

# Markets Integration and Innovation in the Mediterranean Region

ANDREA GALLINA\*

JEL classification: O140, P520

## 1. Introduction<sup>1</sup>

In 1995 the European Union (EU) launched a new political and economic partnership with its Mediterranean neighbours based on a three-points program of (i) policy and security, (ii) economy and finance, (iii) social, cultural and human affairs. In particular, the establishment of a free trade area (FTA) in 2010, gradually to encompass all sectors, has given rise to a lively debate among academics and policy makers about the impact that the liberalisation process can have on the economies of both shores<sup>2</sup>. Many claim that both groups of countries, the EU and the Mediterranean Partner Countries (MPCs) that signed the agreement, will face difficulties in adapting to the new regime. Specifically, it has been pointed out that: the EU members will suffer most from liberalisation because of the comparative advantages enjoyed by the Mediterranean countries in the agricultural sector; while for the MPCs the free entry of European industrial products will undermine the fragile but consistent manufacturing sector<sup>3</sup>. Integration may, thus, partly reactivate the process of a "natural" specialisation in countries, and agglomeration economies cannot be excluded. However, beside the positive effects produced by the growth of two-way trade, and especially the expected industrial links between the European and the Mediterranean enterprises, a number of problems arise. During the transition period the Mediterranean would have a dramatic fiscal loss from

## Abstract

The Euro-Mediterranean Partnership envisages the liberalisation of trade between the 12 Mediterranean Partners and the European Union member countries in 2010. While liberalisation in the agricultural sector should benefit the Mediterranean Partners, the abolition of tariff on imports of manufacturing goods from the European Union will pose stresses to both welfare policies, due to the reduction of tariff revenues, and to the fragile but consistent manufacturing sector. The paper aims to provide an overall picture of the limits and potentialities that the Euro-Mediterranean Partnership presents for the co-development of the MPCs productive structures. The paper concludes that the dynamic benefits from markets integration, namely technological change and innovation, can be achieved by the creation of learning and innovative environments that are bounded to the local socio-economic structures and markets.

## Résumé

*Le partenariat euro-méditerranéen prévoit la libéralisation du commerce entre 12 partenaires méditerranéens et les pays membres de l'Union européenne à l'horizon 2010. Alors que la libéralisation dans le secteur agricole bénéficierait les partenaires méditerranéens, l'abolition des tarifs sur les importations des biens manufacturés de l'Union européenne exercera des pressions tant sur les politiques de bien-être, suite à la réduction des recettes tarifaires, que sur le secteur manufacturier fragile mais important. Ce travail vise à fournir un tableau général des limites et des potentialités que le partenariat euro-méditerranéen présente pour le développement des structures productives des PMP. Ce travail conclut que les bénéfices dynamiques résultant de l'intégration des marchés, à savoir le changement et l'innovation technologique, peuvent être réalisés par la création de milieux novateurs et d'apprentissage qui sont limités aux structures et aux marchés socio-économiques locaux.*

lost tariff revenues. For example, it has been pointed out that in Morocco by the end of the transition, this will total more than 13 percent of the budget revenues, equivalent to more than 3 percent of Gross Domestic Product, and for Tunisia it is estimated that as much as 68 percent of trade taxes will be lost, amounting to a loss of total government revenues of nearly a fifth.

Thus there are several unanswered questions about what will be the actual welfare gain and loss in the process of markets' integration, while maintaining the other two objectives of security and social development. If the positive and negative static effects

of trade creation and diversion in the short, medium-terms can be assessed with current statistical methods, the dynamic effects on the production systems are not easy to

<sup>1</sup> The author is particularly grateful to the participants in the Workshop on Innovation and Exports from SMEs in Developing Countries, held at the University of Molise, Italy, the 22-24 of March 2001 for their helpful comments, to Sergio Gomez y Paloma for the comments on a previous draft of the paper, and to Bruno Amoroso, President of the Federico Caffè Centre, for his patience in discussing the issues tackled in the paper. The usual disclaimers apply. A previous version of this paper has been published as ERF Working Paper nr. 0106.

<sup>2</sup> The work of the Femise Network, coordinated by J. Luis Reiffers of the Institut de la Méditerranée and Heba Handoussa of the Economic Research Forum (ERF), is providing a continuous monitoring of the economic implications of the free trade area.

<sup>3</sup> For example, the OECD estimated that 60 percent of industrial firms in Morocco and Tunisia would not survive against freely imported European products, OECD, 1997.

<sup>4</sup> Economic Research Forum, 1997, pp. 38-39, in Holland, 2001.

\* Dept. of Social Sciences, Roskilde University, Denmark and Director, Federico Caffè Centre, Roskilde University, Denmark

spot. This is also due to the fact that there is a lack of systematic knowledge of the productive structures, particularly of the MPCs and especially of the manufacturing sector. This paper attempts to contribute to the study of the implications of the Euro-Mediterranean Partnership (EMP) on the Mediterranean contemporary manufacturing system, presenting the results of the surveys carried out by the author during the last three years.<sup>5</sup> The implications of the EMP on the agricultural sector have been published in this journal in 1998.<sup>6</sup>

The research has focused on ten countries<sup>7</sup> highlighting the needs, challenges, and potentialities for the development of the small and medium sized enterprises (SMEs) and micro and family enterprises (MFEs) sectors. In particular, in the light of the process of integration with the EU market, the research was driven by the question about what avenues the modernisation of the MPCs' production should take to co-evolve and co-develop, given the existing structures. Thus, I first attempted to draw a picture of the organisational and productive structures of the manufacturing sector. This has produced a taxonomy of the Mediterranean SMEs and MFEs sector (see Table 1). Then, I analysed the needs and potentialities of the firms, looking at their technical and technological capabilities and their relationship with the markets. This was done through in-depth personal interviews with entrepreneurs and with international and local small enterprises' development experts.

Three assumptions placed the research focus on the manufacturing sector: firstly, in the regions' diversified group of economies (non-oil countries) traditional consumer goods industries are still dominant. Secondly, the capacity of the agricultural and petroleum sectors in terms of job creation is very limited, while the manufacturing sector increasingly absorbs jobs. Finally, there is a constant increase of the contribution to Gross Domestic Product and employment by the informal sector.<sup>8</sup>

The paper is organised as follows. Section two presents

the conceptual frame used to explain markets integration and modernisation. Then the analysis of the contemporary manufacturing production systems in the Mediterranean countries and their problems are presented. The paper goes on to discuss the role of innovation in this type of production system as a strategy for co-evolution and co-development. The last section draws some conclusions and proposals for future research.

## 2. The experiences of market integration and modernisation

The assumption made by the supporters of free trade that the abolition of trade barriers will enable the automatic integration of markets and productions through higher rates of innovation following the introduction of newer technologies has been proved to be incorrect.<sup>9</sup> The evidence shows that even in very integrated national or regional markets, the expected process of convergence towards "best practice techniques" and the elimination of regional disparities did not occur. As pointed out by Ernst et al. (2001) the internationalisation of markets has not led to "the wonderland of a borderless world, where capital, knowledge and other resources move freely around the globe, acting as a powerful force of equalization".<sup>10</sup> In practice, the situation is more complex, and the structural differences between sectors and countries, on both the technological and infrastructural playgrounds, can play the opposite role of worsening the existing asymmetries in the distribution of welfare. A similar problematic is depicted by the differentials in the stages of development between the regions of the European 'Banana' and the Southern European regions, despite the enormous amount of structural funds injected for decades, and the existence of a well-functioning common market.<sup>11</sup>

The discussion on the Euro-Mediterranean meso-regional project generally lacks reference to previous historical experiences of market modernisation and integration. A reference would have helped to sort out an atti-

<sup>5</sup> The research project on the "Mediterranean Economies: old and new local production systems" has been coordinated by the Federico Caffè Centre at the Department of Social Sciences of Roskilde University, with the financial support of the Italian Economic and Social Committee (CNEL). The research on the Mediterranean manufacturing sector and the Euro-Mediterranean Partnership has produced two reports, one published by CNEL in 1999 and in 2001.

<sup>6</sup> Cf. Gallina, 1998.

<sup>7</sup> The Mediterranean Partners of the Barcelona Conference are, from West to East: Morocco, Algeria, Tunisia, Malta, Egypt, Israel, Jordan, Palestinian Territories, Lebanon, Syrian Arab Republic, Cyprus and Turkey. In the research project, Malta and Cyprus have not been included.

<sup>8</sup> ERF, 2000.

<sup>9</sup> On a critic on openness and export oriented strategies see for example Rodrik D., 1999. Even enthusiastic neoclassic economists after complex econometric analysis conclude saying: "However one should put less faith on the absolute magnitude of the effect of openness on growth derived from the regression model than on the direction of the impact because the robustness of the model requires more thorough examination. In addition, there may be two-way causality between openness and economic growth. Therefore, more detailed study is warranted on the timing of economic policies and the subsequent growth performance of individual countries. Further research is also warranted to examine the effect of openness on the dispersion of income across countries and over time". In Hui Pan, 1999, p. 118.

<sup>10</sup> Ernst et al., 2001.

<sup>11</sup> As pointed out by Triulzi, 1999, "[...] despite the important sums invested in these areas, it seems that neither corrective redistribution policies nor efforts to move production activities from north to south or to direct part of the production structure of the south towards the markets of the north have produced significant results", p. 226.

tude that considers market and integration as technical matter of financing, rules and prices. This lack is even more serious when we are dealing with different markets, and not only diversity in markets terms but in historical and cultural terms (Amoroso and Gallina, 2000). For example, during the process of formation of national markets in Europe during last century: Integration has succeeded where cultural differences were small or the resistance to modernisation could be brought down by "cultural revolutions". Nevertheless, these operations were not always successful as shown by the cases of Italy, Spain, Great Britain, etc. After more than a century and, despite the various efforts, regional disparities and different markets still exist in these countries.

The European Union should also reflect on its own experiences. Regional and national disparities within the EU remain high and the strengthening of the EU market competitiveness in the context of globalisation has rather increased than weakened problems like regional disparities and poverty. The case of Germany, where all the "obstacles" to integration were removed and no means were saved in the re-unification effort, is there to show that markets might be more than numbers and money.

From a political economy point of view, it is clear that the problem is neither to work out a self-centred development model based on import substitution and high protective barriers, nor to create a strong export-led sector. The problem is rather to create a sound domestic base for the national economy that is able to achieve a good quality and productivity level and to participate in some sector of the international division of labour. The main exports' gain must be used to extend and improve the domestic market. To imagine the increase of exports on the cost of the domestic market would be to upturn aims and means (Amoroso and Gallina 2000).

The analysis of the "diversities", in the sense of how production systems are organised, the influence of cultural bounds on consumption patterns and institutional setups, and the diversities in the social needs of communities, pose the stress on the need to have a different approach to markets integration and innovation. The economic policies and measures advocated by the "polycentric model"<sup>12</sup> respond to this need. Two main considerations are at the base of the feasibility of such approach: on the one hand, integration between areas with marked socioeconomic gaps needs to have transitory regulatory frameworks enabling an appropriate "mise-à-niveau" of the economic sectors within which integration will occur. The process of upgrading should involve not only the modern and fast growing sectors but it should take into account the existing production systems and their level of embeddedness in the local socio-economic fabric. Therefore innovation and transformation of production systems, both industrial and agricultural, should be gradual and contextual. On the other hand, social and macroeconomic considerations

should be introduced in order to avoid de-stabilising effects, while a path of growth that is based on the gradual adaptation of society and markets to the different context should be set-up. This requires an institutional building that overcomes the national boundaries and is instead oriented towards a meso-regional dimension. Again, the case of some South-South recent regional integration agreements, such as for example the Arab Maghreb Union, should be looked carefully from this perspective.

### 3. Markets and productive structures in the Mediterranean

So far, the Euro-Med Partnership is limited to the liberalisation of North-South trade flows, especially due to the technical problems of rules of origin that could emerge if South-South trade is liberalised. Most important is the acknowledgement that, due to the socioeconomic situation in the South, integration policies cannot be limited to trade policies. In fact, the abolition of tariffs can have negative effects if the productive structures are not supported to co-evolve and co-develop taking into account that the construction of local productive systems and markets are a necessary prerequisite to a more independent insertion in the international markets. The existing differences within the MPCs could be exploited for the creation of a south-south integrated regional market, which should be complementary to the Euro-Mediterranean FTA. This aspect does not receive much consideration in the Partnership and it represents, in fact, the Achilles' heel of the project.

Considering also that the circulation of labour between the EU and the MPCs is increasingly restricted, and that the proportion of the population under fifteen will shrink in the next 10-15 years -meaning that the proportion of the population of working age will grow more rapidly than the total population-job creation is dramatically needed. Over the next forty years, the North African countries will need to create about 100 million jobs just to maintain the present hardly tolerable ratio of unemployment and under-employment.<sup>13</sup> With these conditions, it is difficult to imagine that the expected liberalisation of trade, and the consequent specialisation and technological spill-over effects, will be able to face this need. Furthermore, the structural adjustment measures introduced some years ago in many MPCs have reduced the purchasing power of the population, increased social inequality and poverty. This has resulted in increased social tension in several states of the region, notably Egypt, Morocco and Jordan.<sup>14</sup> The shrinkage in private consumption affected also the volume of local demand, while at the same time the given preference to the upgrading of modern

<sup>12</sup> Amoroso et al., 1993, pp. 20-24; Amoroso, 1995, pp. 17-33; Amoroso 1998, pp. 130-150.

<sup>13</sup> Amoroso, 1996, Part IV; Romero, p. 9, in Holland, 2001.

<sup>14</sup> George S., 1996.



suppliers, generally controlled by foreign capitals, forced production to deflect towards different markets leaving local markets with lower quality products or without products. This trend is strictly related to the type of economic policy that should be applied within the general process of internationalisation of the economy. And, in particular if openness should give priority to imports of capital goods and technology or to the creation of an export-led economy. At the present, the analysis of Chevalier and Freudenberg shows that the composition of imports from the EU is increasingly made up of consumption goods, which in turn will put increasing competitive pressure on the local industries during the initial stages of complete liberalisation.<sup>15</sup> The effect of the adjustments are also shown by the striking increase in employment in the informal sector in MPCs.<sup>16</sup> Less institutionalised forms of markets are emerging, despite the attempt of the authorities to reduce the black economy. This phenomenon shows both the existence of increasing demand for goods from lower segments and an enormous amount of under-employed labour force.

The local demand for goods and services is supplied by an underwood of micro and family enterprises (MFEs), which are family based and with low ratio of capital investment.<sup>17</sup> They represent not only a productive structure but also a social system whose reproduction is based on a fragile interconnection of social practices, cultural values, and power structures. Markets are shaped like the traditional Souq, where purchasing, selling, production and consumption are social and socialising functions, strongly influenced by family and interpersonal relationships often based on the belonging to ethnic groups. This means that opportunistic behaviour is limited and information about prices and quality is generalised. Thus, demand and production are strongly connected and shape each other.

These elements depict a complex picture of the economies of the southern Mediterranean countries that is impossible to ignore. Local suppliers and local markets do not represent a romantic vision but an important source of income and stability. The growth of working population, and thus of migrants, places the stress on the importance of local production systems and markets. Due to their structural characteristics, the combined effect of the structural adjustments and the uncontrolled liberalisation of EU imports will pose a serious obstacle to the MPCs' markets and production systems endogenous development. Besides, the tools for establishing an incisive inter-industry co-operation, enabling a gradual modernisation of the manufacturing sector of MPCs, are still weak.

A closer look to the structural characteristics of the sector that will be most exposed to the process of liberalisation will enable us to understand the areas in which a sustainable development framework for the north-south co-operation policies in the field of innovation can be established.

## 4. Contemporary Mediterranean Manufacturing Systems

The choice to study the needs and the role of small enterprises was based on the fact that in the Mediterranean they represent the production base on which social and economic stability depends. In fact, despite the weakness of the statistical indicators, it has been highlighted in various fora that the relationship existing between employment and SMEs is so deep that their role can be considered strategic. The statistics available in each country show that the manufacturing firms with less than ten employees account for: in Egypt 95 percent, in Jordan 93 percent, in Lebanon 88 percent, in the Occupied Territories of the West Bank and Gaza 89 percent, in Tunisia 42 percent, and in Morocco and Israel 50 percent of the total industrial units. Their contribution to the employment varies between 20 and 45 percent and between 10 to 25 percent to the Gross Domestic Product.<sup>18</sup>

The economic structure of MPCs presents a scarcity of large enterprises and they have a different nature compared to the European, due to the fact that the national bourgeoisie has played a modest role in the economic life of Mediterranean countries. This role has been replaced by the military economic apparatus, a heavy public sector and by few large transnational corporations. Today, the reduction of the public sector, with its role of jobs and income creator, has resulted in an increasing amount of self-employment in the region. This, as already pointed out by Pietrobelli and Rabellotti, can be the result of both the fact that there are not better opportunities or because 'own-account' employment is preferred to wage jobs.<sup>19</sup> Thus, SMEs are not just a sponge with which to soak up unemployment, they can be also very dynamic; although detailed in-depth research is needed to identify the potentials of the newly established firms. This is to say that the sector in question is very heterogeneous and that its growth in term of capital accumulation and investment is linked not only to its micro dynamic but also to the evolution of the macroeconomic setting.

### *Small enterprises in the MPCs: a qualitative study*<sup>20</sup>

Qualitative interviews to entrepreneurs, and to privileged informants in the ministries of industries and planning and in the international organisations offices in the countries surveyed, have been conducted during the peri-

<sup>15</sup> Chevalier A. and M. Freudenberg, 1999, p. 4.

<sup>16</sup> Economic Research Forum, 1998, p. 133.

<sup>17</sup> Amoroso B., 1999; Gallina A., 1999.

<sup>18</sup> The figures are taken from Amoroso and Gallina, 2001, p. 42. Data are elaborated by the authors from the national statistics, such as the industrial census, and from ERF, 1999.

<sup>19</sup> Rabellotti R. and C. Pietrobelli, 1999, p. 17-18.

<sup>20</sup> This section is based on the documentation and interviews carried out by the author during fieldwork in various countries of the Mediterranean region in the past 3 years.

od 1998-2001. The field research has provided the material for the description and analysis of the difficulties and potentialities for the development of the small and medium-sized enterprises sector of the Mediterranean region. From the surveys, it has emerged that SMEs can be divided into three main categories: retailing, services providers to other enterprises, manufacturing. It is in particular on the latter that we concentrated our attention. Within the manufacturing sector the concentration of SMEs is stronger in the traditional sectors, such as textiles, wearing apparel, agri-food, leather and shoes, wooden furniture and articles, etc. The characteristics that they have in common are the low level of capital investment, the use of family manpower, informal credit, use of low technology, a family-based management, and low intra-firm division of labour. Very often these enterprises are organised in clusters diffused in the urban and peri-urban areas. At first sight, the level of specialisation is very low, firms producing the same finished goods for the same market, but each product is personalised for each different customer. Therefore, competition-with-the-neighbour is not a major threat, and proximity instead means exchange of know-how and information about markets, prices and new technology in a complete "shared knowledge environment".<sup>21</sup> In Amman Downtown, a small cluster of 12 firms producing furniture purchase wood together in order to obtain a better deal with the importer. Therefore information about the quality and the price of the raw material is shared. A similar thing happens in the cluster of furniture producers in the industrial city of Dawra, Beirut. When not in use, the owner of a particular cutting machine put it at disposal of the other producers, teaching them how to use it and thus spreading out technical knowledge in the cluster. Sharing of information and co-operation among producers can take place also in more organised settings. In the Artisan Village of Sale, Rabat, the pottery producers are organised in an association who has the main role of informing about raw material prices, international standards and markets, and new technology development, especially about the ovens for cooking the clay. The presence of developed close personal relationships among producers and between them and the customers contribute to the creation of "social capital" (in the sense of Putnam, 1993) and to the sharing of specific technical knowledge.

On the employment side, more attention should be paid to the fact that SMEs and MFEs are not only the owner/entrepreneur but they are made of artisans, wage employees and apprentices. For example, the often-neglected fact that they employ youngsters, orphans and students as trainees provides an important opportunity for them to learn a profession and have a little income. The firms' owners claims that the attempts of the government to regulate the training and the social security of the

workers hinder their activities putting other burdens on the already fragile existence.

On the production side, throughout the entire region, the SMEs and the MFE is a workshop of limited dimension, localised on the streets or inside apartments with crowded production chains and little and old equipment. The machines used are in fact simple; even though some of them have been used for more than fifty years they still provide the necessary work. Most of the production in the traditional sectors is labour intensive and the specific operation for which the machines are used, such as cutting wood and metal or sewing, are very simple. According to the sector and the type of firm the output obtained can be either that typical of the craft production (with a lower level of standardisation), or mass-produced for a contractor.

This important type of heterogeneity is not reflected in the statistical classification of the industrial structure. Artisan micro-enterprises, with only one or two workers and without machines, are classified in the official statistics together with small enterprises with some investments in fixed capital, and with small enterprises with higher level of mechanisation. Some of them work only as subcontractor for importers of finished goods or perform both for other enterprises and for the final market. Other enterprises despite the size are oriented towards the international markets, even though not directly but always through an intermediary. In some cases the specialised output of the craft production can be so high that they can be classified as "niche" products.

An attempt to summarise the main type of SMEs and MSEs in the region and their productive and organisational characteristics is provided in the following table. The categories and indicators in the table are elaborated following the information gathered during the field works. The table takes into account many factors: the number of employees, the legal registration, the technological level, the internal division of tasks, and the relationship with the markets and with the employees.

It is important to emphasise that firms can belong contemporarily to different categories due to the presence of similar characteristics in the type of production and organisation. This means that a craft industry can be small and internationalised and maybe specialised in a product that can be considered as a niche.

The common characteristic of these firms is the flexible organisational and productive structure and the presence of special ties with similar and geographically close firms. In theory, there are all the pre-conditions for developing a production system as such into well-organised group of enterprises able to enjoy economies of scale and technological externalities. However, the situation is more complex and the SMEs and MFEs sector faces many problems in the daily activities that hinder the possibility to develop into a more dynamic and prosperous sector.

<sup>21</sup> Gallina A., 1999b.

Table 1. *Towards a taxonomy of small manufacturing firms in the Mediterranean Region*

Artisan-artistic	Micro	Small	Medium
<i>Number of employees:</i>	One-two workers	Between 5 and 10 workers	Up to 50 workers
<i>License:</i>	Not registered	Not registered	Registered
<i>Technological level:</i>	Labour intensive	Labour intensive	Labour intensive
<i>Organisational level:</i>	Low division of labour	High division of labour	High division of labour
<i>Management:</i>	Owner/director	Owner/director	Formal management
<i>Market:</i>	Local customers and tourist sector	Local customers, tourist sector and intermediaries	Intermediaries
<i>Financial organisation:</i>	Informal credit	Informal credit	Mix of informal and formal credit
<i>Relation with the workers:</i>	Family	Workers paid by piece produced	Wagers
Subcontractors	Micro	Small	Medium
<i>Number of employees:</i>	Less than 5 workers	Between 5 and 10 workers	Up to 50 workers
<i>License:</i>	Not registered	Not registered	Registered
<i>Technological level:</i>	Labour intensive	Labour intensive	Good ratio capital/labour
<i>Organisational level:</i>	High division of labour	High division of Labour	High division of Labour
<i>Management:</i>	Owner/director	Owner/director	Formal management
<i>Market:</i>	Local or international customers	International customers	International customers
<i>Financial organisation:</i>	Advance payment from the customer	Advance payment from the customer	Formal credit
<i>Relation with the workers:</i>	Family	Workers paid by piece produced	Wagers
Specialised in niche products	Micro	Small	Medium
<i>Number of employees:</i>	Less than 5 workers	Between 5 and 10 workers	Up to 50 workers
<i>License:</i>	Not registered	Registered	Registered
<i>Technological level:</i>	Labour intensive and/or specialised technology	Labour intensive and/or specialised technology	Capital intensive
<i>Organisational level:</i>	High division of labour	High division of labour	High division of labour
<i>Management:</i>	Owner/director	Owner/director	Owner/director
<i>Market:</i>	Local and national customers	Local, National and international customers	National and international customers
<i>Financial organisation:</i>	Informal credit	Informal credit	Mix of informal and formal credit
<i>Relation with the workers:</i>	Family	Specialised workers paid by piece produced	Wagers
Internationalised	Micro	Small	Medium
<i>Number of employees:</i>	-	Between 5 and 10 workers	Up to 50 workers
<i>License:</i>	-	Registered	Registered
<i>Technological level:</i>	-	Capital intensive	Capital intensive
<i>Organisational level:</i>	-	High division of labour	High division of labour plus Quality control (ISO)
<i>Management:</i>	-	Family oriented management (with external managers)	Non family management
<i>Market:</i>	-	Intermediaries	International customers
<i>Financial organisation:</i>	-	Formal credit	Formal credit
<i>Relation with the workers:</i>	-	Highly specialised workers	Highly specialised workers

Source: author's elaboration

### *Mediterranean small enterprises structural and operational problems<sup>22</sup>*

The list of problems faced by the Mediterranean SMEs is not, generally speaking, much different from that of other developing countries. As it has emerged in the vari-

ous debates, the problems must be seen from both the demand and the supply side, but also on the infrastructural playground.

On the demand side the factors identified are: the change of consumption pattern of the population, the change in the requisite on the production imposed by the local norms, the weakening of the purchasing power of the population, the imposition of international standards.

On the supply side, the problems are related to the quality of the products, the absence of continuous product innovation, the lack of raw material of good quality, obsolete tech-

<sup>22</sup> This section benefits from the participation to the activities of the working-group on "Quality and Commercialisation Problems in Mediterranean SMEs" established within a network of Mediterranean non-governmental organisations and experts working for micro-enterprises development. The working group was established as a follow up of a project co-financed by the EU DG Development.



nology, poor design, poor packaging and presentation of the products. Little attention is generally paid to the fact that in the Mediterranean the owner of a SME is not necessarily a risk-taker entrepreneur, but is only a craftsman/producer and thus is not prepared to grasp the occasions offered by the market. The obstacle represented by the lack of marketing capacities is overtaken using intermediaries, which reduces the margins of profit and easily ends-up in creating a situation of dependency and exploitation.

It emerged also that many of the problems faced by SMEs in their daily productive routine are related to lack of infrastructure, roads and communications and provisions such as electricity, water and telephone, especially in Lebanon, Palestine and Algeria, or to lack of adequate spaces. The concentration of all production phases in a limited place determines losses in the value added due to the difficulty in organising the production line in a more rationale way. The lack of an internal division of labour is often linked to the lack of machinery, which in turn produces competition among workers paid on a piece-basis and thus a less friendly working environment. The absence of qualified manpower is another problem that is diffused especially in textile and clothing firms, which utilise young and cheap labour. Furthermore, these small producers have few marketing skills and can survive only because they are not in need to go to the market: it is the customer, either a final buyer or another firm that go to the workshop and buy.

## 5. Learning for Innovating in the SMEs and MFEs sectors

The intangible factors, such as personal relations and tacit technical knowledge (the "know how" and "know who" of Lundvall's taxonomy)<sup>23</sup> emphasised in the description of the SMEs and MFEs production system are the main sources of change in the products and production processes. Innovation consists mainly of incremental adaptation to new materials, to new techniques and design. Therefore, it is easy to find firms working with the same technology for more than fifty years. This can be also explained by the fact that in mature sectors process technology is subject to a discontinuous process of innovation and, therefore, it is not necessary for the firm to replace its capital stocks through intense acquisition of new machinery.<sup>24</sup> This does not pose any problem to their capacity and the product supplied can still be sold on the local market.

Product innovation has an incremental nature and it depends very much upon the ability of the producer to imitate. However, it is easily foreseeable that, due to the lack of good raw material and of marketing skills, such production is not sufficient to match the standards of the international markets. Innovation activities, although hidden and difficult to measure, are routine activities for the SMEs and MFEs if we consider the special rela-

tionship that exists between the firm, its production and the customers. The capacity of the "practical man" (Hansen and Serin 1997) to adapt to new demand and to new design gives to the small firms an important advantage, and shows the existence of a knowledge base that should not be neglected by industrial and innovation policies within the Euro-Mediterranean Partnership. It should also be stressed that the process of innovation, as an accompanying measure of the more general process of modernisation, in order to be sustainable with the existing stock of localised knowledge needs to focus on the learning capacity of the workers and entrepreneurs. It is therefore important that, besides the solution to the obstacles emerged during the field study, an institutional set-up reinforcing and stimulating the learning capacity, according to the needs and the structure of the local production systems and markets will be properly developed.

Although it should be recognised that a central asset for the innovation process is the stock of tacit knowledge owned by the producers and by the workers employed, the negative attitude towards external sources of information and knowledge could create situations of "lock-in". In this direction the presence of "shared knowledge environment" in many clusters of enterprises, in which resources and information are shared and competition is replaced in many cases by co-operation, needs to be emphasised. The "absorption attitude" of the firm should thus increase if the unity of the community of producers must be maintained instead of being fragmented by process of exclusion. To make these factors available for the firms of that specific production system means to integrate social informal networks and community of producers. Learning about each other and about each other's activity becomes an important aspect of the process of innovation. The same applies to vocational and professional training schemes. The professional training schemes and the "infra-mural" informal system should interact with each other. The first system can supply the second providing the skills related to newer development in design and materials, while greater emphasis should be given to the importance of the "infra-mural" informal training for its role for young unemployed. The resistance of the firms towards the introduction of measures that affect their production directly, such as training scheme, social security schemes and support schemes, is due not only to their attitude, but also to the large gap existing with the institutions working for industrial development. Different levels of integration between local public authorities and private groups of interest should be supported in order to contribute to cohesion and solidarity between the environment's different elements, as well as to enhance collective values and rules. Once acknowledged, the importance of this sector for the socio-economic stability of the region and for the process of Euro-Mediterranean co-development, greater efforts for further research in this sector should be made.

## 6. Conclusions and implications for future research

The paper has attempted to link the analysis of a macro process, the creation of a political and economic Partnership be-

<sup>23</sup> Similar conclusions have been reached by North and Smallbone, 2000, when analysing the innovation dynamic in British printing industries. On the different types of knowledge see Lundvall B. Å. and B. Johnson, 1994; Ernst D. and Lundvall B. Å., 1997.

<sup>24</sup> See also Sterlacchini, 1999.

tween the EU and 12 Mediterranean countries, with the dynamic at the micro level represented by the SMEs and MFEs sectors. Although the risk of remaining superficial in the analysis of each aspect of the processes occurring at the macro and micro levels, the paper has contributed to a better knowledge of the Mediterranean contemporary manufacturing system, and highlighted some important conditions to be taken into account in the future implementation of the Partnership.

The loss of fiscal earnings and the dismantling of public monopolies will continue to reduce the role of the state in the economy of MPCs, and its possibility to keep the welfare improvements achieved during many years. At the same time, the increasing demand for jobs and the contraction of the purchasing power cannot be met only by export-oriented strategies or technological innovation. The passage from import substitution to export promotion has been even in the most successful cases very painful, and despite strong intervention of the state as in the Asian countries. Exports oriented strategies can lead to specialisation in productions that make little contribution to indigenous technology and human capital development.<sup>25</sup> On the other hand, although the infant industry argument is very appealing, the reduction of tariff on imports of capital goods, which represent an important share of total imports, can produce important technological advances if appropriate technological training measures are supported.

The upgrading of the industrial sectors, as demonstrated also by the number of measures undertaken by the single countries, is a priority issue on the agenda. However, due to the structure of the sector and the varieties in the type of firms existing the risk of creating incurable fractures, only concentrating the efforts on specific segment of the productive systems, namely medium-high and high-tech sectors and medium-sized firms, is very high.<sup>26</sup> Also, the importance given to the creation of special economic zone does not take into account previous experiences in other countries, as for example in Asia, showing the risk that protected zones like those serve basically the interest of large international firms investing in unskilled and labour intensive activities.<sup>27</sup> Finally, an entry in the international production chain through sub-contracting can be dangerous if it aims only to cost reduction instead of enhancing the technical capabilities and the technological confidence of the entrepre-

neurs, workers and apprentices.

With the progress towards the establishment of a completely free trade area, to take advantage of the new regime depends also on a set accompanying measures, both fiscal and monetary, such as for example the exchange rate policy, tax holidays, and export incentives.<sup>28</sup>

The analysis of the productive structures has shown the difficulties in considering the SMEs and MFEs as a homogenous sector to which apply blueprints solutions. Even in the policy discussion very little reference is made to this problem, and the discussion is mainly based on the problem of formalisation/regulation of the informal sector. In the field study has emerged that these firms are not backward, immobile and impermeable form of organisation. Instead, they are receptive to changes, both on the demand and on the supply sides, but lack a dynamic macro-economic setting enabling to stimulate production and a learning capacity enabling to mobilise a process of innovation that is sustainable with the stock of competencies possessed.

It is impossible to imagine that these entrepreneurs can be transformed, in a span of time like the one envisaged for the establishment of the free trade area, in the multi-skilled and dynamic craftsmen/managers of Piore and Sabel's books.<sup>29</sup> The increase of the human value added must be on the agenda, but cannot be separated from the contextual factors and from the macro-economic setting. In this direction, a better knowledge of the technological and technical capabilities possessed by the entrepreneurs and the workers, the types of innovation processes that take place, the various elements that characterise the local environment, the socio-economic context and the markets represents a priority for both theoretical and policy-oriented research. To conclude, due to the fact that in the region there is:

- (a) An increasing demand from a growing population with pattern of consumption different from those supplied by global firms; and,
- (b) A manufacturing sector strongly tied with the local markets and local commodity chains;

SMEs and MFEs sectors in the Mediterranean countries can contribute to the establishment of a more balanced Euro-Mediterranean market if the policies for co-evolution and co-development of these production systems are able to move production towards higher quality, while gradually introduce new forms of production and consumption. This can be achieved by reinforcing the current intra-industrial complementarities involving not only the modern SMEs, but also the family and small enterprises in the traditional sectors. In this way the economic objective can be achieved without hindering the achievement of the other objectives of security and socio-cultural co-operation.

## References

For technical reasons we are forced not to publish the references. We apologize with the Autor. References are available at the editorial office of New Medit.

<sup>25</sup> In a study by Ariff and Hill, 1985, on the development strategies of South East Asian countries is showed that in export promotion zones trade unions are virtually excluded, work norms are so high that workers develop physical and mental disorders, p. 49

<sup>26</sup> See also the Note of the European Union Economic and Social Committee "Le politiche di innovazione delle PMI e dell'artigianato (VI Vertice Euromed), Bruxelles 3 Agosto 2000. See also Chourou (2001) for evidences on the Industrial Modernisation Programme effects in Tunisia.

<sup>27</sup> Ariff and Hill, 1985, p. 48.

<sup>28</sup> For example, through a strong devaluation Tunisia during the mid-1980s managed to export in the EU labour intensive goods, such as textile and garments, in which for example Italy and Spain enjoy a strong competitive advantage.

<sup>29</sup> Similar conclusions can be found in McGrath S. and K. King.