Program Information Document (PID)

Appraisal Stage | Date Prepared/Updated: 13-Nov-2018 | Report No: PIDA25874
BASIC INFORMATION

A. Basic Project Data

<table>
<thead>
<tr>
<th>Country</th>
<th>Project ID</th>
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<th>Parent Project ID (if any)</th>
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<tr>
<td>Egypt, Arab Republic of</td>
<td>P168630</td>
<td>Private Sector Development for Inclusive Growth DPF (P168630)</td>
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<tr>
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<th>Estimated Board Date</th>
<th>Practice Area (Lead)</th>
<th>Financing Instrument</th>
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<tr>
<td>MIDDLE EAST AND NORTH AFRICA</td>
<td>04-Dec-2018</td>
<td>Finance, Competitiveness and Innovation</td>
<td>Development Policy Financing</td>
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<th>Borrower(s)</th>
<th>Implementing Agency</th>
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<td>Arab Republic of Egypt</td>
<td>Ministry of Investment and International Cooperation, General Authority for Investment &amp; Free Zones</td>
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Proposed Development Objective(s)

Enabling financial inclusion, private sector development and strengthening fiscal management for inclusive growth in Egypt.

Financing (in US$, Millions)

**SUMMARY**

<table>
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<th>Total Financing</th>
<th>1,000.00</th>
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<td><strong>DETAILS</strong></td>
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<tr>
<td>Total World Bank Group Financing</td>
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Decision

The review did authorize the team to appraise and negotiate.

B. Introduction and Context

Country Context

1. Egypt, the largest country in the Middle East and North Africa region (MENA) with a population of 91 million, and the fourth largest economy, has embarked upon a bold program of major reforms that are needed to address some longstanding structural constraints to inclusive growth. Previous program of reforms (from 2015-2017) aimed to promote macroeconomic stability, achieve energy security and enhance competitiveness and business environment, which are yielding substantial gains. Real GDP grew, introduction of a new Value-Added Tax (VAT) and the gradual
phasing-out of energy subsidies helped fiscal consolidation, while the energy sector reforms have led to a more reliable electricity supply for firms. Business environment reforms included new industrial licensing and investment laws, leading to gains. However, despite these gains, substantial challenges remain for economic inclusion and equal access to opportunities for majority of the population, with strong constraints to private sector. Stark spatial inequality also exists, with poverty and vulnerability being higher in rural areas.

2. This DPF is anchored in the Government of Egypt’s (GoE) medium-term reform program. GoE developed a long-term vision – Egypt’s 2030 Sustainable Development Strategy – and has articulated a four-year reforms program – Egypt Takes Off – to support its strategic vision in medium-term. This program was endorsed by Parliament in July 2018. The three pillars of the reform program are based on the following: first, access to finance as an essential ingredient for growth of microfinance and formal employment by small and medium enterprises. Second, private sector development through improved corporate governance, ease of doing business, investor facilitation services, supporting entrepreneurship, enhancing transparency and automation of procurement, improved processes for property registration and facilitating disruptive technology of transport ride sharing. Third, strengthened fiscal management via facilitating online income tax filings, reduction in energy subsidies, publication of GoE’s Medium-Term Debt Management Strategy, and fiscal empowerment of local governments. The reforms supported in this DPF also build on a substantial base of analytical work supported by the WBG.

Relationship to CPF

3. The proposed DPF contributes to the implementation of the World Bank Group’s (WBG’s) MENA Strategy, the Systematic Country Diagnostic (SCD) and Country Partnership Framework (CPF) 2015-19. The proposed program’s focus on private sector-led economic growth, inclusion and job creation are top priorities of the WBG in Egypt as identified in the CPF. The program is also consistent with WBG’s Strategy for Middle East and North Africa (MENA) region which aims to promote peace and stability in the region and renew the social contract between the state and citizens via private sector-led economic growth to spur job creation. This operation builds on the findings of SCD and CPF on the need to focus on implementation and institutional aspects in addition to legislative reforms, where well-drafted executive regulations following laws, as well as clarity of institutional measures are critical for effective implementation.

4. The DPF seeks to address upstream reforms on legal, regulatory and institutional barriers for unlocking the potential of private sector investments across all three pillars of financial inclusion, enabling private sector development and strengthened fiscal management. The menu of proposed reforms are closely linked to (i) WBG’s twin goals of ending extreme poverty and boosting shared prosperity; (ii) the strategic pillars of WBG MENA Strategy related to renewing social contract and supporting inclusive growth; (iii) all three pillars of Egypt’s SCD 2014, namely, private sector led job creation, spatial integration, and inclusion; and (iv) the private sector-led job creation pillar of the Egypt CPF.

C. Proposed Development Objective(s)

5. The development objective of this operation is enabling financial inclusion, private sector development and strengthening fiscal management for inclusive growth in Egypt.

Key Results

6. The following key results are envisaged under the Program: Increase in number of microfinance beneficiaries using mobile payment or e-payment (including females and including beneficiaries located outside Greater Cairo and Alexandria); Increase in number of published registrations under electronic collateral registry used by firms, individual debtors and syndicated loans; Increase in number of new coded investors under Capital Markets Law; Increase in the
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value of the extent of shareholder governance index in Doing Business rankings; reduction in the number of days needed to start a business; increase in the number of firm registrations at new Investor Service Centers in lagging regions of Egypt; Non-governmental finance leveraged to complement government financing in an equal share under the “Fekretak Sherketak” / Egypt Ventures initiative; increase in the number of SMEs participating in public tenders and/or being awarded contracts; property registration offices in “new urban communities” implementing more transparent procedures for deed registration; increase in number of ride-sharing driver licenses issued; Increase in number of companies filing annual income tax returns electronically; reduction in energy subsidies as a percentage of GDP; publication of an updated expanded medium-term debt management strategy by GoE; and all Governorates and districts preparing their FY2020/21 capital investment plans in accordance with a formula-based transfer system for capital budgets.

D. Project Description

7. The proposed DPF is a stand-alone, two-tranche operation (with each tranche being US$500 million) aimed at supporting GoE’s effort to improve inclusive growth, structured under three objectives, each supported by a corresponding pillar: i) Improving financial inclusion and access to finance; ii) enabling private sector investments in key development areas to encourage entrepreneurship and job creation; and iii) strengthened fiscal management through facilitating online income tax filings, reduction in energy subsidies, publication of GoE’s Medium-Term Debt Management Strategy, and fiscal empowerment of local governments. The operation contributes directly to the GoE’s overall vision to place inclusive growth and job creation. It further contributes to improving governance, transparency, and public service delivery. The GoE program provides the anchor for this DPF, supporting selected policy actions. All measures supported by the DPF carry strong government ownership and are fully embedded within the Government Program. The reforms supported in this DPF also build on a substantial base of analytical work supported by the WBG.

8. The proposed DPF will support the following specific policy reform actions and tranche release conditions which contribute to the policy objectives of the GoE program:

a. **Pillar 1 - Financial inclusion and access to finance:**
   
   i. Improving access to finance for subsistence entrepreneurs and microfinance by allowing use of mobile payment in microfinance activities and electronic payment by microfinance institutions;
   
   ii. Facilitating greater access to finance for SMEs by strengthening the implementation of the framework for secured transactions by establishing and operationalizing an electronic collateral registry for security interests in movable property;
   
   iii. Fairer and more efficient capital markets and broadening the investors base by amending the Capital Markets Law.

b. **Pillar 2 – Private sector development:**
   
   i. Strengthening corporate governance and minority shareholder protection through regulations supporting the new Companies Law;
   
   ii. Improving ease of doing business and enhancing the business environment by reducing the number of steps to establish a company;
   
   iii. Providing investor facilitation services in lagging regions such as Upper Egypt and/or frontier Governorates, easing business establishment and operations;
iv. improving the ecosystem for entrepreneurship through the “Your Idea, Your Company” program to provide technical assistance, funding and improve the regulatory framework for private sector-led entrepreneurship;

v. promoting and facilitating SME participation in public procurement and enhancing transparency and automation of public procurement through new procurement law;

vi. improving processes for property registration and efficiency of land administration through improving property deeds registration in new urban communities (via new law) and simplification in property title registration process (via draft new law on title registration system), to improve transparency and quality of information;

vii. facilitating disruptive technology in the transport ride sharing sector through regulations supporting new Ride Sharing Law to determine conditions, procedures and controls required for issuance of operations licenses, taxes and charges, and operations cards; a framework for taxes, charges and social insurance premiums; and specifying data and information required to be kept and maintained by ride-sharing companies;

c. **Pillar 3 – Strengthened Fiscal Management:**

   i. simplifying tax payment and improving the business environment via facilitating electronic filing of tax returns;

   ii. publication of an updated expanded medium-term debt management strategy by GoE;

   iii. reduction in energy subsidies and continuing adjustments to energy prices via electricity and fuel price adjustments, for promoting private sector investment in energy sector and creating fiscal space for necessary investments in human capital;

   iv. fiscal empowerment of local governments by improving quality, transparency and sustainability of capital spending at Local Administrative levels (Governorates and districts).

E. Implementation

Institutional and Implementation Arrangements

9. **MIIC**, through the General Authority for Investment & Free Zones (GAFI), will be the main coordinating agency for monitoring and evaluation among the participating ministries/agencies of this program. The prior actions detailed in this operation are the prime responsibility of concerned Ministries and entities of the Government of Egypt. MIIC will coordinate with other ministries and agencies on achievement of results. Being the main counterpart of the World Bank Group in Egypt, MIIC will have the responsibility of presenting the information related to the reform implementation and progress made toward results on time and in a format satisfactory to the World Bank.

F. Poverty and Social Impacts and Environmental Aspects

Poverty and Social Impacts

10. Prior actions supported by this DPF are expected to have both direct and indirect effects that interact differently in the short- and long-term with the wellbeing and job prospects of the poor and vulnerable. Prior action 9 (pillar 3) on energy price adjustments is expected to have a direct negative impact on households’ welfare in the short term through the increase in price of energy products; in the short term, households have limited ability to adjust their consumption or income in response to price increases. Given the large share of the poor residing in Upper Egypt, the negative effect
is expected to be spatially concentrated in that part of the country. Simulations of the July 2018 energy price adjustments (using 2015 survey data) suggest that the most recent energy price adjustments negatively affect households’ welfare. The poorest quintile (bottom 20 percent of the distribution) is estimated to experience a welfare loss equivalent to 5.2 percent of their household budget spending; the richest quintile is estimated to lose about 1.6 percent of their budget spending. Around 70 percent of these welfare losses are a result of fuel price increases, and the rest are due to electricity price increase. Impacts vary across locations, with larger welfare losses found among households residing in regions with higher poverty rates.

11. It would be important that available social assistance mechanisms such as the Takaful cash transfers and the food smart cards are utilized to mitigate the effect on the poor, especially those living in Upper Egypt. In the long-run, the positive effects of reducing regressive and expensive subsidies, rebalancing investment in economic sectors, and the stronger ability of the government to efficiently support the most vulnerable are expected to outweigh the short-term losses. The reforms in the energy subsidies have facilitated budgetary expansion of social protection programs with more targeted subsidies. In addition, the mitigation strategy for the income loss is through a programmatic support on additional finance to social protection program (proposed operation of US$500 million) and recently approved projects on health sector (US$530 million) and education reforms (US$500 million). The social protection program seeks to expand the coverage of conditional cash transfer program from 2.2 million households to 3 million households, introduction of human capital development linking cash transfers to school attendance of 80% by children of marginalized families and at least 4 visits to health centers by the poor and marginalized families. This is being complemented with health program expanding the supply of primary health services in lagging governorates. Finally, an economic inclusion program called Forsa is being launched targeting training of at least 30,000 individuals on job skills or small assets transfers for livelihood support and job creation.

12. For all other policy actions, a common thread of the assessment is that there is a potential for actions to have positive indirect effects via private sector job creation. Other policy actions are not expected to have a direct adverse effect on the poor or vulnerable as these actions do not directly influence prices faced by households. Policy reform actions from the operation’s Pillars 1 and 2 may influence small and medium enterprises (SMEs) and enable them to be job creators. SMEs are the largest employers in Egypt and evidence analyzed in World Bank (2014) shows that weak job growth in Egypt can be explained by lack of growth of SMEs. Potentially positive, though indirect, poverty and social impacts can be realized if the measures of Pillars 1 and 2 support SME growth and hiring. Majority of the prior actions under these two pillars will benefit already formal SMEs; the full job creation potential of these actions may be realized if they incentivize formalization. Actions under pillars 1 and 2 will mainly reduce the costs of accessing credit to formal SMEs thereby increasing their job creation potential. Informal firms could benefit from the expanded access to credit only once they formalize. The job creation impact of regulations to be introduced for ride share platforms is unclear.

13. Prior action 10 under pillar 3 (improving quality, transparency and sustainability of capital spending at Local Administrative levels) has the potential to improve basic services provision since governorates with high poverty rates also have poor access to basic services and infrastructure. Access to improved services such as water and sanitation services can directly enhance living standards of the population as well as their human capital accumulation and improve households’ welfare. This prior action on formula for capital allocation will improve allocation and planning of capital expenditure at governorate and district levels due to more predictable and transparent financing. These levels of government are responsible for local development functions such as sanitation, transport, health, education, etc.

Environmental Aspects

14. Over the past two decades, Egypt has continuously updated its environmental policy and regulatory framework with provisions to integrate environmental concerns with national development plans and ensure the protection of
human health and the sustainability of natural resources. The most recent “Sustainable Development Strategy: Egypt Vision 2030” is putting equal emphasis on its three pivotal dimensions: economic, social and environmental.

15. The assessment conducted by the World Bank, as per OP 8.60, concluded that the policies supported by the proposed DPF are likely not to have significant negative impacts on Egypt’s environment nor its natural resources. Some of the DPF prior actions may implicitly contribute to climate change co-benefits. For example, Prior Action 5 under Pillar 2 on the establishment of “Your Idea, Your Company” program avails opportunities for the development of clean energy and environment friendly technologies and support services by the young firms and entrepreneurs. Prior Action 9 under Pillar 3, which relates to efficiency pricing of fuels and electricity, is also expected to contribute to the reduction of carbon emissions due to the anticipated demand response resulting from the increase in prices to end consumers. A second tranche release condition on regulations supporting new Ride Sharing Law could potentially result in negative environmental impacts particularly in terms of air quality. However, a recent Presidential Decree (419/2018) which provides economic incentives (custom deductions) for cleaner fuel cars (electric, hybrid, CNG-powered cars) coupled with the removal of subsidies for gasoline fuel could help mitigate the environmental impacts. It will be important to ensure that pertinent national air emission inspection for the vehicles used are periodically and strictly implemented.

G. Risks and Mitigation

16. The overall risk rating of this operation is high. The major risks to the operation’s ability to achieve its development objective include: (a) political and governance challenges; (b) macroeconomic challenges associated with high inflation and the large public debt ratio; (c) sector strategies and policies of an unprecedented nature for Egypt’s context; (d) institutional and implementation capacity; (e) existing weaknesses in public financial management; and (f) difficult social conditions and potential environmental risks. The Bank will continue to closely monitor these risks, which are mitigated through strong ownership by government, citizen engagement in decision making, and a robust supporting program of technical assistance and sector-specific lending operations.
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APPROVAL

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