



EGYPT:
Financial Sector Reforms
&
The Role of Fiscal Policy in Promoting
The Domestic Financial Sector

Hany K. Dimian
Deputy Minister of Finance
Egypt

Euro-Med Economic and Finance Senior Official Meeting
Brussels,
27 June 2007

OVERVIEW

**I. THE ROLE OF FISCAL POLICY IN PROMOTING
FINANCIAL SECTOR REFORMS IN EGYPT**

II. HIGHLIGHTS ON MAIN FINANCIAL SECTOR REFORMS

III. FACTS ON EGYPT'S DOMESTIC BONDS MARKET

I. ROLE OF FISCAL POLICY IN PROMOTING FINANCIAL SECTOR REFORMS IN EGYPT

1. Background on Fiscal Policy / **New vision** in Egypt
2. Resolving a significant part of **NPLs** owed by Public Enterprises: impact on Banks and Companies' bank profits/ mergers/ privatizations/ Credit to the private sector... etc. (LE 26 bn to less than LE10 bn)
3. Supporting **largest privatization transaction** in the financial sector for BOA at some LE 9.1 Billion. Authorities are willing to repeat exercise: Impact on credit and interest structure, non-financial public enterprises.
4. **Pension system**: plans to move to defined contribution system, while allow a portion of contributions invested in non-government papers. Professional Fund Managers for private/public schemes (2008/2009).
5. **Debt Management** and introduction of **primary dealers** system for treasury bonds, where they may act as underwriters and market makers.

I. ROLE OF FISCAL POLICY IN PROMOTING FINANCIAL SECTOR REFORMS IN EGYPT

4. Legal reforms

a. *Stamp Duties (2006):*

i. Streamlining:

- Abolishment of 8 different types of stamp taxes on banking activities
- Unifying 3 rates of stamp taxes on banks' loans and credit facilities to one single rate (2/1000).
- The unified tax is applied on actual amount of loans utilized, instead of total credit line approved by the bank.

ii. Reduced Rates

- Life insurance premium from 3% to 1%
- Transportation services from 15% to 10%
- All other insurance premium from 20% to 10%

b. *Income Tax*

i. Simplified / Improved System

ii. Lower Rates

I. ROLE OF FISCAL POLICY IN PROMOTING FINANCIAL SECTOR REFORMS IN EGYPT

5. Implementation of a **wide-ranged** reforms in Budget and Treasury functions

a. **Introducing advanced systems for efficient budget management and institutions including:**

- i. Budget classification and automation / consolidation /transparency*
- ii. Medium term projections*
- iii. New Organic Budget law (start drafting soon)*

I. ROLE OF FISCAL POLICY IN PROMOTING FINANCIAL SECTOR REFORMS IN EGYPT

b. Reorganization of Treasury sector and functions:

- Advanced **accounting and reporting** framework
- **TSA**
- **Debt management**/ Improved maturities and share of traded papers/ non-CBE financing.
- **Cash** management
- **Risk** management
- Assets /Liability Management (**ALM**)
- **GFMIS** to replace existing manual framework
- Improving Check Cycle → Move to **electronic transfer**
- Re-engineering of financial relations with main non-bank debtors (SIF).

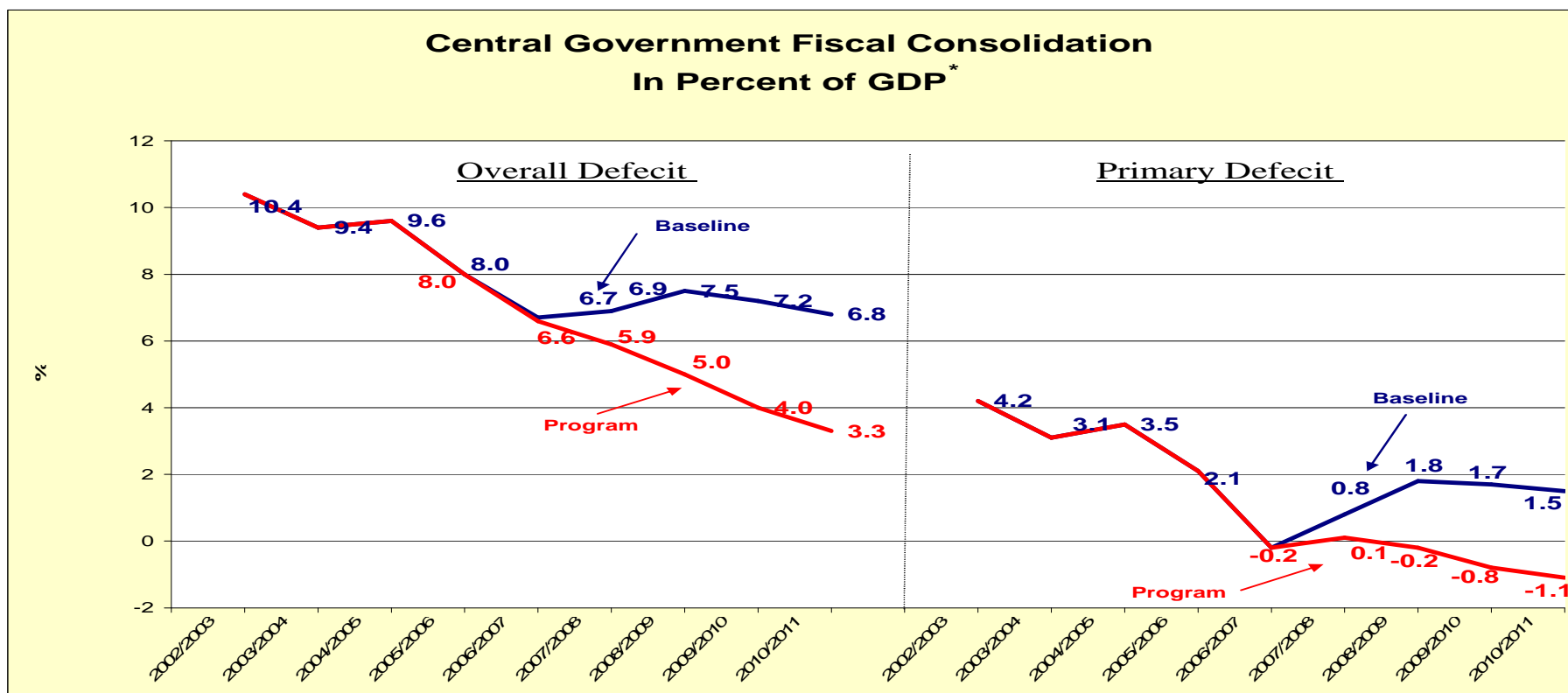
I. ROLE OF FISCAL POLICY IN PROMOTING FINANCIAL SECTOR REFORMS IN EGYPT

These Reforms Help:

- Better management of public monies (140-150% of GDP + other contingent liabilities)
- Improved transparency / market performance
- Better sovereign and non-sovereign risk management
- Better monetary policy management

I. ROLE OF FISCAL POLICY IN PROMOTING FINANCIAL SECTOR REFORMS IN EGYPT

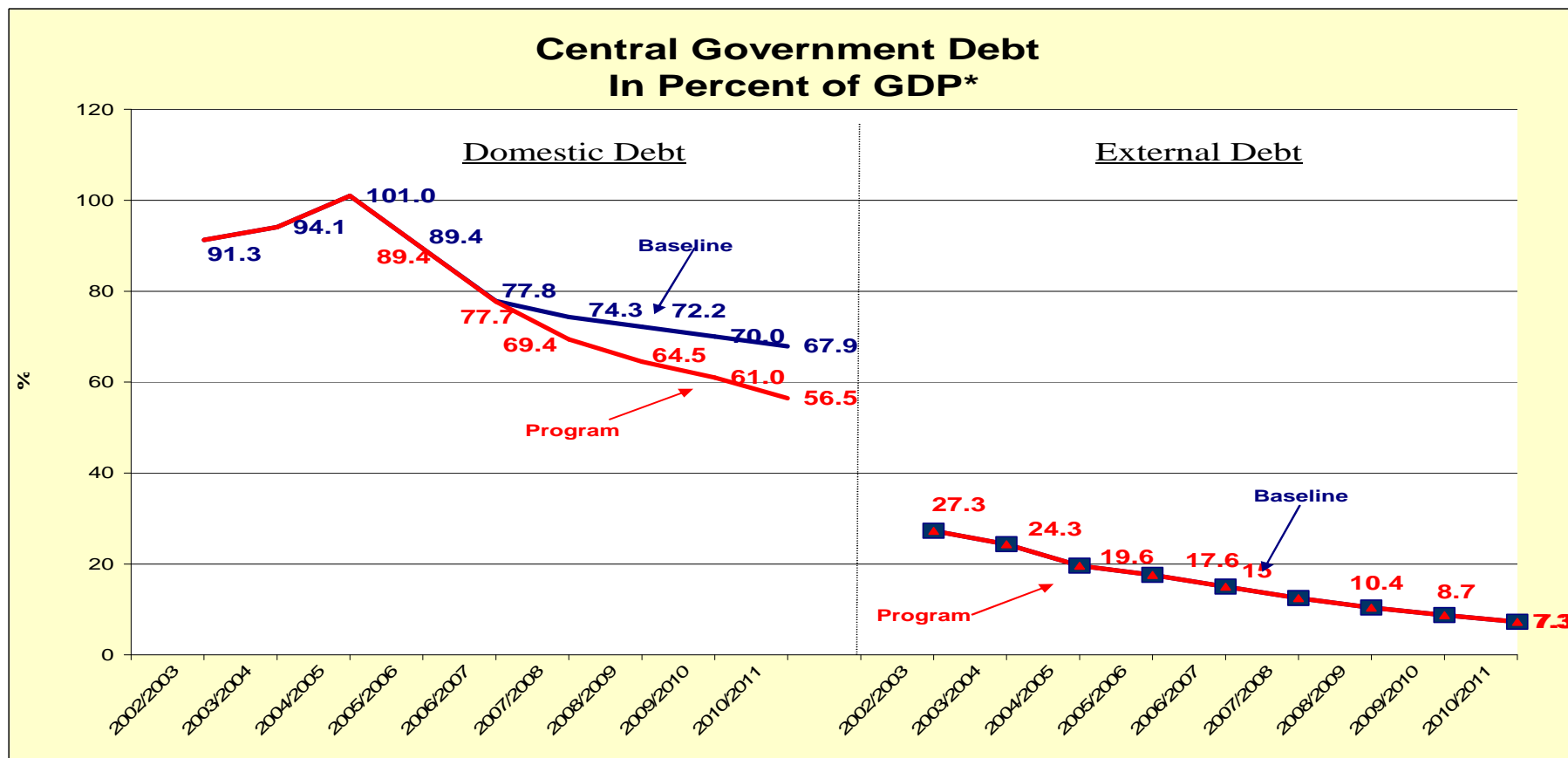
6. Fiscal consolidation



* Includes central administration, municipalities, and services authorities (education, health, ...etc.)

I. ROLE OF FISCAL POLICY IN PROMOTING FINANCIAL SECTOR REFORMS IN EGYPT

6. Fiscal consolidation



* Includes outstanding gross debt of central administration, municipalities, and services authorities (education, health, ...etc).

II. Main Financial Sector Reforms

As quoted by IBRD (2006) “the most substantive and comprehensive drive towards financial sector strengthening to have been launched so far in Egypt and indeed in any other countries in the Middle East and North Africa Region”.

II. Main Financial Sector Reforms

A: The Banking Sector

Goal: Improve access to finance, and enhance competitiveness, transparency and efficiency of the financial sector.

1. Main Features

- a. Improving Regulatory Framework. and the development of risk-based prudential regulation.
- b. Introducing advanced financing tools according to market needs.
- c. Consolidation of banking system through privatization, mergers and acquisitions, and sale of public banks' shares in 17 joint venture banks. The number of banks to be reduced from 57 in 2004 to 39 banks. *(Expected to become 34 banks by end of 2007).*
- d. Restructuring of public banks.
- e. NPLs problem.

II. Main Financial Sector Reforms

A: The Banking Sector

2. Regulatory Framework

- a. Unified Bank Law no.88 for 2003
- b. Adoption of Anti Money Laundering Law; Egypt removed from FATF blacklist in 2004.
- c. Increasing minimum capital requirement for banks operating in Egypt to LE 500 million, and to US\$ 50 million for foreign branches. Coupled with largely resolving NPLs problem, banks' capitalization problem mostly resolved.

II. Main Financial Sector Reforms

A: The Banking Sector

3. Consolidation of the Banking Sector

- The number of operating banks declined from 57 in 2004 to 41 in December 2006, and to 39 in 2007.
 - i. Mergers
 - ii. Acquisitions
 - iii. Sale of public banks shares in 13 Joint Venture Banks.
 - iv. Privatization of Bank of Alexandria

II. Main Financial Sector Reforms

A: The Banking Sector

i. 10 Mergers during 2004-2007

Merged Banks		New Entity	Date
First Bank	Second Bank		
American Express Bank (branches in Egypt) and Egyptian American Bank	Egyptian American Bank	Egyptian American Bank	Sep-04
Misr Exterior Bank	Misr Bank	Misr Bank	Sep-04
Credit Liones Branch	Credit Agricole Indo Swiss-Egypt	Calyon	Mar-05
Misr America International Bank	Arab African International Bank	Arab African International Bank	Sep-05
Mohandes Bank	National Bank of Egypt	National Bank of Egypt	Oct-05
Bank of Commerce and Development	National Bank of Egypt	National Bank of Egypt	Dec-05
Nile Bank with Islamic International Bank for Investment and Development and United Bank of Egypt		United Bank	Jun-06
Egyptian American Bank	Calyon	Credit Agricole Egypt	Aug-06
Misr International Bank	NSGB	NSGB	Nov-06
Banque du Caire	Bank Misr	Bank Misr	Feb-07

Source: Central Bank of Egypt

II. Main Financial Sector Reforms

A: The Banking Sector

ii. 14 Acquisitions during 2004-2007

Acquired	Acquirer	Date
Cairo Barclays	Barclays	Mar-04
Port Said National Bank for Development	Arab Banking Corporation International	Aug-05
Suez Canal Bank	Arab-Banking Corporation International	Aug-05
NSGB	Societe General Paris	Feb-05
Egypt Commercial Bank	Piraeus	Jun-05
Misr International Bank	NSGB	Sep-05
Misr Romania	BLOM	Dec-05
Misr America International	Arab African International	May-05
Egyptian American Bank	Credit Agricole	Feb-06
Delta International Bank	Shareholders in Delta International Bank	Feb-06
CIB	Ripplewood	Feb-06
Cairo Far East	Audi	Mar-06
Misr Iran Development Bank	National Investment Bank	Apr-06
Alexandria Commercial Maritime	Union National Bank	Aug-06

Source: Central Bank of Egypt.

- Excluding the acquisition of Port Said National Bank for Development, all acquisitions listed above include the sale of public shares in joint venture banks.

II. Main Financial Sector Reforms

A: The Banking Sector

iii. Sale of public shares in 13 Joint Venture Banks since 2004

Divested Public Bank	Acquirer	Acquired Shares in Joint Venture Bank
	Ripplewood	CIB
National Bank of Egypt	Arab-Banking Corporation International	Suez Canal Bank
	Societe General	NSGB
	NSGB	Misr International Bank
Misr Bank	BLOM	Egypt Romania
	Arab African International	Misr America
Banque du Caire	Audi	Cairo Far East
	Union National Bank	Alexandria Commercial Maritime
	Barclays	Cairo Barclays
	Piraeus	Egypt Commercial Bank
Bank of Alexandria	Credit Agricole	Egyptian American Bank
	Shareholders in Delta International Bank	Delta International Bank
	National Investment Bank	Misr Iran Development Bank

Source: Central Bank of Egypt

II. Main Financial Sector Reforms

A: The Banking Sector

iv. Privatization of Bank of Alexandria

The fourth largest public bank holding 5.9% of total banking assets as at end June 2004, worth LE 37.4 billions. Privatization primarily supported by resolving NPLs problem.

- **Process initiated during September 2004.**
- **Citi Group as financial consultant.**
- **Bank officially offered for sale during March 2006.**
- **Sanpaolo IMI acquired 80% of stakes in return of US\$ 1.6 billion, 5% for bank employees and 15% to be offered in stock exchange.**
- **Transition of ownership during December 2006.**
- **Using proceeds to settle part of SOE NPLs.**

II. Main Financial Sector Reforms

A: The Banking Sector

4. Settlement of NPLs

Wide-ranged program to settle NPLs of State Owned Enterprises outstanding to public banks worth 26:

- LE 6.9 billion (Jan 2006)
- LE 9.1 billion (Dec 2006)
- Remaining LE 10 billion (12 to 18 months)

II. Main Financial Sector Reforms

A: The Banking Sector

5. Measures Ahead

- The merger of Misr Bank and Banque du Caire is scheduled to be completed by end of 2009.
- Merger of Egyptian Workers Bank into Industrial Development Bank of Egypt.
- Merger of Egyptian Arab Land Bank into Housing and Development Bank.
- Merger of six Development Banks and Agricultural Credit bank into two separate banks.

II. Main Financial Sector Reforms

A: The Banking Sector

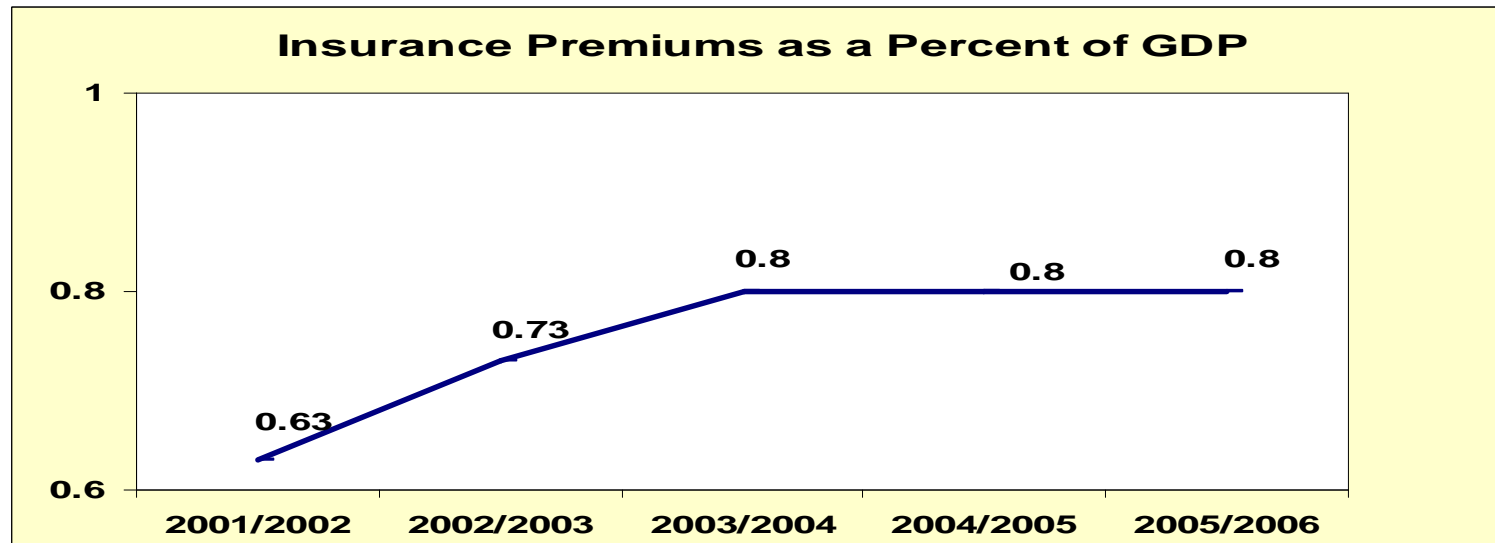
5. Measures Ahead

- Divestiture of public shares in the remaining 4 joint ventures: Egyptian Saudi Finance Bank, Egyptian Workers Bank, Export Development Bank of Egypt and BNP Paribas Le Caire
- The repayment of public enterprise NPLs worth nearly LE 10 billion during next 12-18 months using privatization proceeds.
- Enhancing the activity of central credit registry

II. Main Financial Sector Reforms

B: The Insurance Sector

1. High potential Market Premiums increased from less than 0.4 % of GDP in the 1990s to 0.8% in 2005/2006. Per capita share \$9/yr, in other countries reaches 4.5% of GDP.



2. Market witnessing Bank/Insurance alliances (Bancassurance).
3. Completed restructuring, due diligence, and valuation for four public companies, to be offered for privatization.

II. Main Financial Sector Reforms

B: The Insurance Sector

4.
 - a. Establish Insurance Holding Company (Capital LE 25.2 bn) to restructure insurance companies.
 - b. Establish real estate asset management company to separate insurance from real estate management activities.
 - c. Promoting insurance brokerage firms through forthcoming amendments.
 - d. A **new health insurance system** aiming to cover all citizens by year 2011 being drafted. World Bank to start Actuarial studies soon.

II. Main Financial Sector Reforms

B: The Insurance Sector

5. Upgrading regulatory body, and move towards applying risk-based prudential models, and apply regulations and standards of the International Association of Supervisory Authority.
6. Expected to merge Misr Insurance, Al Chark and Egypt RE, and offer to sale during 2007/2008.
7. Reforming premium rates for Motor Third Party Liability Insurance (MTPL) to break-even currently low making activity.

II. Main Financial Sector Reforms

C: The Capital Market – The stock Exchange

- 1. Institutional and Regulatory Reform**
 - a. Egypt is nearly in full compliance with IOSCO principles for securities regulations.**
 - b. Establishment of the Investor Protection Fund (IPF) to hedge investor against non-commercial risk. (2004/2005)**
 - c. Issuing new codes of Ethics and Conducts for the brokerage and fund management activities to ensure proper conduct of brokerage firm and mutual fund managers. (2004/2005)**
 - d. Applying online trading and Omnibus Accounts Rules.**

II. Main Financial Sector Reforms

C: The Capital Market

2. Instructional Reforms

- a. Introduction of the primary dealers system for treasury bonds, where the primary dealers act as underwriters and market makers.
- b. Introduction of **intra-day trading** of the same stock to settle most active stocks at T+0, and other stocks at T+3.
- c. Launching the Dow Jones CASE Egypt Titans 20 Index, which tracks the 20 blue chips of the Egyptian market.

II. Main Financial Sector Reforms

C: The Capital Market

3. Product Development and New Financial Rules

Issuing new derivative products

- 500 thousand Open End certificates issued for the third time by ABN-Amro Bank, which were traded on Euronext Amsterdam, starting 9 March 2006. The bank has also issued 500 thousand Close End certificates on 15 June 2006, listed and traded on Borsa Italiana.
- 1 million Open End certificates on CASE 30 Index licensed by CASE to be issued by Deutsche Bank, namely “EUR X-Pert”, traded on Frankfurt and Stuttgart Stock Exchanges.
- 500 thousand Open End certificates on CASE 30 Index issued by Goldman Sachs International, that are listed and traded on Frankfurt and Stuttgart Stock Exchanges.
- 380 thousand Open End certificates were issued and traded on the Swiss Exchange.

II. Main Financial Sector Reforms

C: The Capital Market

4. Technological Upgrading of trading and surveillance systems

- a. Upgrading the capacity of the trading system** to accommodate more than 100,000 transactions per day.
- b. Linking of the trading system of CASE with the clearing and settlement system** of the Misr for Clearing, Settlement and Depository, to provide a “Straight through Processing” environment.
- c. Activation of the online trading system** allowing investors to place their sell/buy orders directly on the Internet

II. Main Financial Sector Reforms

C: The Capital Market

5. Disclosure and Information Dissemination

- a. **An automated Disclosure and Listing system** is currently in place, to speed up the process of the information cycle from listed companies to the ESE and to market participants.

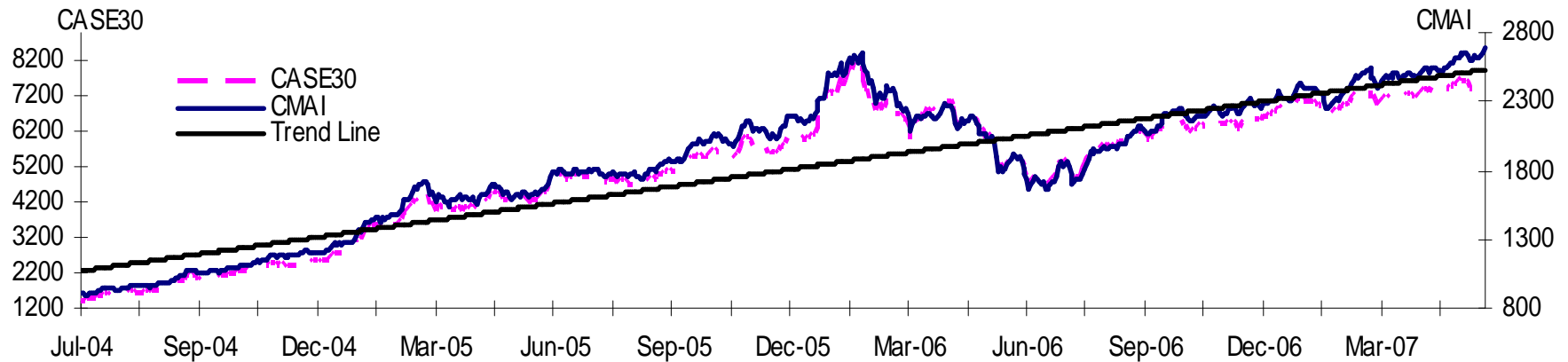
- b. **A new database compiling all listing information** of the listed companies on the ESE, and facilitating the issuance of customized reports and requests is also in place.

- c. Proper dissemination is further insured through **Egypt for Information Dissemination (EGID)**, which is a fully owned subsidiary of the Cairo and Alexandria Stock Exchange, exclusively in charge of transmitting CASE data to all recipients, both locally and internationally.

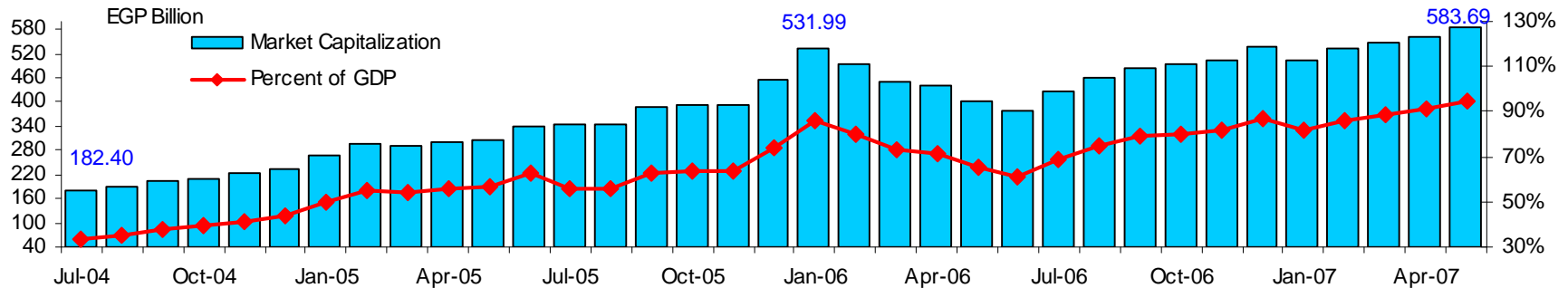
II. Main Financial Sector Reforms

C: The Capital Market

CMAI and CASE 30 (Jul 04 – May 07)



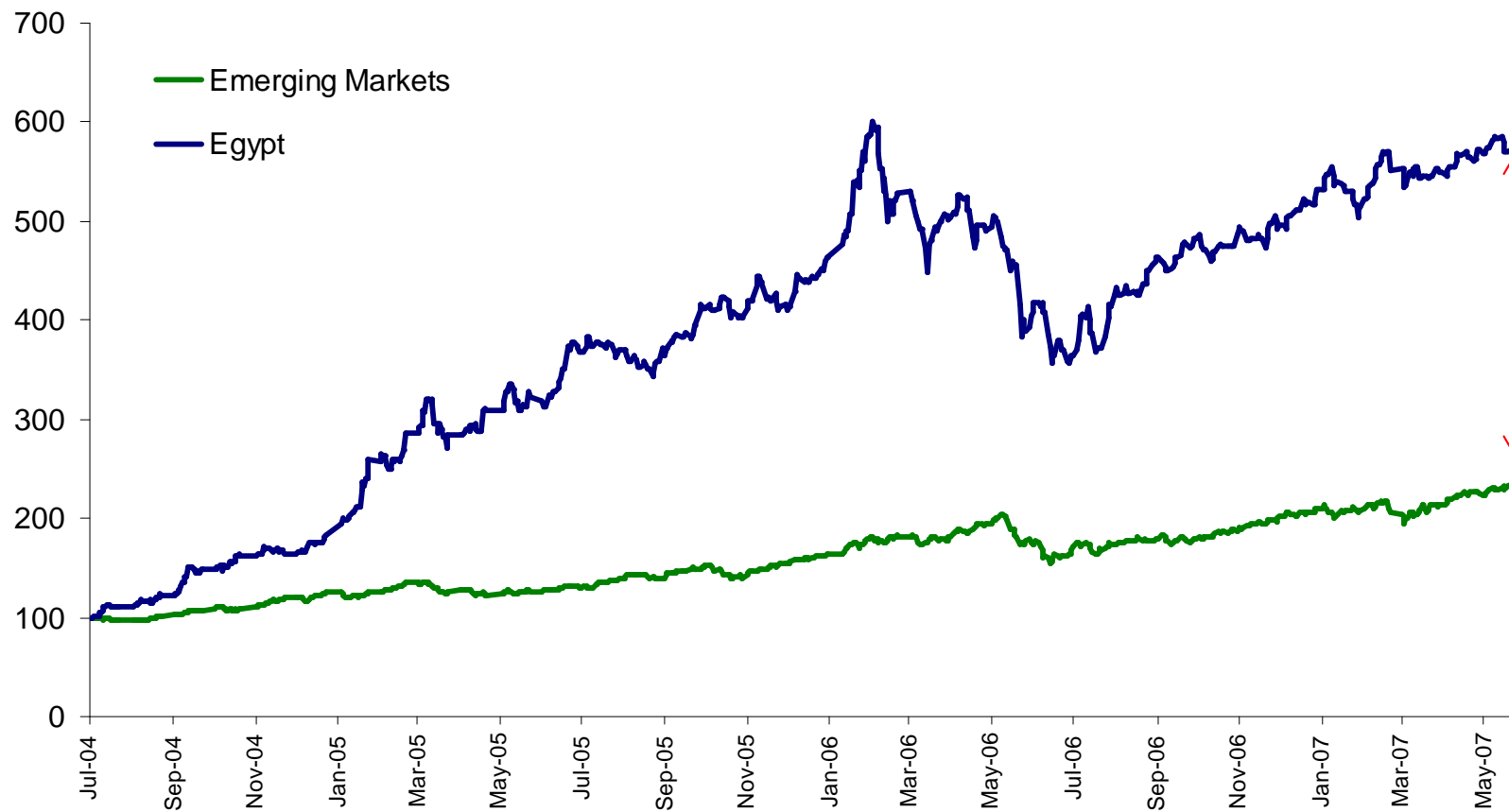
Market Capitalization



II. Main Financial Sector Reforms

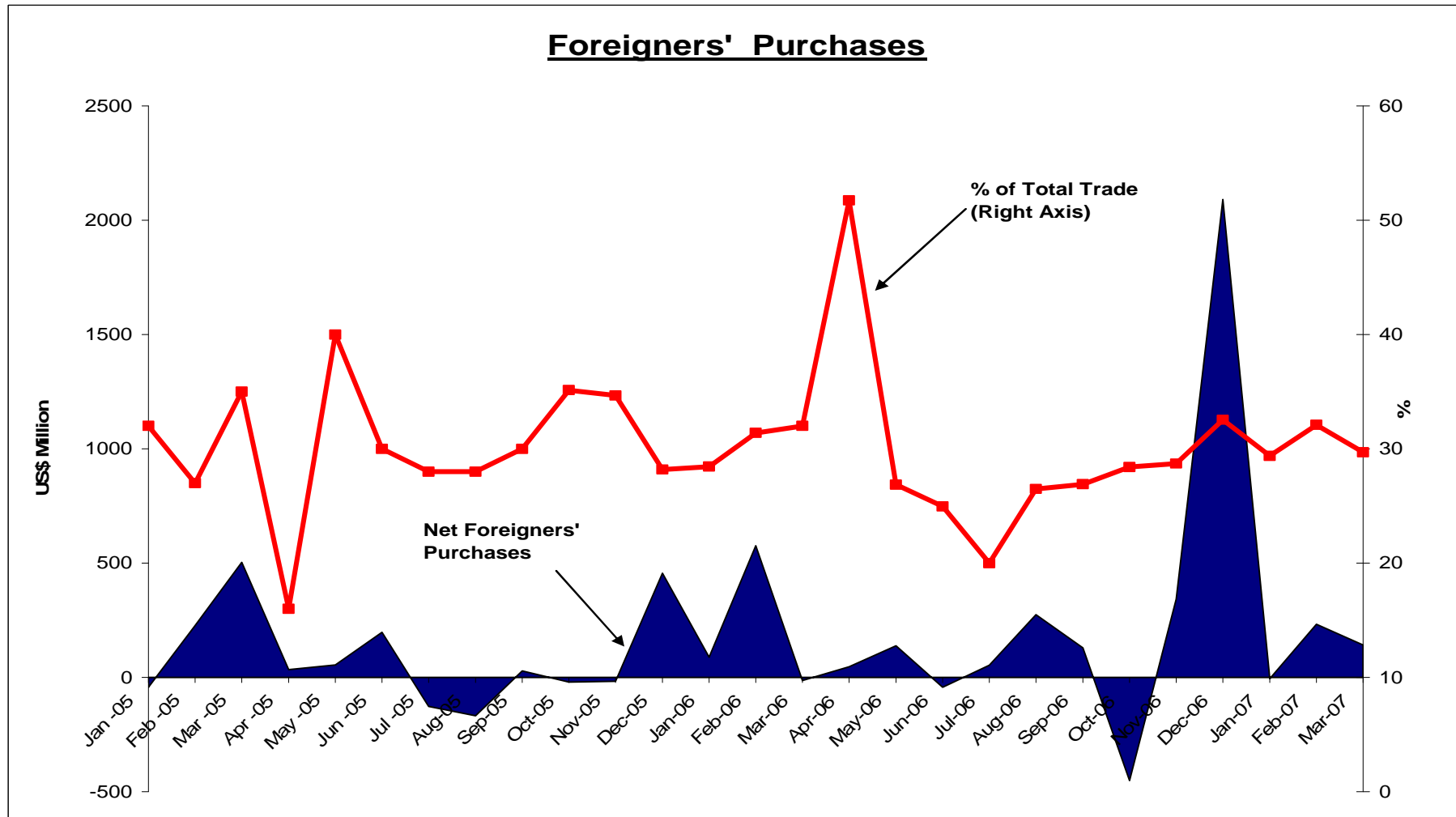
C: The Capital Market

MSCI Egypt vs. MSCI Emerging Markets



II. Main Financial Sector Reforms

C: The Capital Market



II. Main Financial Sector Reforms

D: Other Financial Services

1. Framework of Mortgage Market Reform

- a. Law allows banks, **mortgage** companies, trusts and insurance companies to provide mortgage loans.
- b. Law allows for debt **securitization**.
- c. Mortgage related insurance products.
- d. Mortgage lending increased during 2006. Total mortgage lending increased from LE 15.8 million in June 2005 to LE 514 million in June 2006 and LE 571 million in September 2006, reaching 1064 in March 2007.
- e. The government issued LE 1 billion bond (20 years maturity) to serve as a benchmark.
- f. Costs of real estate registration was reduced a number of times

II. Main Financial Sector Reforms

D: Other Financial Services

2. Financial Leasing

- a. The **Financial Leasing** Law No.95/1995 . Amendments in May 2001 exempting financial leasing from sales tax and fees.
- b. Leasing companies can register as importers in case of bringing goods in the country for lease out.
- c. Leasing operations in Egypt/ companies are still limited.

II. Main Financial Sector Reforms

D: Other Financial Services

3. Establishment of Egypt's First Credit Bureau

- The establishment of Egypt's first private credit bureau,
- 27 banks joined as shareholders.
- Issued capital LE 30 million.

III. An Overview on Domestic Bonds Market

III. An Overview on the Bonds Market

1. Regulated by Capital Market law (no. 95/1992) , CBE law (no. 88/2003) , Central Depository Law (no. 93/2000), Minister of Finance Decree (no. 480/2002) on Primary Dealers.
2. T-bonds par value LE 57 billion, Corporate Bonds less than LE 4 billion.
3. T-bills and T-bonds are issued through an auction system and are tradable in the secondary market.
4. Government papers dematerialized since 2004.
5. Electronic settlement since 2004 (t+1).
6. T-bills market liquid some LE 1 bn/day. T-Bonds less liquid.

III. An Overview on the Bonds Market

1. T-bills market liquid some LE 1 bn/day. T-Bonds less liquid.
2. Egypt has no restrictions on capital movements and accepted article VIII in the IMF Articles of Agreement.
3. Average life of Government papers increased from half years in 2004 to 2.1 years in 2007, and targeted at 3.5 years in 2 years.
4. MOF target to replace non-traded papers (CBE) with traded ones.
5. No with holding tax

III. An Overview on the Bonds Market

10. REPO agreements between MOF and banks, but banks do not use between each other.
11. Looking ahead to allow bond lending and short selling.
12. Market appetite is very high for all maturities. All issues are highly oversubscribed (even 20 years fixed income bond issued in 2005 was 2.8 times oversubscribed)
13. In 2005 first international (oil backed) securitized transaction worth 1.55 billion series notes due in 2010 and 2011 were issued.
14. In 2005, MOF issued 10 years note for 1.25 billion (coupon @4.45%) fully guaranteed by US government.
15. Next week Egypt is issuing its first Egyptian Pound Global Note linked to US\$.