private sector in Lebanon. Lending is estimated to comprise 120 per cent of GDP, a level comparable to rates in developed countries. Moreover, the financial sector has proved highly resilient during periods of political instability. In the Sudan, the United Nations Development Programme has managed projects for private sector financing, such as establishing a microfinance service in Darfur and other areas of the country and providing capacity-building programmes for entrepreneurs.

40. An unprecedented number of investors have withdrawn from stock markets. However, some argue that they could eventually return to emerging markets and the banking sector. The cost of future lending in the United States and other markets will undoubtedly increase to reflect a re-evaluation of risk. The financial crisis has negatively affected sovereign funds, investors and stock markets in many countries in the ESCWA region. On the positive side, countries such as Kuwait and the United Arab Emirates have introduced deposit guarantee schemes. In Lebanon, banks enjoy high levels of liquidity due to Central Bank regulations and policies. Islamic banks have an important market share in the region and enjoy high capitalization rates. However, the full impact of the liquidity crunch on the private sector in the region has yet to be fully felt and determined.

IV. RESPONDING TO THE CHALLENGES FACING THE PRIVATE SECTOR IN ADVERSE ENVIRONMENTS: TECHNICAL SUPPORT

41. Capacity-building is increasingly regarded as an important means to strengthen private sector development in the ESCWA region. However, such types of interventions suffer from several challenges and have to date been applied in a fragmented fashion, with no clear goals or defined set of priorities, and have not been accompanied by suitable quality assurance mechanisms and impact assessment.

42. Capacity-building programmes are normally structured in three distinct phases comprising: the design phase, which includes the assessment, beneficiary involvement and setting clear objectives and priorities; the implementation phase; and the evaluation and impact assessment phase. In general terms, capacity-building involves programme design and development, training and delivery modules, seminars, workshops, conferences, round-table discussions, field visits, organizational twinning, e-learning, knowledge portals and coaching and mentoring.

43. Tailored capacity-building interventions are thought to strengthen private sector resilience, which in turn leads to economic development. Economic development mitigates the impact of conflict, reduces the risk of a return to conflict, and creates a greater sense of well-being for all, especially among conflict-affected populations.

44. Different types of capacity-building programmes are implemented during conflicts and post-conflict settings. A comprehensive capacity-building programme in a post-conflict setting can comprise the following activities: strategic planning; leadership; organizational excellence; performance management; human resource development; public financial management; and the role of the public sector in economic development. In a conflict situation, the following focus areas or modules can be factored into a capacity-building programme after an assessment is made on the causes of conflict. These modules can include: crisis and uncertainty management; the factors which can lead to short-term successes, such as retention of investment; cash flow management and microfinance; effectiveness versus efficiency; necessary versus important skills.

45. Capacity-building components that focus on the public sector can include anti-corruption initiatives, management of public finances, decentralization, governance, human resources management, private sector development, legal and regulatory frameworks and conflict management.

46. Regular assessments of the impact of capacity-building modules are critical so that they can be improved and benefit from further development. The assessment could be conducted at three levels: the institutional/system level; the organizational level; and the individual level. Among the tools that can be used at the institutional level are field and stakeholder analysis and focus group discussions. Assessment tools at the organizational level include document analysis, regional development planning, focus group discussions, organizational capacity assessment tools, stakeholder analysis and SWOT analysis. At the individual level, assessment tools that could be deployed are task, job and training needs analysis and focus group discussions.

47. There are different types of capacity-building techniques and can consist of participant-centred (learning not teaching) techniques, experimental learning, lecturing, exercises and project based or centred on case studies and role-playing.

48. The combination of capacity-building, vocational training and micro-credit schemes could prove beneficial in efforts to initiate and strengthen private sector development in rural areas. The Association for Development of Rural Capacities has been active in similar capacity-building activities in southern Lebanon. The transparency it has adopted in its dealing with beneficiaries and donors and its political independence have played a large role in its success. It is worth noting that only 1 per cent of beneficiaries have defaulted on their loans.

49. Another non-governmental and non-profit organization engaged in promoting entrepreneurship in Lebanon is Bader. Established in late 2005 following an initiative sponsored by 40 young Lebanese business leaders, Bader seeks to fulfil its objectives through education, finance and networking. The education component of Bader initiatives focuses on promoting entrepreneurship education among young adults. The networking component seeks to develop networking opportunities within Lebanon and the Lebanese diaspora in order to facilitate the development of new businesses (start-ups) and SMEs. The financial component aims to facilitate access to capital for these types of enterprises through the development of

finance-oriented projects. The economic sectors targeted by Bader are the services and technology sectors and innovative business categories.

V. RECOMMENDATIONS

- *Reformed and improved public service delivery are essential as inefficient, tedious administrative processes, corruption and bribery are obstacles to private sector resilience.*

50. Increased public sector wages and corporate tax regimes could play an important role in limiting corruption. There is a desperate need for institutional reforms that increase the efficiency and accountability of the public sector, as well as the introduction of incentive pay and other benefits for public servants in order to limit their dependency on bribes to make ends meet.

51. Inefficient and overly burdensome administrative procedures increase the cost of doing business and increase the potential for corruption. Administrative procedures could be streamlined and long and tedious bureaucratic procedures curtailed. An online ‘one-stop shop’ is an initiative that merits consideration as it would minimize the time, cost and effort needed by a business to receive public services and meet the required conditions or regulations set by the State. By decreasing the cost of doing business, business regulation reforms would make a positive contribution to the creation of new employment opportunities and attract investments for new businesses and other enterprises.

52. The process of starting up a new business needs to be inexpensive and formalities and capital requirements kept to a minimum in order to create a conducive business environment. Compliance regulations for business operations need to be straightforward and inexpensive; labour laws should not discourage hiring of foreign personnel; customs formalities should be inexpensive and swift; and liquidating a business should be a simple and straightforward matter. The provision of financial instruments to assist in times of crisis is also significant.

- *The challenge facing the Arab financial sector is to sustain resilience through the introduction of macroeconomic policies aimed at controlling inflationary pressures and maintaining economic growth.*

53. Policy recommendations to increase the resilience of Arab Banks in times of crisis include adherence to sound banking practices, starting from the initial encounter with the client (depositor/borrower) to the risk management operations covering the bank’s overall portfolio. The disparity between the short-term nature of liabilities and the long-term nature of assets needs to be carefully managed. Risk management is effective in the presence of efficient money and capital markets and liquidity buffers.

54. The financial sector will continue to play an essential role in supporting the resilience of the private sector. Islamic finance has the potential of becoming an important form of financing because of its high levels of capitalization and immunity to the financial crisis.

- *Strengthening educational systems and addressing the mismatch between education and skills needed on the labour market are necessary to mitigate the impact of conflict on socio-economic development and strengthen private sector resilience.*

55. There is a growing need to make further investments to develop human resources in the region, particularly in conflict-affected countries. Staff with greater skills and training would allow the public and private sectors to improve their capacities/performance and enable them to better address the challenges associated with conflict and instability.

- *Investment retention in crisis-afflicted countries needs to become a priority in countries suffering from conflict and instability.*

56. Addressing the challenge of investment retention will require tailored solutions which take into account the distinctive features and institutional set-up of private and public sector enterprises working in countries experiencing conflicts or occupation.

57. An integrated approach needs to be adopted in order to create synergies between emergency interventions and long-term development objectives, as well as a focus on priority sectors within specific localities and on the growth dynamics of investors.

58. A three-track interactive approach, which sets targets for priority and promising sectors, may be considered. Such an approach would aim to generate additional capital investments from existing enterprises in order to bring local enterprises up to international standards, particularly in terms of product quality and ensure the widest possible spin-off benefits from FDI.

59. An integrated approach to investment retention is highly recommended in conflict situations. This approach should not only seek to embed transnational companies in the host country's economy, but also work in favour of national investors. Aftercare promotes business/investment retention and expansion to generate employment and output and indirect benefits through multiplier effects and spin-off benefits, such as local procurement and enhancement of local skills.

60. Among the specific objectives of an integrated approach to investment retention targeting the industrial level are: improved access to finance for local enterprises to access finance; promotion of laws and policies conducive to investment retention and attraction; and industrial development focusing on existing SME support programmes and initiatives, facilitating access to such programmes, and creating a coalition among enterprises to sustain long-term economic development efforts. Enterprise-level objectives could include enhancing technological capabilities, promoting access to export markets and supply sources, and fostering enterprise competitiveness.

61. Strategic components could be integrated into the work programme of an investment promotion agency in order to ensure sustainability. The Palestinian Investment Promotion Agency (PIPA) could adopt a similar approach, including the following functions:

(a) *Investor aftercare services*: PIPA could launch new services, such as sectoral-geographic clustering, networking among enterprises and linkage programmes with regional and global transnational corporations;

(b) *Policy advocacy*: PIPA could expand the scope of its lobbying efforts to promote the development of a legal framework for investment, skills development and creative solutions for financial intermediation;

(c) *Investment attraction*: PIPA may consider refocusing its investment promotion activities to seek FDI inflows from particular countries and transnational corporations.

- *Capacity-building interventions can strengthen the public sector's capacity to support private sector resilience in crisis-affected countries.*

62. Tailored capacity-building interventions to strengthen the public sector's performance are an important tool to consider. The success or impact of any capacity-building intervention will greatly depend on clear goals such as: Government legitimacy; employment generation; tackling the root causes of the conflict; and stabilizing the economy and positioning it for growth. Sensitivity to the context in which the capacity-building modules are to be conducted, notably the nature of the conflict and the country's level of development, is also crucial. It is also important that the host country should have full ownership and that the goals that have been set are realistic.

- *Interventions deploying a combination of capacity-building, vocational training and microcredit schemes are recommended for start-ups and young entrepreneurs.*

63. The success of such interventions greatly depend on: (a) choosing clients carefully, through interviews and the conduct of family-link cash assessments; (b) monitoring and training of beneficiaries; and (c) group pressure through municipalities.

64. When targeting young entrepreneurs, this strategy needs to be accompanied by a combination of education, finance and networking schemes to better equip beneficiaries.

- *A comprehensive study on strengthening private sector resilience in crisis-affected countries is required as a stepping stone for the formulation of suitable policies and implementation of impact-driven interventions.*

65. A comprehensive study on strengthening private sector resilience in conflict-affected countries is timely and important. The study should appraise the challenges facing the private sector in these countries, examine survival strategies, map existing weaknesses within the public and private sectors, and attempt to propose mitigation strategies and interventions by transnational corporations and Governments. The study should draw on best practices from around the world and expertise accumulated within the region.

Annex*

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