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I. Introduction

This report has dual objectives. The first objective is to try to assess the role currently played by Small Scale Enterprises (SSE's) in Egyptian industry, in particular, and the Egyptian economy, in general. The second objective is to propose two credit programs for US-AID's intervention to assist the Egyptian SSE's sector.

In order to achieve the first objective, the Private Sector's role in Egyptian industry will be examined. This role can best be described in terms of the Private Sector's contribution to total investment, industrial output, employment, exports, and the number of privately owned industrial firms operating in Egypt. The examination of the role played by the Private Sector in Egyptian industry will demonstrate that there has been steady growth in this role since the Open Door Policy of 1974 was adopted. The Private Sector's relative share of industrial output in FY 83/84 stands at 34.3% of total industrial production. This percentage covers only formal and organized industry which is under the supervision of the Ministry of Industry. It does not take into consideration the output of artisinal firms involved in industrial type activities. The output of artisinal firms involved in industrial type activities is estimated at 15% of total industrial output. However, the output of artisinal firms does not show up in Ministry of Industry' statistics because these establishments are not under its supervision. Hence, the combined output of privately owned formal and informal industrial firms should bring Private Sector's share of industrial output to a much higher rate than the previously stated 34.3%.

The role played by SSE's in the Egyptian economy, in general, and

Egyptian industry in particular, can best be described within the Private Sector's role in both the Egyptian economy and industry.

Furthermore, this report examines the current definitions of SSE's prevailing in Egypt. Moreover, four definition of the SSE's sector are proposed. These four definitions take into consideration the number of employees per firm and the value of their fixed assets, excluding land and buildings. In addition, these four definitions subdivide the SSE's sector into the following:

1st: Artisans

2nd: Very Small Scale Enterprises (VSSE's)

3rd: "Average" Small Scale Enterprises (ASSE's)

4th: "Large" Small Scale Enterprises (LSSE's).

Furthermore, it is worth pointing out that the term SSE's will be used in this report to mean the following:

firms employing between 10 and 200 employees and the current value of their fixed assets not exceeding LE 500 thousand. Moreover, whenever the term "SSE's sector is used, it will mean artisans and SSE's (1).

Having reviewed the current definitions of SSE's in Egypt, in addition to suggesting four definitions for subdividing the SSE's sector, the report proceeds to review the common characteristics shared by Egyptian SSE's. Furthermore, the role played by SSE's in each industrial subsector is briefly examined.

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(1) Artisans are firms employing less than 10 individuals.

The next section of this report reviews briefly the Public Agencies which SSE's have to deal with before beginning operations, and throughout the life of the project.

The following section of this report examines the use of credit by SSE's. Hence, the credit needs of SSE's, whether short term working capital financing, or medium term financing of fixed assets are outlined. A brief overview of loans granted to the Private Sector, in general, and Egyptian industry, in particular, are outlined.

Section VI examines the constraints and problems which have hindered the growth and productivity of SSE's. Hence, constraints related to SSE's production, labor, raw materials, marketing, credit, as well as, other contraints, are briefly discussed. Moreover, laws and regulations which have been restricting SSE's activities are briefly addressed.

Having examined the background setting where SSE's have to operate, the report proceeds to suggest two credit programs which respond to SSE's needs. The objective of the two credit programs are outlined. For instance, one of the major problems constraining SSE's from operating at full capacity is the lack of liquidity for financing working capital. Thus, a "Working Capital Credit Program" is proposed in order to provide SSE's with the needed credit for financing their working capital.

The first credit program is short term by its nature. Thus, its maturity is up to one year. The currency of payment and repayment is local currency for off-the shelve purchase of raw materials and intermediate goods. All other terms of the proposed Working Capital Credit Program are outlined in the report.

The second credit program proposed in this report is a Medium Term

facility. This credit program is suggested to assist SSE's in dealing with another constraint which has prevented a large number of these firms from operating at full capacity. The constraint in question is the outdated, worn-out and highly depreciated machinery and equipment used by a large number of SSE's. Machine break-down has resulted in a large number of SSE's operating while 50% of their machinery is being repaired. However, very often the needed spare parts are not available and have to be manufactured in a local shop. This implies that time devoted to repairing SSE's machinery prevents the equipment from being used in the production of goods (which is their primary function). Egyptian banks have been reluctant to meet SSE's demand for credit. This is due to the fact that a large percentage of SSE's do not have the required collateral. The value of collateral requested by Egyptian banks may reach 200% to 300% of the loan amount. The majority of SSE's do not own the land and/or the buildings where their businesses are located. Thus, SSE's do not own the two most important collateral requested by banks. Hence, a large percentage of SSE's loan requests are turned down. It is believed that the proposed term lending facility fills a market gap for SSE's credit needs.

Furthermore, the purpose of the Medium Term Credit Program is to provide SSE's with the required foreign exchange for importing US equipment and machinery. In order to make this second credit program attractive, a two year grace period is suggested. In addition, the repayment period is five years. Other terms of the Term Credit Program are outlined in the report.

In order to entice banks to participate in the two proposed USAID

credit programs, several options are suggested. These options are divided into two categories.

The first category includes four options such as:

1st: the Interest Spread Option

2nd: the Reverse Interest Spread Option

3rd: Percentage For Funds Management Option

4th: Fee Per Loan Granted Option.

Only one of the above options should be considered for adoption by USAID. It is worth pointing out that banks participation depends on the kind of incentives they may obtain from the proposed SSE's credit programs.

The second category of options includes the following:

. A Credit Guarantee Fund

. Training of Participating Banks Personnel.

From banks' point of view, the last two options should be the key factors for the success of the two proposed credit programs. On one hand, the "Credit Guarantee Fund" should serve the following two purposes:

1st: provide participating banks with some security. Thus reducing their perceived risk exposure when serving a clientele, i.e., SSE's, which they have been reluctant to accommodate.

2nd: reduce the amount of requested collateral by participating banks.

On the other hand, the training of participating banks personnel option would be on a grant basis. It should prove very attractive from banks' point of view, since it increases the proficiency of their employees for carrying out their daily duties.

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It is suggested that five banks should participate in each proposed credit program. Each bank will be allocated $4 million. Thus, bringing total funding to $40 million for the first year of the SSE's credit programs.

Furthermore, the "Fee Per Loan Option" which is more likely to be adopted, should cost about $200 thousnad per bank. This will bring the overall cost of this option to $2 million per year. Furthermore, the "Credit Guarantee Option" would require a USAID contribution between $3 to $4 million for establishing it. The "Credit Guarantee Fund" requires equal contribution by the GOE. It is expected that the bulk of US-AID's and GOE's contribution to the "Credit Guarantee Fund" would be retrieved by them at maturity.

The "Training of Participating Banks Personnel Option" should cost between $65 thousand and $130 thousand, assuming that the courses have to be specifically designed for this group of banks employees. Otherwise if the training courses have already been designed by AUC, or other similar institutions, then it is expected that the regular tuition per student will be applied. This tuition will cost a lot less than the one stated above.

It is hoped that this report would achieve its two previously stated objectives. Moreover, it is hoped that the two proposed credit programs are adopted to assist the SSE's sector to achieve its goals of productivity and growth in income, employment and investment. In addition to improving the quality of SSE's products which should lead to import substitution and/or exports. In either case, the Egyptian economy and the Egyptian people would be the real beneficiaries of the two proposed credit programs.

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II. The Private Sector's Role in Egyptian Industry

A. Introduction

The Private Sector's Role in the Egyptian economy in general and industry in particular, has been steadily growing since the adoption of the Open Door Policy in 1974. Data from the Ministry of Industry for FY 83/84, (Table 1), indicates that Private Sector's share of the gross value of industrial output is about 34.3%, or LE.2,929.4 million. These figures do not include the industrial output of artisinal firms, i.e., firms with less than 10 employees because these establishments are not under the Ministry of Industry's supervision. The output of artisans engaged in industrial type activities is estimated at 15% of total industrial output. Thus, the inclusion of the Private Sector's industrial production of both the formal and informal sectors would result in Private Sector's share of total industrial output in excess of 34.3%.

The importance of the role played by the Egyptian Private Sector in the Egyptian economy in general, and in the Industrial Sector in particular, can best be described in terms of its share in investment, industrial output, employment, industrial exports and the number of industrial firms. A brief examination of the role played by the Private Sector in total investment, industrial employment and exports and the number of industrial firms is warranted.

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B. Investment

The Importance of the Private Sector's role in the Egyptian economy can be demonstrated by the fact that total private investment, from 1977 to FY 1981/82, amounted to LE 3.3 billion which represents 18.3% of total investment. Moreover, the Federation of Egyptian Industries (FEI) reports that Private Sector's contribution to GDP in FY 81/82 amounted to 48%. In the Five Year Plan (1982/83 - 1986/87) the GOE estimates that total Private Sector investment is about LE 8.3 Billion. This represents 23.3% of total investment in the Five Year Plan and includes both the productive and services sectors of the economy. Moreover, it is estimated that total fixed investment for the Private industrial sector (including mining as specified in the plan for 1983/84) was about LE 328 million. This represents 22.8% of total fixed investment for the industrial and mining sectors. The role of the Private Sector in industry is signigicant in the following subsectors:

Leather and Woodworking Products, Mining and Refractories, Foodstuffs, Chemicals, Textiles and Ready Made Garments. A large Final goods represent the majority (or bulk) of Private Sector's output.

However, the Private Sector's role in the production of intermediate goods is also increasing. Furthermore, it is expected that its role in the production of building materials and some capital goods will also be expanding in the coming years.

The increasing importance of the role played by the Private Sector is evident by the fact that since the adoption of the Open Door Policy in 1974 and until the end of June 1983, 1653 projects were

approved by the Investment Authority. Total Investment of these projects was estimated at LE 11.5 Billion, while total equity was about LE 6.5 Billion. The above figures exclude projects whose approvals were revoked because no serious action was taken for implementing them. Table 2 and Table 3 depict the status of projects, formed under LAW 43 of 1974, by of the end of FY 82/83. Furthermore, Table 3 shows that 51% of Law 43 projects are in actual production, while 25% were under construction by the end of FY 82/83. Total investment for projects which are in operation and those which are under construction amount to LE 7,001 million. Total equity for both project categories are estimated at LE 3,795 million.

Table 4 shows that the contribution of the Egyptian Private Sector to the total equity of Law 43 projects is 33%. This is the largest percentage contribution in the equity of these projects. The Public Sector contributed 23%, while Arab investors' contribution was 30% and foreign investors 14%. This demonstrates the importance and the growing role played by the Private Sector in the Egyptian economy since the liberalization Laws of 1974. The 1653 projects approved under Law 43 are expected to provide employment for 224 thousand individuals with total wages and salaries estimated at LE 349 million. Projects which have already began operations provides employment for 74 thousand individuals. The total wage bill for these projects was about LE 149 million which implies that the average annual salary for those employed in these projects is LE 2014.

It is worth pointing out that in the past few years 560 projects were formed under Law 59 with a total equity of about LE 1,353 million.

These projects are 100% owned by Egyptians. On the other hand Egyptians' participation in the equity of Joint Venture projects is about LE 2,290 million. Based on the above, it becomes evident that the Private Sector has been revived and continue to grow and its contribution to total investment and employment has been steadily rising since the adoption of the Open Door Policy in 1974. However, new sitmulus to the Private Sector in credit and technical assistance will strengthen the role it plays in the Egyptian economy and should lead to more growth of this important sector.

Table - 1

Public and Private Sectors Share of Industrial Output

(1983 - 84) Million LE (Current Prices)

Industr.Subsect.	Gross Value of utput 1983/84	Public Sector Output	Private Sector Output	Public Sector Output	Private Sector Share %
Textiles and R.M.	1,905.1	1,411.5	493.6	74%	26%
Foodstuffs	2,595.6	1,842.9	752.7	71%	29%
Chemicals	938	681.2	256.8	72.6%	27.4%
Engineering and Metallurgy	1,912.2	1,596	316.2	83.5%	16.5%
Mining and Refract.	191.1	87.5	103.6	45.8%	54.2%
Woodworking Prod.	425.5	-	425.5	-	100%
Leather Products	581	-	581	-	100%
Total	8,548.5	5,619.1	2,929.4	65.7%	34.3%

Source: Ministry of Industry

Table 2

Number of Law 43 Projects and Their total Investment

From 1974 - FY 82/83

Projects Type	Number of Projects	Total Equity Million LE	Total Investment Million LE
In-Land Projects	1302	5348	10028
Free Zone Projects	351	1172	1453
Total	1653	6520	11481

Source: Investment Authority's Report for FY 82/83.

Table 3

Implementation Status of Law 43 Projects from 1974 - FY 82/83

Projects Status	Number of Projects	Percentage	Total Equity	Total Investment
Projects In Operation	834	51%	2222	3310
Projects Under Constr.	420	25%	1573	3691
Projects with No Action	252	15%	1236	2683
Projects with New Approvals	147	9%	1489	1797
Total	1653	100%	6520	11481

Source: Investment Authority's Report for Fiscal Year 82/83

Table 4

Contribution of the Public and Private Sectors, Arabs and Foreigners in the Equity of Law 43 Projects

Contribution of	Equity Contribution (Million L.E.)	Percentage Contribution
Public Sector	1467	23%
Private Sector	2176	33%
Arabs	1925	30%
Non Arabs	952	14%
Total	6520	100%

Source: Investment Authority's report for FY 82/83

C. Industrial Production

According to the Ministry of Industry the gross value of manufacturing output increased, in nominal terms, in FY 83/84 by 16.6% (from LE 7,323.7 million to LE 8,541 million). Prior to the examination of the performance of each industrial subsector, an understanding of the types of industries comprising each subsector is warranted.

a. Industrial Sub-Sectors

Egypt has not adopted the U.N's International Standard Industrial Classification (ISIC) which classifies industrial activities into 9 major subsectors. Moreover, there is no single classification of industry into various subsectors which has been adopted by Egyptian government agencies and institutions. For instance, the Ministry of Industry classifies industrial production (statistics wise) into 7 different subsectors. On the other hand, the Federation of Egyptian Industries uses 12 different subsectors to report industrial output (including Cinema). Furthermore, the Central Authority For Public Mobilization And Statistics (CAPMAS) classifies industrial production into 20 different subsectors. For the purpose of this report, the Ministry of Industry's classification of industrial output into seven subsectors will be adopted since up-to-date data is readily available. Moreover, this is the same classification used by the IMF and the World Bank in their various reports on Egyptian industry. Thus, a decision was taken to make this report compatible, data-wise, with statistics available from the IMF and the World Bank. On

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the other hand, for reporting the number of firms in each subsector, data from the FEI will be used. Hopefully, the above explanations of the approach to data presentation in this report will help avoid any confusion.

1. The Textiles and Ready Made Garments Subsector

This subsector includes six major industries: spinning, weaving, knitting, dyeing and finishing, ready-made garments, the production of synthetic fibres used in the textile industries and other textile commodities.

In FY 83/84 Public Sector firms accounted for about 74% of total output of this subsector. Private Sector firms accounted for about 26% of total production. Public Sector companies are dominant in spinning, weaving, dyeing and knitting. While privately owned firms dominate the ready -made garments and other apparel products. Private Sector establishments rely heavily on Public Sector companies for most of their raw materials.

From Table 5, it becomes evident that the Textiles subsector ranks second behind Foodstuffs in terms of the percentage contribution to total industrial output with 22.3%.

2. The Foodstuffs Subsector

The Foodstuffs subsector is comprised of six distinct industries, according to the FEI. These industries are: sugar and confectionary products, tobacco and cigarettes, food preservation, edible oil and related products, beverages, milk and dairy products. Cereals, a seventh food industry is included in this subsector with products such as flour, bread, pasta, starch and glucose, etc...

Table 5 shows that in FY 83/84 the Foodstuffs subsector was the largest in terms of its share of manufacturing output with 30.4%. Public sector firms accounted for 71% of total output of this subsector. On the other hand, Private Sector firms accounted for 29% of total output in the same year.

The Public Sector is dominant in the production of edible oils and related products, tobacco and cigarettes, food preservation, sugar and alcoholic beverages. On the other hand, the Private Sector is dominant in milk and dairy products accounting for more than 80% of the value of output.

3. <u>The Chemicals Subsector</u>

The Chemicals Subsector includes the following industries: organic and inorganic chemicals, plastic and rubber products, chemical fertilizers, pharmaceuticals, cosmetics, other chemicals, pulp and paper, and lumber, in addition to Public Sector wood products. Moreover, Public Sector tanneries and footwear are also included in the Chemicals subsector. On the other hand, Ministry of Industry reports data on Private Sector's Woodworking products, Leather products and Footwear in two different categories (subsectors).

In FY 83/84 Public Sector firms'share of the Chemicals subsector output was 72.6% of total production for this subsector. Private Sector establishments accounted for 27.4% of output. The Public Sector dominates the production of fertilizers, inorganic chemicals, industrial gases, rubber and rubber products, pharmaceuticals and other chemicals. The Public Sector also dominates wood (lumber) production, as well as, Pulp and Paper production.

On the other hand, Private Sector establishments play the dominant role in perfumes and cosmetics industries, plastic industries, paints, varnishes and ink. In terms of its relative share of total industrial production, the Chemicals subsector ranks fourth with 11%.

4. The Engineering and Metallurgy Subsector

The Engineering and Metallurgy Subsector includes the following industries: electric and non-electric machinery; transportation equipment; pipes, castings and foundries; valves, fittings,...; basic metals; and basic metals forms.

In FY 83/84 Public Sector enterprises accounted for 83.5% of total production of this subsector. On the other hand, privately owned firms accounted for 16.5% of total output for this subsector. Public Sector establishments dominate each group of industries in this subsector. The Engineering and Metallurgy subsector ranks third in terms of its share of total industrial output with 22.4%

5. The Mining and Refractories Subsector

The Mining and Refractories subsector include the following industries: metallic minerals; non-metallic minerals (except petroleum); refractories; porcelain and chinaware; glass and crystal. In FY 83/84, Public Sector enterprises accounted for 45.8% of Mining and Refractories output. Moreover, Privately owned establishments contributed 54.2% of this subsector's output.

The Mining and Refractories subsector is the smallest (with 2.2%) in its share of industrial output.

6. Woodworking Products Subsector

The Woodworking Products subsector includes primarily the production

of furniture; doors, windows frames and floor tiles.

Private Sector establishments account for 100% of the total Woodworking output.

The Woodworking Products subsector ranks sixth in terms of its contribution total industrial production with 5%. It is worth pointing out that the output of Woodworking Products is sometimes included with the Chemicals subsector by the Ministry of Industry.

7. Leather Products Subsector

The Leather Products subsector includes primarily the production of footwear and other leather products such as, handbags, luggage, belts and wallets,etc...

Private Sector enterprises account for 100% of leather Products output. The Leather Products subsector is fifth in terms of its contribution to industrial output with 6.8%.

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b. Industrial Subsector's performance

The following is a brief examination of the performance of each industrial subsector in FY 83/84. Note that all output figures represent current prices. Thus, rates of growth represent, nominal, rather real rates.

1. The Textiles and Ready Made Garments Subsector

   Growth in this subsector is estimated at 7.2% as evidenced by the rise in the value of output from LE 1,77.1 million to LE 1,905 million.

2. The Foodstuffs Subsector

   Gross value of output of this subsector increased by 25.3% (from LE 2,071.5 million to LE 2,623 million).

3. The Chemicals Subsector

   The value of this subsector's output increased from LE.758.9 million to LE 938, million i.e., at a rate of 23.6%.

4. The Engineering and Metallurgy Subsector

   The gross value of production of this subsector achieved a 12.3% increase (from LE 1,702.8 million to LE 1,905 million).

5. The Mining and Refractories Subsector

   The gross value of output of this subsector grew at about 14.8% as evidenced by the increase from LE 166.5 million to LE 191.1 million.

6. The Woodworking Products Subsector

   Gross value of production for this subsector grew at a rate of 29.6%. from LE 327.9 million to LE 425 million.

7. The Leather Products Subsector

Gross value of output of the leather industries grew at the rate of 12%, from LE 519 million to LE 581 million.

Table 5 shows the gross value of output of the various industrial subsectors, in FY's 82/83 and 83/84, the rate of growth achieved by each subsector (at current prices), and the percentage contribution of each subsector to the total value of industrial production.

From Table 5, it is possible to arrange the various sebsectors in FY 83/84 in terms of their percentage contribution to the value of industrial output as follows:

1st: Foodstuffs with 30.7%;

2nd: Textiles and Ready Made Garments with 22.3%

3rd: Engineering and Metallurgical Products with 22.3%

4th: Chemicals with 11%;

5th: Leather Products with 6.8%;

6th: Woodworks Products with 5%;

7th: Mining and Refractories with 1.8%.

D. Private Sector's Industrial Output

The gross value of the private sector's industrial output increased from LE 2,244.7 million in FY 82/83 to LE 2,929.3 million in FY 83/84. This reflects a 30.5% rate of growth for FY 83/84. Furthermore, the contribution of the Private Sector to the value of industrial production represents 34.3% of the total. These statistics reflect only the output of registered firms with the FEI and which are under the supervision of the Ministry of Industry. Thus, the output of unregistered firms which are currently estimated at 3,000 do not show up in the provided

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statistics. Thus, the contribution of the Private Sector to total industrial output must exceed 34.3%. Furthermore, the contribution of artisans, i.e., firms with less than 10 employees do not show up in statistics provided by the Ministry of Industry. The World Bank estimates that the number of these artisinal firms engaged in industrial type activities is 250 thousand establishments. The output of these artisinal firms are estimated at around 15% of total industrial production as reported by the Ministry of Planning. This fact, when taken into consideration, leads to the conclusion that the actual contribution of the Private Sector to the value of industrial output must definitely be much larger than 34.3%. This conclusion is supported by the fact that privately owned industrial firms usually under-report their output, income, investment and employment for the usual reasons. In addition, the bitter memories of the mass nationalizations of most firms with more than 50 employees are still very fresh in the minds of owners of factories in Egypt.

The nominal growth of total industrial production generated by the Private Sector from FY 82/83 to FY 83/84 can be attributed to the growt of each subsector as follows:

1. Textiles and Ready Made Garments

   The gross value of output of this subsector increased from LE 460.1 million to LE 493.6 million. This indicates a 7.3% annual rate of growth.

2. Foodstuffs

   The gross value of output of this subsector increased from LE 407.3 million to LE 752.7 million. This reflects a 84.8% annual rate of

growth.

3. Chemicals

This subsector achieved a 62% annual rate of growth since the gross value of output increased from LE 158.5 million to LE 256.8 million.

4. Engineering and Metallurgical Products

This subsector grew at an annual rate of 13% reflecting the increase in the value of output from LE 279.8 million to LE 316.2 million.

5. Mining and Refractory Products

The value of output of this subsector increased from LE 92.1 million to LE 103.6 million reflecting a 12.5% growth rate for this subsector.

6. Woodording Products

The value of output of this subsector increased from LE 327.9 million to LE 425.5 million. This implies a 29.8% annual rate of growth for this subsector.

7. Leather Products

The value of production of this subsector increased from LE 519 million to LE 580.9 million. This indicates about a 12% annual growth rate for this subsector.

The relative contribution of each subsector to the total value of Private Sector industrial output can be expressed as follows:

1st: Foodstuffs with 25.7%

2nd: Leather Products with 19.8%

3rd: Textiles and Ready Made Garments with 14.5%

4th: Woodworking Products with 14.5%

5th: Engineering and Metallurgical Products with 10.5%

6th: Chemicals with 8.8%

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7th: Mining and Refractory Products with 3.5%

Table 5 presents the gross value of industrial production in FY'S 82/83 and 83/84.

Table 5

Gross Value of Industrial Output

(In million of LE. at current prices)

Industr Subsectors	1982/83	1983/84	%Change	Subsector Contribution 82/83	% Subsector Contrib % 83/84
Textiles and R.M. Garments	1,777.1%	1,905.1	7.2%	24.3%	22.3%
Foodstuffs	2,071.5	2,595.6	25.3%	28.3%	30.4%
Chemicals	758.9	938	23.6%	10.4%	11%
Engineering and Metallurg.Products	1,702.8	1,912.2	12.3%	23.3%	22.4%
Mining and Refract. Products	166.5	191.1	14.8%	2.3%	2.2%
Woodworking Prod.	327.9	425.5	29.6%	4.5%	5%
Leather Products	519.0	581	12%	7.1%	6.8%
Total	7,323.7	8,548.5	16.7%	100%	100%

Source: FEI and Ministry of Industry.

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Table 6

Grosas Value of Private Sector's Industrial Output

(In millions of LE. at current prices)

Industr. Subsectors	1982/83	1983/84	% Change	Subsector % Contrib. 82/83	Subsector % Contrib. 83/84
Textiles and R.M. Garments	460.1	493.6	7.3%	20.5%	16.9%
Foodstuffs	407.3	752.7	84.8%	18.2%	25.7%
Chemicals	158.5	256.8	62%	7.1%	8.8%
Engineering and Metallurg. Products	279.8	316.2	13%	12.5%	10.8%
Mining and Refract. Products	92.1	103.6	12.5%	4.1%	3.5%
Woodworking Products	327.9	425.5	29.8%	14.6%	14.5%
Leather Products	519	581	12%	23%	19.8%
Total	2,244.7	2,929.3	30.5%	100	100

Source: FEI and Ministry of Industry

Table 7

Public and Private Sectors Share of Manufacturing Output 1983 - 84

Indust.Subsect.	Gross Value of Output 1983/84	Public Sector Output	Private Sector Output	Public Sector Share %	Private Sector Share %	Subsectors Share %
Textiles & R.M.	1905.1	1411.5	493.6	74%	26%	22.3%
Foodstuffs	2595.6	1841.9	752.7	71%	29%	30.4%
Chemicals	938	681.2	256.8	72.6%	27.4%	11%
Engineering & Metallurgy	1912.2	1596	316.2	83.5%	16.5%	22.4%
Mining and Refractories	191.1	87.5	103.6	45.8%	54.2%	2.2%
Woodworking Products	425.5	-	425.5	-	100%	5%
Leather Products	581	-	581	-	100%	100%
Total	8,548.5	5,619.1	2,929.4	65.7%	34.3%	100%

Source : FEI and Ministry of Industry.

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Table 8

Gross Value of SSE's Manufacturing Output 1983/84

(in Millions of LE. at current prices)

	VSSE's Output	% of Private Sector	% of Total Subsector
Textiles	246.8	50%	13%
Foodstuffs	451.6	60%	17.4%
Chemicals	89.9	35%	9.6%
Engineering and Metallurgy	268.8	85%	14.1%
Mining and Refractories	41.4	40%	21.17%
Woodworking Products	148.9	35%	35%
Leather Products	552	95%	95%
Total	1799.4	61.4%	21%

Source: FEI, Ministry of Industry and Mission's estimates

E. Employment in the Industrial Sector

The Ministry of Industry estimates that there were 1,568.7 thousand individuals employed in the formal and organized industrial sector in FY 83/84 vs. 1,466.2 thousand in FY 82/83. This represents almost a 7% rate of growth in the industrial labor force. It should be emphasized that the above figures for total employment in Egyptian manufacturing do not include employment in the artisinal sector. The reason for this is that artisans are not under the supervision of the Ministry of Industry. The number of artisanal firms which are involved in industrial type activities is estimated at 250 thousand. Based on Mission's estimates, the employment in the artisinal sector is around 1 million individuals. This brings total employment in formal and organized industry, as well as, the informal industrial sector at 2,568.7 thousand persons in FY 83/84.

The number of individuals employed in the industrial Public Sector in FY 83/84 was 612.3 thousand which represents about 39% of the total labor force in formal and organized industry. On the other hand, the number of individuals employed in the private industrial sector (excluding artisinal employment) in FY 83/84 was 956.4 thousand. This represents 61% of the total labor force of the formal industrial sector. Employment in the Public Sector increased by 62 thousand individuals between FY's 82/83 and 83/84. This represents about 1% annual rate of growth which is below the 7% rate of growth for the industrial labor force in FY 83/84. The annual rate in increase of the private industrial labor force in FY 83/84 was 11.2%. There were an additional 96.3 thousand persons employed in FY 83/84 than in FY

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82/83. It is worth pointing out that the actual number of employees in the formal private industrial sector in FY 83/84 should be more than double the estimated 956.4 thousand (or 61% of total industrial employment). This is due to the fact that privately owned firms have a tendency to under-report the number of their employees to avoid paying social security taxes, as well as, other taxes. Furthermore, since the Public Sector suffers from accute disguised unemployment, effective employment, percentage wise, should be much less than the 39%, once this problem is addressed by the GOE. The total wage bill for employees of the industrial Public Sector in FY 83/84 was LE 1,026.3 million. This implies that Public Sector's annual per capita wages and salaries in FY 83/84 was about LE 1,676. On the other hand, total wages and salaries in the Egyptian private industrial sector in FY 83/84 was LE 934 million. Once more this figure is understated by about one third based on the general practice of Private Sector firms to under-report the salaries of their employees in order to reduce their social security and income taxes. However, based on the Ministry of Industry's data, the per capita annual wage in the industrial Private Sector in FY 83/84 is about LE 977. The actual annual average wage in the Private Sector should be about LE 2,930. This conclusion is reasonable since it is quite impossible for per capita wages and salaries in the Public Sector to be greater than the equivalent in the Private Sector.

Based on the above, the importance of the role played by the Private Sector in Egyptian industry in terms of employment and total employees' income becomes quite evident.

F. Private Sector's Industrial Exports

The Private Sector's industrial exports increased during FY 83/84 by 41.3%, from LE 50.1 million to LE 70.9 million (in nominal prices). Table 9 shows Private Sector's industrial exports for FY's 82/83 and 83/84. Examination of Table 9 provides the following explanation to how the 41.3% annual increase in the value of Private Sector's industrial exports were achieved.

1st: Exports of Chemical industries increased by 110.6% (from LE 19.4 million in FY 82/83 to LE 40.8 in FY 83/84).

2nd: Exports of Khan El Khalili Products increased by 62.5% (from LE 2,190 thousand in FY 82/83 to LE 3,559 thousand in FY 83/84.

3rd: Exports of Woodworking industries increased by 54.6% (from LE 2,926 thousand in FY 82/83 to LE 4,523 thousand in FY 83/84).

4th: Exports of Foodstuffs industries increased by 24.1% (from LE 3,300 thousand in FY 82/83 to LE 4,094 in FY 83/84).

Other Private Sector's industrial exports declined during FY 83/84. Despite that decrease, the exports of the remaining industrial sectors increased by a larger percentage. Thus, the overall exports of the private industrial sector achieved a 41.3% annual rate of growth in FY 83/84.

In FY 83/84, the following Private Sector's industrial exports declined:

1st: Building Materials exports declined value wise by 39.2% (from LE 153 thousand in FY 82/83 to LE 93 thousand IN FY 83/84).

2nd: Textiles and Ready Made Garments exports declined by 23.9% (from LE 9,578 thousand in FY 82/83 to LE 7,287 thousand in FY 83/84).

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3rd: Metallurgical industries exports decreased by 21.3% (from LE 9,472 thousand in FY 82/83 to LE 7,287 thousand in FY 83/84).

4th: Leather industries exports decreased by 2.3% (from LE 3,153 thousand in FY 82/83 to LE 3,080 thousand in FY 83/84).

The relative contribution to the value of Private Sector industrial exports by each industrial subsector in FY 83/84 can be expressed as folows:

1st: Exports of Chemicals industries with 57.5%;

2nd: Exports of Metallurgical industries with 10.5%;

3rd: Textiles and Ready-Made Garments with 10.3%;

4th: Woodworking industries with 6.4%;

5th: Foodstuffs industries with 5.8%;

6th: Khan El Khalili products with 5%;

7th: Leather industries with 4.4%;

8th: Building Materials products with 0.1%

Table 10 depicts the exports of the Private and Public sectors at current prices from 1975 until FY 1983/84. It can be noted that the percentage contribution of Private Sector's industrial exports to total industrial exports decreased from 27.4% in 1975 to 10.9% in 1983. This gradual decline in the percentage of Private Sector's contribution to total exports of the industrial sector may be attributed to the following reasons:

1. A gradual decline in industrial exports to the Eastern Bloc nations.
2. Local demand for industrial products has been growing rapidly. This encourages entrepreneurs to try to satisfy this local demand

and ignore exports.

3. Egyptian laws governing exports of industrial goods may have been a hinderance to Private Sector's entrepreneurs efforts for exporting their products.

The role played by Private Sector's industrial exports is not as substantial, percentage wise, as its contribution to the value of industrial output and employment. However, Private Sector's industrial exports especially in Textiles and Ready Made Garments, as well as, Food Processing should be targetted for the proper credit programs for exports promotion. The benefits which can accrue to the Egyptian economy in terms of a source of foreign exchange earnings should lead to a positive balance of payments and trade.

G. Number of Industrial Firms Operating in Egypt:

a. Overview

A 1985 publication of the Federation of Egyptian Industries (FEI) reports that based on their membership records there are 10,000 Private and Public Sector industrial firms in Egypt. The number of Public Sector industrial firms is 330 (1). This implies that there are 9,670 Private Sector industrial firms which are members of the FEI.

It is estimated that the actual number of private industrial enterprises operating in Egypt with 10 or more employees exceeds the FEI memberships by about 35%. This implies that the actual number of privately owned industrial enterprises is roughly about 13,000.(2)

It has been the practice in Egypt for privately owned industrial firms to under-report the number of their employees and the value of their fixed assets in order to avoid paying taxes and to avoid paying the annual membership fees for joinig Public Organizations such as the FEI.(3)

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(1) This figure includes one Public Sector firm involved in the production of motion pictures.

(2) A recent World Bank report estimates that the number of artisinal firms exceeds 250 thousand. Artisans are defined as establishments employing between 1 and 9 workers.

(3) Although in March 1985, the FEI reports that the number of industrial firms which are members at the Federation is 10,000, detailed breakdown of these firms by subsector was not available at the writing of this report.

b. Number of Industrial Firms Registered with the Federation of Egyptian Industries (FEI)

i) The number of industrial establishments which are members of the FEI as of February 1985 is 10,000.

ii) The number of Public Sector industrial firms is 329.

iii) The total number of privately owned industrial enterprises is 9,670.

iv) It is estimated that about 90.6% of the Private Sector industrial firms employ between 10 to 50 individuals, i.e., 8,761.

v) It is estimated that about 8% of the privately owned firms employ between 51 to 200 workers, i.e., 774.

vi) It is estimated that 1.4% of private sector establishments employ more than 200 employees, i.e., 135.

c. Estimated Number of Privately Owned Industrial Firms in Egypt

Based on data provided by the FEI and discussions with various GOE officials and/or experts in the field of industry, it is estimated that the actual number of privately owned industrial firms operating in Egypt exceeds the FEI's memberships by approximately about 35%. This brings the total number of Private Sector industrial firms to about 13,000, as of March 1985.

i) It is estimated that about 90.6% of these firms, i.e., 11,774, employ between 10 to 50 individuals.

ii) The number of firms employing between 51 to 200 individuals is estimated to be around 1,040. This represents 8% of the estimated total number of industrial firms.

iii) The number of Private Sector firms employing more than 200

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Table 9

Value of Industrial Exports (at current prices)

Thousand LE.

Industrial Exports	Year 1982/83	Year 1983/84	Relative Percentage 82/83	Relative Percentage 83/8
Leather	3153	3080	6.3%	4.4%
Khan El Khalili	2190	3559	4.4%	5%
Woodworking	2926	4523	5.8%	6.4%
Chemicals	19536	40767	38.6%	57.5%
Textiles	9578	7287	19.1%	10.3%
Foodstuffs	3300	4094	6.6%	5.8%
Metallurgy	9472	7451	18.9%	10.5%
Construction Materials	153	93	0.3	0.1%
Total	50128	70854	100%	100%

Source: FEI, Ministry of Industry and CAPMAS.

Table 10

Value of Public & Private Industrial Exports

(Current Prices)

(Million LE).

Year	Public Sector	Private Sector	Total	% Public	% Private
1975	155.7	58.9	214.6	72.6%	27.4%
1976	162.8	44.3	207.1	78.6%	21.4%
1977	207	43	250	82.8%	17.2%
1978	178	44	222.1	80%	20%
1979	210	62	272.4	77.2%	22.8%
1980	420	72	492.	85.4%	14.6%
1981/82	429.8	55.9	485.7	88.5%	11.5%
1982/83	431.8	50.1	481.9	89.6%	10.4%
1983/84	578.2	70.8	649	89%	11%

Source: FEI, Ministry of Industry and CAPMAS

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Table 11

Public and Private Industrial Firms (Number and Relative Importance

January 1985

Industries	Public Sector	Private Sector	Total	Percentage Public Sector	Percentage Private Sector	Percentage Subsector
Leather	3	4654	4657	0.1%	99.9%	34.9%
Textiles	42	2730	2772	1.5%	98.5%	20.8%
Engineering	56	1628	1684	3.3%	96.7%	12.6%
Printing Paper	19	1164	1183	1.6%	98.4%	8.9%
Foodstuffs	38	849	887	4.3%	95.7%	6.7%
Chemicals	44	829	873	5%	95%	6.6%
Building & Construction	60	476	536	11.2%	88.8%	4%
Woodworking	20	382	402	5%	95%	3%
Cereals	19	180	199	9.5%	90.5%	1.5%
Petroleum & Mining	18	49	67	27%	73%	0.5%
Metallurgy	10	59	69	14.5%	85.5%	0.5%
Total	329	13,000	13,000	2.5%	97.5%	100%

Source: Mission Extimates Based on FEI Statistics.

Table 12

Estimated Number of (Private Sector)Industrial Firms

Industries	Firms with 10-50 Employees	Firms with 51-200 Employees	Firms with More Than 200 Employees	Total
Leather	4593	48	13	4654
Textiles	2304	366	60	2730
Engineering	1594	31	3	1628
Printing & Paper	1106	58	-	1164
Foodstuffs	690	132	27	849
Chemicals	637	141	51	829
Building & Construction	463	8	5	476
Woodworking	275	84	23	382
Cereals	54	126	-	180
Petroleum & Mining	-	45	4	49
Metallurgy	58	1	-	59
Total	11,774	1,040	186	13,000
Percentage	90.6%	8%	1.4%	100%

Source: Mission's estimates based on data from the FEI.

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III. Small Scale Industrial Enterprises Operating in Egypt

A. Definitions of Small Scale Enterprises

There is no single definition of small scale enterprises which is universaly adopted by every public institution in Egypt. The only known definitions of this sector of the economy are the ones which have been adopted by DIB and the Ministry of Planning. The definitions which are currently in effect at DIB differentiate between artisans, "very" small scale enterprises (VSSE's) and small scale enterprises (SSEs), as follows:

a. Artisans are defined as firms with 9 employees or less

b. Very Small Scale Enterprises are defined as firms with fixed assets not exceeding LE 250 thousand excluding land and buildings

c. Small Scale Enterprises are defined as firms with fixed assets worth more than LE 250 thousand but not exceeding LE 500 thousand, excluding land and buildings.

A yearly adjustment of the above definitions is based on some price index prepared by CAPMAS.

On the other hand, the Ministry of Planning defines small scale industrial establishments as follows:

- firms employing less than 25 employees; and
- the value of their fixed assets, including land and buildings is less than LE 50 thousand; and
- using machinery with less than 10 Horse Power.

Other Egyptian public institutions and/or agencies do not have a clear cut definition for small scale industrial establishments, but attempt to differentiate between formal and organized firms, on one hand, and informal and artisanal firms on the other. For instance, the

Ministry of Industry considers all enterprises with capital assets exceeding 8,000 LE as industrial firms, while those with less capital than the level stated above are considered as artisans. It is apparent that the Ministry of Industry does not have a specific definition of small scale industrial enterprises.

On the other hand, the Federation of Egyptian Industries (FEI) recognizes industrial establishments with LE 5,000 in capital or 25 employees as the minimum size of establishments which are required by law to become members. The Federation does not have a specific definition of SSE's despite the fact that in several of its publication and/or annual reports it addresses the performance, problems and constraints impeding the growth of SSE's without any attempt to specify their definition of SSI. One can state that the Federation considers all industrial establishments which cannot fulfill their membership requirements as artisans and part of the Egyptian informal sector. From the above, one can infer that no attempt by Egyptian authorities and/or public agencies and institutions has been made to adopt the SSE's definitions put forth by international organizations such as the World Bank, UNIDO, and the ILO, to name but a few.

The World Bank defines small scale industrial firms as those employing between 10 to 50 employees. This definition did not receive any acceptance by Egyptian authorities. Even though DIB is the single Egyptian entity which has put forth definitions of small scale enterprises, still it does not take the number of employees into consideration in its own definitions.

A possible option, which is suggested here, is to associate DIB's

three definitions with a specification of the number of individuals employed by firms. The following classification of the SSE's sector is suggested for adoption:

1. Artisans: should be defined as firms employing less than 10 workers.
2. Very Small Scale Enterprises (VSSE's): should be defined as firms employing between 10 and 50 workers and the value of their fixed assets not exceeding LE 250 thousand, excluding land and buildings.

   This is a modification of DIB's definition of VSSE's since it combines it with some specification of the number of employees per firm. Note that the value of fixed assets included in this definition is usually changed every year. This change takes into consideration CAPMAS directives for an annual inflation rate.
3. "Average" Small Scale Enterprises (ASSE's): should be defined as firms employing between 51 and 100 individuals and the value of their fixed assets not exceeding LE 350 thousand, excluding land and buildings. The value of ASSE's fixed assets, as specified in this report, should be adjusted yearly using the same inflation rate advocated by CAPMAS.
4. "Large" Small Scale Enterprises (LSSE's): should be defined as firms employing between 101 and 200 individuals and the value of their fixed assets not exceeding LE 500 thousand, excluding land and buildings. This is DIB's definition of small scale enterprises slightly modified for taking the number of employees per firm into consideration.

This definition should undergo yearly adjustments for the value of firms'fixed assets. This yearly modification should be identical to the change in DIB's definition of SSE's.

Having proposed the above definitions which classify firms into four categories, it is worth pointing out the following terminology:

1. Small Scale Enterprises (SSE's): should mean firms employing between 10 and 200 workers and the current value of their fixed assets not exceeding LE 500 thousand, excluding land and buildings.
2. The Small Scale Enterprises Sector: The SSE's sector should include all firms employing not more than 200 individuals and the current value of their fixed assets not exceeding LE 500 thousand, excluding land and buildings.

B. Characteristics of Egyptian Small Scale Enterprises

In this section, the major characteristics of SSE's operating in Egypt are briefly outlined.

a. Management Practices

A large number of SSE's are family owned or partnerships. Moreover, a large percentage of these enterprises are managed, by the owner(s). This characteristic is emphasized even stronger by the dislike of most owners for multiple plants or distribution centers or off-premises sub-assembly operations. In addition, most enterprises are located close to the owner's home. Usually, the owner, his wife, brothers and other relatives supervise the production area and handle day-to-day operations. Managerial skills of strategic planning, management by objective, forecasting cash flow for identifying possible shortages, reinvestment of current profits for future gain, have not been adopted nor have they been developed by the majority of SSE's owners/managers.

The majority of managers of these enterprises do not perceive any need for improving their administrative skills and style, which they strongly believe are more than appropriate for handling financial, accounting, production and marketing issues of their business. A. D. Little's study indicated that managers/owners of these firms do not perceive any need for assistance to improve these skills.

Egyptian entrepreneurs can be characterized as being dedicated, hard workers, ingenious and trying to do their best despite the various institutional constraints they are faced with.

b. Production Technology

In terms of production technology and processes, one can classify firms operating in the Egyptian Private Sector into the following categories:

1. Large firms, usually joint venture firms, which use the latest in modern technology and relatively sophisticated equipment.

2. Next, we find firms which have modernized part of their machinery, but still use outdated technology and processes in the rest of their production facility.

3. Firms which are still using outdated machinery and traditional production processes. These firms are usually labor-intensive.

4. At the bottom of the technological ladder, we find firms employing a small number of workers, few machines, and very primitive production processes. The majority of these firms are unregistered with GOFI.

C. Employment Practices

SSE's entrepreneurs usually perceive one of the major constraints facing their firm is the lack of skilled workers.

This may be due to several factors which include the migration of large numbers of skilled workers to higher wage paying countries such as the Gulf states, the shortage of vocational training centers, and the lack of desire by young men to enter these centers because they wish to obtain a University degree and become white collar employees rather than blue collar workers. In addition, many skilled workers prefer the low wages of Public Sector companies and government factories to the high wages offered by Private Sector firms because of the "security" usually perceived in working for public enterprises. Enterprises which are relatively small (10-50 employees) and whose value of fixed assets is relatively low, cannot attract the skilled workers they need. This is due to the fact that these firms cannot afford to pay them the competitive wages which will either attract them and/or keep them.

Another problem faced by Private Sector enterprises is the relative lack of discipline of Egyptian workers. A large number of workers usually take days off after pay-days. Labor laws favor employees rather than managers/owners. For instance, it is extremely difficult to fire an employee once he is hired, unless it can be proven that he has committed a major offense such as stealing, etc.

d. Raw Material Procurement

Raw material procurement is one of the major problems facing Egyptian SSE's. In many cases raw materials are not available in the required quantity nor the desired quality. Some factories operate at 50 percent (or more) below capacity.

because the supply of raw materials is controlled by the government and its Public Sector enterprises. In other cases where raw materials are not government controlled, and due to the fact that demand exceeds supply, all raw materials procurement are done on a cash basis. This fact has resulted in a bias against smaller enterprises which do not have the ready resources and the staff who can devote the required time and effort for materials procurement.

The source of large quantities of materials and intermediate goods for SSE's is Public Sector companies and government factories. This has caused Private Sector companies, especially the small scale ones, to find themselves in competition with Public Sector companies and government factories for materials and intermediate goods. The low quality of raw materials and intermediate products obtained by SSE's from Public Sector and government enterprises has resulted in low productivity and led to the operation of a large number of Private Sector firms below capacity.

Import restrictions and import rationalization policies and regulations have added to the problems faced by SSE's in their attempt to fulfill their needs of materials and intermediate products. This problem is even more aggravated by the unavailability of foreign exchange on a wide scale at the official exchange rate. Firms seeking to obtain foreign currencies for importing materials and intermediate goods usually obtain the foreign exchange at the market rate, which

is currently higher than the official rate by approximately 12 percent. On the other hand, Public Sector companies and government factories obtain all the foreign exchange they need for importing materials and intermediate products at the official exchange rate. This is just another example of the hardships faced by the Private Sector firms in comparison to Public Sector enterprises.

e. Marketing

SSE's managers/owners do not perceive marketing their products as their firms'major priority. This is due to the fact that SSE's managers/owners strongly believe that the demand for finished goods exceeds the existing supply. Thus, all commodities produced by their factories can be sold without any difficulties. Thus, it can be safely stated that marketing is usually relegated to third place, i.e., after production and finance by SSE's managers/owners.

It is worth pointing out, that SSE's managers, owners use their experience to acquaint themselves about the market needs, as well as, their close competitors. Each firm tries to establish its own niche in the market. Depending on the price and quality of their final products, small scale firms usually establish a clientele for the goods they produce. Very few SSE's owners/managers try to examine market statistics in order to determine the market gap their output should attempt to fill. Although, there is a new trend by new ventures to undertake market studies which may be simple or

elaborate, to determine the market gap their planned factories would attempt to fill. Moreover, market studies try to determine the existing competitors, if any, as well as their productive capacities, major features and prices of their products. Very few SSE's have their own distribution outlets. Deliveries are usually carried out at the factories. Furthermore, the majority of SSE's do not use advertising because they believe it is too costly, In addition, SSE's strongly believe that market demand for their products is greater than their productive capacity, thus there is no need to waste funds on costly advertising campaigns.

A small percentage of SSE's managers/owners believe that exporting their products would increase their profit margins, as well as, provide them with a good source of foreign exchange. These foreign exchange earnings may be used in importing raw materials and/or intermediate products. However, managers/owners have not thought to export their products for the following reasons:

1. the existence of a large and rapidly growing domestic market eager for final products;
2. the burdensome and often complicated exports procedures, laws and regulations;
3. the lack of clear and specific information on the needs and requirements of foreign markets.

It is believed that establishing an information center at the FEI would be very beneficial. The exports information center should provide SSE's, as well as other firms, with the needs and requirements of some specific foreign markets-Egyptian products which have a comparative advantage in foreign markets should be indentified to SSE's.

Hopefully, when SSE's take full advantage of the provided information on foreign markets and do export their products, the benefits which will accrue to these firms will also be passed on to the Egyptian economy as well.

C. Small Scale Enterprises Role in Industrial Sub-Sectors

The importance of the Egyptian Private industrial sector and the key role played by SSE's in it, can best be described by the number of firms and the share of output produced by these small establishments. Table 1 shows the industrial output produced by each subsector and the percentage of this output which can be attributed to the Public and Private Sectors in FY 83/84. On the other hand, Table 8 shows VSSE's share of industrial output in FY 83/84. Furthermore, Tables 11 , , and 12 depict the total number and percentages of Public and Private Sector industrial enterprises operating in Egypt.

In order to highlight the crucial role played by SSE's in the Egyptian Private industrial sector, a detailed examination of each group of industries, based on the FEI classification of its Chambers follows:

1. Leather Industries

Leather industries constitute the largest number of industrial firms with an estimated establishments 4567. This represents about 34.9% of the total number of industrial firms operating in Egypt, i.e., 13,329. There are only 3 Public Sector establishments in this group of industries representing 0.1% of the total number of firms engaged in leather industries. On the other hand, the largest number of Private Sector firms, i.e. 4,654 belong to the Leather industries. This represents 99.9% of

the total number of firms which are part of the Leather industries subsector.

Table 12 classifies privately owned industrial firms producing leather goods by employment size. There are about 4593 firms with 10-50 employees. This represents 98.7% of total private industrial firms in this category. The majority of these firms are relatively small in size with 20 employees or less. It is worth noting that firms in the 10-50 employment bracket contribute about 95% of the gross value of output of this subsector. The number of private firms with 51 to 200 workers is about 48, which represents 1.03% of total private industrial firms. Finally, there are about 13 firms with more than 200 employees. This represents 0.28% of the total number of private firms belonging to this subsector. Overall, VSSE's i.e., firms with 10 to 50 employees dominate Leather industries in terms of their contribution to the gross value of output and the number of firms.

2. Textiles and Ready Made Garments Industries

In terms of the number of industrial firms, Textiles and Ready Made Garments is the second largest group of industries with an estimated 2,772 firms. This represents 20.8% of all industrial firms in Egypt. There are 42 Public Sector enterprises, or 1.5% of the total number of firms. The number of privately owned

firms is estimated at 2,730, i.e., 98.5% of the total number of textile firms.

Examination of Table 12 which classifies Private Sector firms by employment size, we note that 84% of Textiles firms have between 10 and 50 employees, 13.4% have between 51 and 200 employees, and only 2.2% employ more than 200 individuals. Once more, we observe that VSSE's, i.e., firms with 10 to 50 employees dominate the Textiles and Ready Made Garments industries in terms of the number of firms which are estimated at 2,304. Moreover VSSE's account for about 50% of the gross value of Private Sector's output of the Textiles and Ready Made Garments industries VSSE's contribution, estimated at LE 246.8 million, represents 13% of the gross value of output generated by Textile and Ready Made Garments industrial firms.

3. Engineering Industries:

This group of industries contains the third largest group of firms which are estimated at 2,772. There are only 42 Public Sector firms in this group of industries. Public Sector enterprises represent only 1.5% of the total number of firms of this group. On the other hand, there are 2,730 privately owned firms which represent 98.5% of the total number of Engineering enterprises.

Table 12 depicts the classification of Private Sector

Engineering enterprises by employment size. A close examination of Table 12 indicates that there are 1,594 firms with 10 to 50 employees, 366 firms with 51 to 200 employees, and only 3 firms with more than 200 employees. These Engineering firms represent 97.9% and 0.2% of the total number of firms of this group of industries. Thus VSSE's i.e., firms which employ between 10 and 50 individuals comprise the largest number of firms of Engineering industries with 1594 enterprises. Once more, the importance of VSSE's in terms of the number of firms of this group of industries is demonstrated.

The Ministry of Industry does not differentiate in its statistics between the output of Engineering and Metallurgy firms. For the combined value of output fo privately owned Engineering and Metallurgy firms, VSSE's contribution is estimated at 85% or LE 268.8 million. This represents 14.1% of the gross value of output of both the Public and Private Sectors Engineering and Metallurgy companies.

Overall, VSSE's contribution to the number of firms and gross value of output of Engineering industries is substantial.

4. Printing and Paper Industries:

This group of industries is the fourth largest, in terms of the number of firms estimated at 1,183, or 8.9% of the total number of industrial firms. There are 19 Public Sector firms and 1164

Private Sector firms, representing 3.3% and 96.7% of the total for this group of industries, respectively.

Table 12 denotes that there are 1,106 Private Sector firms with 10 to 50 employees representing 95% of total number of private firms of this group of industries. Moreover, firms with 51 to 200 employees are estimated at 58 (or 5%) of the total. There are no privately owned firms engaged in Printing and Paper employing more than 200 workers.

Output of Printing and Paper industrial firms is usually included under the Chemicals subsector by the Ministry of Industry. No data was available at the writing of this study on the percentage output of Printing and Paper firms. Thus, the relative contribution of VSSE's could not be specifically derived. On the other hand, it is worth pointing out that VSSE's contribution to the gross value of the Chemicals Subsector, to which Printing and Paper firms belong to, was estimated at 35% of LE 89.9 million as shown in Table 12 . Moreover, VSSE's contribution represents 9.6% of the gross value of output of the Chemicals subsector. Overall, VSSE's contribution to the number of firms of this group of industries is substantial at (95%) although their relative contribution to the gross value of output of the Private Sector at 35%, is less significant.

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5. Foodstuffs Industries

Foodstuffs industries is the fifth largest group of industries with an estimated 887 firms. In terms of the number of firms, this group represents 6.7% of the overall number of industrial firms in Egypt. The number of Public Sector enterprises belonging to this group of industries is 38, representing 4.3% of the total for this group of industries. There are 849 privately owned Flodstuffs firms representing 95.7% of the overall number of Flodstuffs enterprises. Tables 11 and 12 classify Private Sector Foodstuffs firms by employment size. VSSE's, i.e. firms with 10 to 50 employees represent 81.3% of the overall privately owned Foodstuffs firms. There are 132 firms with 51 to 200 employees comprising 15.5% of the total. In addition, 27 firms (or 3.2%) employ more than 200 persons.

Ministry of Industry usually includes the output of Foodstuffs and Cereals in one subsector. Thus, in FY 83/84 the total value of industrial output of privately owned Foodstuffs and Cereals firms was LE 752.7 million. VSSE's contributed 60% (or LE 451.6 million) of total value of private sector's output for Foodstuffs and Cereal Industries. Furthermore, VSSE's (firms with 10 to 5(employees) contribute 17.4% of total output of Foodstuffs and Cereal enterprises.

In summary, VSSE's contribution in terms of the number of firms

or share of Private Sector's output for Foodstuffs industries is significant.

6. Chemicals Industries

The group of establishments belonging to Chemicals Industries is the sixth largest with 873 Public and Private firms. There are 44 Public and 829 Private sector enterprises. These firms represent 5% and 95% of the total number of Chemicals firms, respectively.

Tables 11 and 12 show the number and classification of Private Sector Chemicals firms by employment size. The 637 firms with 10 to 50 employees comprise 76.8% of total number of Private Sector Chemical firms. There are about 141 firms (or 17%) with 51 employees. In addition, there are an estimated 51 firms (or 6.2%) with more than 200 employees.

Ministry of Industry includes in its data on the Chemicals industries, the output of tanneries, footwear, pulp and paper and forestry, in addition to the traditional organic and inorganic Chemicals industries.

Table 12, depicts VSSE's contribution to the Chemicals industries as reported and defined by the Ministry of Industry which amounted to LE 89.9 million in FY 83/84. This represents an estimated 35% of Private Sector's output for Chemicals industries and 9.3% of the combined output of Private and Public Sectors Chemicals firms.

To sum-up, VSSE's contribution to the number of Private Sector firms and the value of output of the Chemical industries is quite important.

7. Building and Construction Industries

There are an estimated 536 Building and Construction firms. These firms represent 4% of the overall number of industrial firms. Public and Private Sector firms are estimated at 60 (or 11.2%) and 476 (or 88.8%), respectively.

Tables 11 and 12 show the number and percentage distribution of Private Sector firms by employment size. Examination of these tables indicate that VSSE's (firms with 10 to 50 employees) comprise 97.2%, with 463 enterprises. The number of firms with 51 to 200 employees is 8 (or 1.7%). Finally, there are only 5 firms (or 1.1%) with more than 200 employees.

Building and Construction firms are no longer under the Ministry of Industry's supervision. These firms are part of the Ministry of Housing and Reconstruction. It is estimated that VSSE's share of total Private Sector's building and construction output is around 45%

In summary, VSSE's contribution to the number of building and construction firms and to Private Sector's output of this group of industries is significant.

8. Woodworking Industries

The number of firms engaged in Woodworking industries is estimated at 402. There are 20 Public Sector firms (or 5%) and 382 Private Sector enterprises (or 95%) producing Woodworking products.

Tables 11 and 12 show the number and distribution of Private Sector firms by employment size. VSSE's, i.e., firms with 10 to 50 employees, constitute 72% of Woodworking industries with an estimated number of 275. These are 84 firms with 51 to 200 employees, and 23 firms with more than 200 employees, respectively. These firms represent 22% and 6% of the total number of Woodworking Private Sector enterprises, respectively

It is estimated that 35% of total woodworking output is produced by VSSE's. In FY 83/84 VSSE's woodworking output was valued at LE 148.9 million.

Overall, VSSE's contribution, to the number of woodworking enterprises and their total output is significant.

9. Cereals Industries

There are about 199 enterprises within the Cereals group of Industries. The 19 Public Sector Firms represent 9.5%, while the 180 private enterprises constitute 90.5% of the total. Tables 11 and 12 classify Private Sector's firms by employment size. The 154 enterprises with 10 to 50 employees represent only 30% of the total number of Cereals industries firms. On the other hand, the

remaining 126 Private Sector firms represent 70%. There are no firms belonging to Cereals industries with more than 200 employees.

The output of Cereals Industries is part of the Foodstuffs Subsector according to the data available from the Ministry of Industry. It has been estimated that 60% of output of Foodstuffs (including Cereals industries) is generated by VSSE's.

Once more, the important role played by VSSE's (firms with 10 to 50 workers), in terms of the number of firms and their contribution to Private Sector's industrial output, is demonstrated by Cereals Industries.

10. Petroleum and Mining Industries

There are about 67 industrial enterprises engaged in Petroleum and Mining activities representing 0.5% of the total number of industrial firms operating in Egypt. The 18 Public Sector firms represent 27% of the total for these industries. On the other hand, 49 Private Sector enterprises constitute 73% of the total.

Tables 11 and 12 show the classification of Private Sector Petroleum and Mining Industries firms by employment size. There are no firms 10-50 employees, i.e., no VSSE's. There are 45 enterprises with 10 to 200 workers and 4 firms with more than 200 workers. These two categories of firms represent 91.8% and 8.2% of the total number of private Petroleum and Mining firms, respectively.

Based on the above, it becomes evident that only within the Petroleum and Mining Industries that VSSE's do not play any role, whether in the number of firms or in industrial production.

II) Metallurgy Industries

The Metallurgy industries is the smallest category of industrial groups in terms of the number of firms with only 69 firms. Enterprises belonging to the Metallurgy industries represent only 0.5% of the total number of industrial firms in Egypt. There are 10 Public and 59 Private Sector Metallurgy firms representing 14.5% and 85.5% of the total number of firms for this group of industries. Tables 11 and 12 show the classification of privately owned firms belonging to Metallurgy industries by employment size. There are 58 firms (or 98.3%) with 10 to 50 workers, i.e., VSSE's. There is only one firm (or 1.7%) with 51 to 200 workers. There are no Metallurgy firms with more than 200 employees.

Ministry of Industry includes Metallurgy and Engineering industries in a single subsector. Thus, output statistics do not differentiate between these two group of industries. VSSE's contribution to the Private Sector's output of Metallurgy and Engineering industries is estimated at LE 268.8 million in FY 83/84. This represents 85% of the overall Private Sector's share for this subsector.

To sum-up, VSSE's contribution to the Metallurgy industries, in terms of the number of firms and the share of Private Sector's output is very significant.

In conclusion to this section and based on the above analysis of the eleven group of industries, it becomes quite evident that:

1st: The Private Sector plays a very important role in Egyptian industry in terms of the number of firms estimated at 13,000 vs 329 firms belonging to the Public Sector Private Sector enterprises constitute 97.5% of the total number of industrial

firms while publicly owned enterprises represent only 2.5%.

2nd: Enterprises which can be classified as VSSE's, i.e., firms with 10 to 50 employees are estimated at 11,774 establishments. VSSE's constitute about 90.6% of the overall number of Privately owned industrial firms in Egypt.

3rd: Private Sector's Share of total industrial output was estimated for FY 83/84 at LE 2,929.4 million which represents 34.3% of overall industrial output. This contribution of the private industrial sector is underestimated for the following reasons:

i. privately owned firms under-report their output, employment, investment,in order to avoid paying taxes;

ii. it does not include the output of the estimated 3,000 firms which are not members of the FEI.

iii. data from the Ministry of Industry does not include the output of the estimated 250 thousand artisans. The industrial output of artisinal firms is estimated at 15% of the total. Thus, when we add the output of the formal and organized private industrial sector to the informal sector engaged in industrial type activities, Private Sector's share of industrial output may exceed 45% of the total industrial production. This is another indication of the crucial role played by the Private Sector in the Egyptian economy despite all the constraints and regulations they are operating under.

4th: VSSE's share of Private Sector's industrial output in FY 83/84 was LE 1,799.4 million. Thus, representing 61.4% of total private sector's industrial output. Furthermore, VSSE's share of

industrial output represents 21% of total industrial productic
valued at LE 8,548.5 million in FY 83/84.

IV. Public Agencies Interacting with SSE's

A. Introduction

Small Scale enterprises operating in Egypt must deal with various public agencies. These dealings usually represent serious headaches for manager/owners of small firms. The red tape that a company has to put up with from the idea stage until it begins operations and throughout its existence is horrendous. It seems that laws and regulations which govern various business activities are regulatory in nature rather than promotional or contributional to growth. The so-called support that these public institutions are supposed to render to industrial firms is not always forthcoming or easy to obtain. When such support is rendered it usually involves a lot of time and delays that business people cannot really afford.

The following is a very brief listing of the various public agencies which industrial firms in general, and small scale ones in particular, have to deal with.

B. Federation of Chambers of Commerce

For a firm to obtain legal status and be able to operate in Egypt, it must register with the Federation of Chambers of Commerce and become a member. This membersnip must be renewed every year by paying the necessary fees and hence be continued throughout the life of the company. This Federation has the task of advising the GOE on laws and programs which can stimulate the business environment.

Periodically a bulletin is issued by this Federation containing statistics and other information which may be of interest to business in general.

C. Department of Commercial Registration

In order to be allowed to operate in Egypt, a business firm must obtain an official license to operate from the Department of Commercial Registration. Furthermore, every firm must carry its registration number on all its documents since this is a requirement by law. Moreover, this registration number must be displayed on companies'premises.

D. General Organization for Industrialization (GOFI)

GOFI is an agency of the Ministry of Industry which has the task of advising it on industrial planning matters as well as preparing industrial plans. Industrial projects formed under Law 159 of 1981 must obtain GOFI's approval before they are allowed to operate. Once a project is approved, it must register with GOFI. Even joint venture projects formed under Law 43 of 1974 must, in many cases, get some kind of concurrence from GOFI through the Investment Authority. Latest data and statistics on Egyptian industry should be available at and through GOFI. Studies are carried out to determine demand and project supply in order to determine market gaps and for the preparation of the national plans. Companies, new or existing, are refused to be granted approval going into some industrial activity because GOFI's studies have indicated that there is no market gap to be filled. Some people feel that GOFI has been an impediment to the growth of

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the industrial Private Sector by its refusal to grant approval to numerous projects instead of promoting and encouraging the growth of the industrial sector.

E. Department of Industrial Control (DIC)

Another agency of the Ministry of Industry which is responsible for the quality control of industrial products. Every private industrial firm must obtain the approval of DIC on the price and quality of its products. Sometimes, DIC's approval must be sought before raw materials, equipment or spare parts are imported.

F. The Local Councils

The local councils are the agencies of the central government which are responsible for granting approval for locating a factory within their jurisdiction and zone. Moreover, local councils must grant approval of building plans and issue a building permit before any construction may start. Moreover, industrial premises must be inspected after construction has been completed. When everything satisfies the local council's criteria, an "industrial permit" is issued, granting the factory permission to begin operations. Periodic safety checks must be also carried out.

G. Local Public Utilities Department

There are four local public utilities companies which an entrepreneur has to deal with: the potable water, the electric power, the telephone and sewage disposal departments. Once a building permit is obtained from the local councils, a businessman must visit each of those public utilities organizations in order to receive their services.

H. Federation of Egyptian Industries

This Federation is similar to the Federation of Chambers of Commerce, except that it deals only with industrial firms. Every industrial firm with 25 or more employees or 5,000 L.E. in fixed assets is required by law to become a member. Membership in this Federation must be requested only after the factory has been granted approval by local councils.

I Tax Department

All industrial firms are required by law to register with the tax department in their jurisdiction in order to obtain a tax register and to stamp their legal accounting ledgers before they can begin operations.

J. Social Insurance Authority

Industrial firms are required by law to register with the local bureau of the Social Insurance Agency at the start of operations. Workers must also be registered with this agency.

Employers must pay social security taxes for each employee. This has led employers to underestimate the number of their employees by only registering some of them in order to avoid paying the full amount of social security taxes they owe.

All the above agencies are those that SSE's must deal with in order to be able to begin operations. Throughout its life every industrial firm will have to deal with one or more of the following agencies of the bureaucratic apparatus:

- Agencies of the Ministry of Supply
- Agencies of the Local Government

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- Agencies of the Ministry of Health (if the enterprise manufactures pharmaceuticals)
- Agencies of the Ministry of Agriculture (if the enterprise is a food industry)
- The Unified Standards of the Ministry of Industry
- The Department of Industrial Control of the Ministry of Industry
- Government and Financial Institutions
- The Chamber of Commerce
- The Federation of Egyptian Industries
- Customs Authority (if the enterprise is involved with imports)
- The Export Development Authority (if the enterprise is involved with exports)

From the above, one can obtain a fair notion about the bureaucratic apparatus that small scale industrial firms have to deal with before they are granted permission for beginning their operations or throughout the life of the company. This demonstrates that laws and regulations and the institutions which oversee that they are abided by are regulatory by nature and do not support nor promote the growth and welfare of industrial firms.

V. Use of Credit by SSE's

Overview

Egyptian banks have been generally reluctant to respond to the credit needs of small scale firms. Banks operating in Egypt are usually characterized by being very conservative in their lending practices. Banks collateral requirements usually range from 200% to 300% of the size of the loan being negotiated. Assets which are used as collateral by banks, in order of importance, are land and buildings, equipment, bills of exchange and raw materials inventory (placed under the custody of the bank). The extreme risk aversion by commercial banks and their heavy reliance on collateral requirements for granting loans to SSE's may be due to the fact that these firms do not keep adequate financial records. Thus, their credit worthiness cannot be determined through the analysis of the firm's income statement, cash flows and balance sheet. In terms of the use of credit by SSE's, it is possible to differentiate between working capital financing and fixed assets financing.

A. Working Capital Financing

Working capital financing represents a major and acute problem for SSE's. The lack of liquidity experienced by small scale factories is a constraint which prevents a large number of SSE's from operating at full capacity. Hence, the shortage of cash for financing the purchase of raw materials, intermediate goods and payments for other operating cost items, hinder SSE's productivity and growth. This shortage of liquidity which affects the majority of SSE's arises from the fact that the procurement of raw materials and intermediate

products which are essential for the production process are strictly on a cash basis. On the other hand, the majority of sales by SSE's, for competitive reasons, are on a 20 to 45 days credit basis. This practice always creates cash liquidity problems for SSE's. This cash flow problem is being aggravated by the fact that banks do not make it a practice to grant SSE's loans for financing their working capital needs.

It must be emphasized that the largest firms belonging to this sector of the economy have been more successful than the smaller ones in obtaining the credit they need. On the other hand, smaller firms, in the 10-50 employment bracket, have been usually unsuccessful in obtaining the needed credit. The DIB has granted quite a few working capital loans, with maturity of one year or less, in the past few years. Public Sector banks have also granted working capital loans, although they have been reluctant to provide data (when requested) on the number and value of these loans. Needless to say, that SSE's do not have enough adequate sources of credit for financing their working capital needs.

B. Fixed Asset Financing

New and existing enterprises seek credit to finance the importation of machinery. The DIB has provided a large number of loans to SSE's to finance their imports of machinery. This has been possible through the various foreign credit programs which have been available at DIB and geared for the Private Sector. It is safe to say that the largest percentage of these foreign currency loans have been granted

to large SSE's because they have the necessary collateral and do keep reasonably good financial records. In addition, these large SSE's have probably established a good track record with the banking industry. Thus, their credit worthiness have been well demonstrated. Hence, they do not represent a high risk, when compared to VSSE's i.e., firms with 10-50 employees.

The smaller firms in this sector try to raise the needed funds through sources other than banks, i.e., either through relatives or friends, or by taking one or more additional partners. One factor which works against the smaller or newly established SSE's is the fact that the majority of these companies do not own the land or the buildings where their factories are located. It has been generally observed that for those firms that seek credit from banks for expanding existing capacity or for new ventures, that loans are granted not because of the economic and financial feasibility of the project, but only for the soundness of the security and value of the clients collateral. This practice by banks has restricted expansion and growth of SSE's, and hence have had a negative impact on incomes and employment for the economy in general, and the Private Sector in particular.

It is worth pointing out that some SSE's do seek bank loans from commercial banks because of their reluctance to pay interest which is considered usury, and hence forbidden under the teachings of Islam. For this group, Islamic banks with their concept of partnership, or Musharaka, are an attractive source of credit. For those SSE's which

have sought bank credit, some of the concerns usually expressed are: high interest rates, stiff collateral requirements, complicated procedures, extensive information requested by banks about the firm, very short grace period, and the short term of the loan.

Note that any project design effort for alleviating the credit needs of SSE's must take into consideration SSE's characteristics and constraints in terms of their use of credit. Hence, identified problem areas must be tackled through the proper credit mechanism. The benefits which may accrue to this important sector in terms of productivity, income and employment should be fruitful to the economy as a whole.

D. Overall View of Loans Granted to the Private Sector

A recent World Bank report stated that loans and advances offered by the banking sector increased from LE 2.5 billion at the end of 1978 to LE 13.4 billion as of 6/30/84. This represents an average real rate of increase about 25% per annum. Private business has become the single largest beneficiary of bank credit receiving LE 6.5 billion or 48.5% of total loans and advances as of June 30, 1983. About one third of loans granted to the Private Sector were in Foreign Exchange. Total loans and advances to the Private Sector can be broken down to the various sectors of the economy as follows:

a. 33.4% for trade purposes;

b. 27.9% for industrial purposes;

c. 18.1% for services;

d. 5.9% for agriculture;

e. 14.7% for others.

It is worth stating that because only 20% of the deposit base of the banking sector has been generally for more than one year, term lending has comprised only about 13% - 15% of total loans to the Private Sector. Term lending has also been affected by the relatively conservative approach of the banking sector in Egypt and its reluctance to commit funds for long periods of time i.e., for more than one year. To lengthen the maturity of deposits, a better structured interest rate favoring interest rates on medium and long term loans, in addition to a less traditional approach of the banking sector, would be required. The introduction of ten year government "investment" certificates and other similar commercial bank savings certificates is a move in the right direction. It also fulfills the apparent need of the Egyptian Private Sector for term lending.

E. Financing the Industrial Sector

From FY 1977/78 To FY 1981/82 the total capital investment in the industrial sector amounted to LE 18.2 billion. The Private Sector's share of total capital investment was LE 3.5 billion. Bank loans and advances to the private industrial sector increased from LE 269.8 million in 1978 to LE 1,161.1 million in 1981. This increase represents an annual growth of 37% per year in real terms. During the same period, term loans (more than one year) increased by 40% annually: from LE 49.9 million to LE 202.1 million. Part of those loans were made in foreign currency: LE 24.1 million in 1978 and LE 69 million in 1981, respectively. Term lending to the private industrial sector, in this

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period, amounted to 17.4% of total loans to this sector. Commercial banks have adopted a highly conservative lending policy. Loans are generally granted to well known customers with excellent credit standing with high and rigid collaterial requirements.

Egyptian banks often lack the capability and desire to take risks on the basis of sound and objective analysis of project's financial and economic feasibility. Thus, the commercial banking sector does not seem to fullfill the needs of the private industrial sector for term lending. The only two banks which were willing to grant medium to long term loans to the private industrial sector are DIB and MIDB. These loans required very sound appraisal of projects viability by DIB's and MIDB's officials. Moreover, DIB has emerged as the main institution for providing foreign currency loans to the private industrial sector. DIB's total term lending during the current Five Year Plan (1982/1983 - 86/87) would be about 25% of the total investment in the private industrial sector.

Commercial and joint venture banks have not been very willing to grant loans to SSE's nor to Artisans because of their feelings that these loans are very risky and costly. Banks procedures, collateral requirements and details requested on loan applications have been cumbersome and sometimes unjustified with respect to the size of the loan. On the other hand, SSE's managers have been skeptical and many of them are reluctant to comply with bank's complicated and demanding requirements. This situtation has left SSE's and Artisans with inadequate and unresponsive sources of credit. DIB and Nasser Social

Bank are the only two banks which have been responsive to the credit needs of SSE's and Artisans. In 1978, 25% of DIB's term lending was granted to SSE's. The percentage of DIB's term lending to SSE's rose to 30% in 1982/83 and is expected to reach 50% in 1986. On the other hand, the Nasser Social Bank which is a non-interest charging bank, usually demands a share of profits of industrial ventures (about 12% of total investment). However, loans for productive purposes comprise only a small portion of its loan portfolio, 5% in 1980/81 and less than 1% in 1981/82. However, Nasser's loan activities are quite less significant, since it only represents 1% of DIB's loan portfolio.

Based on the above, one can safely state that the GOE, working closely with the banking sector and USAID, should encourage the development of a large medium term deposit base through the appropriate credit instruments and programs. This will alleviate part of the problem faced by the private industrial sector for term lending. On the other hand, SSE's definitely need the appropriate credit support program in order to meet their demand for short and long term credit.

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VI SSE's Constraints and Problems

A. Introduction

In this section, an examination of the constraints whwich have hindered SSE's growth and productivity is undertaken. Moreover, the regulatory problems that SSE's have to confront in their daily operations are highlited.

B. Production Constraints

A large percentage of SSE's suffer from the inadequacy of a highly depreciated production equipment. Moreover, a large number of firms use very out-dated and primitive productiion processes. This has caused the majority of firms to operate below capacity.

Production equipment problems can be attributed to machine breakdown due to its old age, inavailability of spare parts and the power blackouts and brownouts.

Firms usually suffer from the lack of information on new technologies and seem to be eager to identify sources of information on new technologies which may improve their production processes.

The shortage of skilled and highly trained servicemen and repairemen have aggravated the problems associated with the production processes used by SSE's. It has also added to the length of time a machine remains idle and hence has a negative impact on firms' productivity.

The majority of SSE's suffer from unavailability of raw materials and intermediate goods in the required quantities and/or qualities. Moreover, it seems quite apparent that small scale

industrial firms which began operations after the Open Door Policy of 1974 was adopted, rely very heavily on the imports of intermediate products. Cases in point (to name but a few) are:

1. The Chipsy Company for production of potato chips;
2. The Cripsy Company for the production of potato chips.
3. The NOVA washing machine factory;
4. The El Karnak washing machine factory.

Another problem which continues to affect the productivity and growth of SSE's is the O.K. shortage of skilled workers due to their migration to other Arab Copuntries.

What may be very puzzling is that managers/owners of SSE's perceive the lack of unskilled workers as one of the constraints that have plagued their firms productivity. One may attribute this perception to the reluctance of a large percentage of would-be workers to subject themselves to the hard work and discipline that working in a factory entails.

C. Labor Constraints

The apparent unavailability of skilled and unskilled workers is one of the most accute constraints faced by SSE's. It seems that Egyptian unskilled labor do not want to subject themselves to the discipline that working in a factory entails. On a visit to a candy and Halawa factory in Quena, it was observed that a large number of men were sitting and chatting in a public square. Meanwhile, the owner of a factory complained that he cannot find unskilled labor. When told about the healthy men sitting in the public square, the owner mentioned that they have fathers, brothers

or sons working in other Arab countries who send them money and hence have almost stopped completely from seeking employment. This raises the important labor issue in Egypt which needs to be addressed and solutions to this complex problem should be sought. USAID/Cairo may take the initiative in such a study which may prove crucial at this stage of Egyptian development. On the other hand, recruiting foremen does not seem to be a problem faced by SSE's. Some of the factors which have ill affected labor productivity are worker turnover and absenteeism. Labors tend to be absent without permissions or get a job in a competing factory without giving advance notice. Workers tend to take days-off after pay-days without advising managements of their plans. Managers tend to close their eyes on such behavior because of their inability to find replacement.

D. Marketing Constraints

The majority of Egyptian SSE's do not perceive that they have any problems marketing their products in a country characterized by shortages of products for end users. On the other hand, SSE's suffer from the flood of competing imports which are usually favored by Egyptian consumers. Despite the fact that Egyptian manufactured goods may be cheaper, and in many cases, the quality difference may be hard to detect. Price controls and unlicensed companies have also caused SSE's to experience unfair competition.

E. Financing and Credit Constraints

With the exception of DIB, most banks do not like to deal with SSE's for the previously stated reasons. When approached by SSE's

banks usually request collateral which vary between 20% to more than 300% of the value of the loan. Moreover, loans are usually offered for short terms: the largest percentage for one year maturity, while a small percentage of loans have a three year maturity. Despite the borrowers' requests for longer periods of time for loan repayments. Furthermore, the complexity of loan application procedures and the vast amount of information about the borrower and his enterprise have also been another deterrent for the used of bank credit. A large number of SSE's raise the required funds through family and friends. For the past four years the majority of SSE's which have been fortunate in obtaining loans from financial institutions, have used this credit for financing the purchase of machinery. While a small percentage used this credit for fulfilling working capital requirements. SSE's in general, feel that current interest rates are too high and would constitute a heavy burden (on their firms) which they are not willing to bear. Others cannot accept the concept of interest rates which are considered as "usuary", hence are permissible under Islamic teachings. These firms favor dealing with Faisal Islamic Bank or the International Islamic Bank for Investment and Development. These two banks do not charge interest and follow the concepts of participation in profits or losses, i.e., "Musharaka".

Despite all the above, and based on the findings of previous studies one cannot help but realize the tremendous need and desire of SSE's for sources of funds for financing medium term equipment procurement and working capital requirements, as well as long term

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project financing.

F. Miscellaneous Constraints

The following constraints handicap the productivity, growth and general performance of SSE's but are less accute in nature than the ones outlined above.

a. Management Constraints

Managers-owners of small scale industrial firms do not perceive that they face any problems with respect to the adequacy of their skills for dealing with bookkeeping, accounting, production techniques, production planning, sales and distribution or purchase of raw materials. Despite this perception, it seems quite apparent that more than 50% of SSE's managers/owners need the proper training in the areas stated above.

b. Expansion Constraints

Small scale industrial firms which wish to expand their existing productive capacity are usually, constrained by the lack of sources of credit which would participate in financing this expansion. Thhe following factors have affected SSE's plans for expanding their existing capacity:
shortage of well located sites and/or space at a reasonable cost, the need for new machinery to replace the old and outdated ones and the shortage of skilled and unskilled workers. On the other hand, firms which have plans for increasing their rates of production within their existing capacity perceivethat the unavailability of workers (skilled

or unskilled) and the short supply of raw materials and intermediate goods are some of the major constraints they have to overcome. Furthermore, the lack of responsive sources of credit for financing short term working capital needs is another major constraint handicapping the productivity and operations SSE's at their full capacity.

G. Regulatory Problems

Government laws and regulations seem to be designed for controlling economic activities in general, and the Private Sector in particular. Hence, some regulations and laws constitute on obstacle to the growth and development of SSE's which are part of the Private Sector.

The following constitute some of the areas which have affected the economic activities and growth of SSE's:

i. The establishment of the "Imports Rationalization Committee" had led to a slowdown of the processing of imports applications which are usually perceived to be complicated and tedious.

ii. The ever continuous changes in imports laws and regulations have let to confusion and instability in decisions concerning procurement of imported raw materials and intermediate goods

iii. Labor laws are considered by most managers/owners of SSE's completely in favor of workers and against the interests of the enterprises.

iv. Social Security payments payments by firms for their workers are considered quite high by owners who would welcome equal

sharing of this burden by their employees.

v. A continuous concern by most SSE's is the arbitrary process of determining taxes owed by firms. This has discouraged many entrepreneurs from going into industrial type activities and preferring trade.

In conclusion, it is worth pointing out that some of the major constraints hindering the planned growth of SSE's within their existing productive capacities are the lack of required workers and raw materials in the needed quantitites and qualities. For firms which would like to expand their productive capacities, the major hinderance to their plans are usually lack of needed space and the required funds for new machinery, and their inability to locate the skilled an unskilled workers they need.

VII. USAID Program Options for Assisting SSE'S

A. Proposed Working Capital Credit Program:

a. Introduction

One of the major problems hindering the growth and productivity of SSE's in Egypt is the lack of liquidity for financing working capital. SSE's usually purchase raw materials and other intermediate goods on a cash basis. On the other hand, for competitive reasons most sales are done on a 20 to 30 days credit basis, (sometimes even up to 45 days credit basis if competition is strong in that particular industry). This situation has forced a large number of SSE's to operate at around 50% below capacity. Egyptian banks have been reluctant to finance working capital needs of SSE's for the reasons previously outlined previously in Chapter V of this study.

b. Purpose

The purpose of the proposed Working Capital credit program is to assist SSE's in dealing with their severe liquidity problems. Currently, SSE's do not have a recognized and continuous source of credit which may assist them by financing their working capital needs.

This proposed working capital credit program will enable SSE's (its beneficiaries) to be able to operate close to full capacity. This implies an increase of approximately 50% in the industrial output of the beneficiaries of this program. The positive impact on the Private industrial Sector, in particular, and the Egyptian economy in general will be quite substantial. Industrial employment will increase since

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with funds abailable to purchase the necessary raw materials and intermediate goods, there is a need to hire more labor to operate the machinery and equipment which will be no longer idle. As employment and output are increased, total income in the economy as a whole should also increase.

Egyptian consumers will also benefit, on one hand, from the increased supply of commodities which may be currently in short supply. On the other hand, consumers will also gain from the overall improvement in the economy in terms of the increase in income and employment.

c. Project Description

USAID would provide the equivalent of $20 million to be divided equally between five banks.(1) Thus, each bank would obtain about $4 million to be used for financing the working capital credit needs of SSE's. (200). A smaller funding size than a $4 million per bank than a $4 million may not be attractive for program participation. Especially, when the proposed credit program is designed for a clientele which banks have been generally reluctant to serve. Based on data obtained from DIB on their short term loans for Artisans, Very Small Scale Enterprises (VSSE's) and Small Scale Enterprises (SSE's), the average working capital loan for the proposed US-AID credit program was estimated at LE 40,000. This would imply about 100 working capital loans per bank, or 500 W.K. loans among the five participating banks.

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(1) Although with the same funding size, i.e., $20 million, four banks can be selected for this credit program. Hence, each bank would acquire $5 million for on lending. It is believed that it is better to increase the number of banks in order not to exhaust the absorptive capacity of each one.

These W.K. loans will enable SSE's to deal with their liquidity problems and enable them to purchase the required raw materials, intermediate goods, spare parts and other operating cost items which are usually part of working capital. Furthermore, SSE's who shall benefit from the proposed credit program should hopefully be able to operate at full capacity.

d. Beneficiaries

Based on discussions with V SSE's managers/owners (firms with 10 to 50 employees) and several banks officials, it became quite evident that the smaller firms which comprise the SSE's sector are the ones which suffer, more than larger ones, in terms of the lack of sources of credit which respond to their demand for loans. Thus, it may be recommended that these firms become the primary beneficiaries of the proposed credit programs. On the other hand, to ensure that the largest number of SSE's benefit from the proposed credit programs, a higher upper bracket (employment wise) may be adopted. The following options for the beneficiaries of US-AID Credit Programs are suggested.

1. Option "A": VSSE's

Option "A" stipulates that the beneficiaries of the proposed credit programs are officially registered firms with 10 to 50 employees on condition that the value of their fixed assets (excluding land and buildings) does not exceed LE 300 thousand (1).

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(1) DIB currently defines VSSE's as those firms with fixed assets not exceeding LE 250 thousand, excluding land and buildings. This definition is adjusted every year by using a certain CAPMAS price index. Thus, it is expected that within a year DIB's definition would specify the value stated above.

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This option would ensure that very small scale firms be the major and only beneficiaries of the proposed credit programs. The justification for this option would be that larger SSE's have been relatively successful in obtaining banks'credit. On the other hand, the majority of Egyptian banks have failed to positively respond to the demand for credit by VSSE's.

The reason for using DIB's definition of VSSE's, as well as, the employment size of the firm, is two-fold:

i. DIB is the only Egyptian financial institution which has adopted specific definitions for this sector of the economy;

ii. DIB must be the first bank to participate due to the fact that since it began operations in 1970, it has granted more loans to artisans, VSSE's and SSE's than any other Egyptian Bank;

iii. DIB has cooperated fully with the Mission's professional staff in every information we have sought;

iv. DIB has the best statistical department and their records are well kept and very well organized. This is evidenced by the fact that information requested from various departments were provided in record time;

v. The specification of an employment size for firms which should benefit from this credit program is compatible with World Bank's definition of SSE's being establishments with 10 to 50 employees.

2. Option "B": SSE's

Option "B" stipulates that the beneficiaries of the proposed Credit Programs are officially registered industrial firms with 10 to 200 employees, on condition that the value of their fixed assets (excluding land and buildings) does not exceed LE 550 thousand (1). This option makes use of a broader definition of SSE's. It allows the whole spectrum of SSE's operating in Egypt to benefit from the proposed credit programs. Thus, VSSE's, average SSE's and larger SSE's would benefit from the proposed credit programs. This option has its advantages and disadvantages. The obvious advantage is that it allows equal access to credit to all SSE's. On the other hand, in some sense, it makes the proposed program biased against VSSE's, i.,e., firms with 10 to 50 employees and possessing fixed assets (excluding and buildings) worth not more than LE 300 thousand. The reason being that LSSE's have had some degree of success in obtaining bank credit while VSSE's and ASSE's have been less successful in obtaining bank loans. Moreover, LSSE's are more sophisticated in terms of their financial record keeping and may have established some track records with banks. Thus, it is expected that LSSE's would be the primary beneficiaries of the proposed credit programs if "Option B" is adopted. Note that VSSE's are those firms which are in

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(1) Option "B" takes into consideration DIB's definition of SSE's when this credit program is expected to be operative.

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terrible need for a source of financing for their working capital requirements. It may be suggested, as a first Stage, to adopt Option "A" for the beneficiaries of the proposed credit programs to ensure that it reaches smaller SSE's industrial firms which are in need, more than larger ones, for this type of financing which is expected to enable them to operate at full capacity.

3. Modified Option A

In order to make the two proposed credit programs accessible to the largest number of firms, the lower limit specifying at least 10 employees per firm may be dropped. Thus, the "Modified Option A" would specify the following criteria for programs beneficiaries: officially registered firms with not more than 50 employees and the value of their fixed assets not exceeding L.E.300 thousand (excluding land and buildings). This option would accommodate artisinal firms, i.e., firms with less than 10 employees. It is worth pointing out that the average DIB loan to artisans in FY 84 was for L.E. 18,416. Moreover, the smallest loan to end-users from the Production Credit Program was for L.E. 12,000. This loan was used by a factory to import spare parts. Loans to micro-scale enterprises (artisans) can be expected to vary from LE 500 to LE 30,000, based on information obtained from DIB.

Although, "Modified Option A" is suggested, it must be emphasized that it will be more difficult to convince banks to participate in a credit program which would serve the credit needs of micro-SE's. Past history has demonstrated that Egyptian banks are reluctant to respond to entice banks to extend credit to firms smaller than the ones they have been reluctant to serve.

4. Modified Option B

Similarly, "Modified Option B" would not require that firms benefitting from the two proposed credit programs employ at least 10 workers. The purpose of modifying "Option B" is to allow micro-SE's to benefit from the proposed credit programs. Some artisinals firms may have approached the same level of technical know-how which characterizes VSSE's. Thus, it may be reasonable to include them in the proposed credit programs. On the other hand, micro-SE's may be able to expand their scale of operations and achieve a higher degree of sophistication in their production processes with the appropriate credit programs.

5. Generalized Option A

This option is similar to "Modified Option A". The only difference is that "Generalized Option A" eliminates any specification of the firm size in terms of the number of its employees. The justification for this option may be stated that participating banks may not be able to effectively enforce the employment size of the firm. It is worth pointing out that Private Sector establishments usually under-report the number of their workers in order to avoid paying social security and income taxes. Thus, the actual number of employees per privately owned firms may be very difficult to determine since their records usually do not show it.

6. Generalized Option B

This option would specify the beneficiaries of the proposed credit programs as follows: any officially registered firm employing not more than 200 workers and owning fixed assets valued at L.E. 550 thousand or less, excluding land and buildings.

The justification for "Generalized Option B" would be the following:

1st: the widest eligibility possible for officially registered firms in Egypt.

2nd: enabling micro-SE's to be eligible for receiving credit from the proposed programs by eliminating the lower limit stipulation for employment in each establishment.

7. Option C

"Option C" would specify that beneficiaries of the two proposed credit programs have the following characteristic:

Any officially registered Private Sector firm with fixed assets not exceeding L.E. 550 thousand, excluding land and buildings. The justification for "Option C" would be based on the following:

1st: increasing the number of Private Sector firms which may be eligible for receiving credit funds from the proposed credit programs.

2nd: eliminating completely any employment size for eligible firms which may prove difficult to enforce by participating banks.

3rd: making use of DIB's existing definition of SSE's with a slight modification. The purpose of the modification would be to allow artisans (micro-SE's), as well as, VSSE's to be incorporated under an eligibility umbrella loosely called SSE's.

8. Comments on the Beneficiaries Options

Seven Options specifying the beneficiaries for the two proposed credit programs were suggested. Moreover, the justification for each option was outlined. The question which needs to be addressed is the following:

Which "Beneficiaries Option" should US-AID adopt for the two proposed SSE's credit programs.

The answer to this question depends on the Mission's SSE's strategy, as well as, the Mission's specific objectives for SSE's credit programs.

e. Principal Terms of the Working Capital Credit Program

1. Procurement

Each participating bank is allocated about $4 million for on-lending to small scale firms as specified under "Beneficiaries of the Proposed Credit Program.

Participating banks grant loans in local currency (LE) for off-the-shelve procurement of raw materials, intermediate goods and spare parts. In addition to financing other items which are part of working capital.

2. Interest Rate

The interest rate charged by participating banks on the proposed working capital credit program should be the market rates of interest for industry, currently as specified by the Central Bank of Egypt at the time program becomes operative.

In order to assist SSE's in achieving their productivity and growth objectives, it is suggested that participating banks do not collect from them additional service charges on the extended credit. Banks will be compensated for these charges from one of the options set up to offset the administrative costs of processing and managing small size loans. The proposed options will also be designed as part of the overall USAID strategy to encourage banks to participate in the proposed SSE's credit programs.(1)

3. Exchange Rate To Participating Banks

Currently, funds disbursed through the Production Credit Program are available at $1 U.S. equivalent to 1 L.E. This exchange rate is below the current official exchange rate, i.e., 1 U.S. $ = 1.34 L.E. It is suggested that the Production Credit exchange rate, which is lower than the official rate, be also available to participating banks. It is further suggested that the exchange rate be determined at the time the loan agreement is signed between participating banks and, or CBE/GOE.

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(1) More on the various options which should be established to encourage banks to participate in the proposed credit programs for SSE's will be outlined below in the Section on "USAID Options to entice banks participation in the SSE's credit Programs".

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The stipulation of making program's exchange rates lower than official exchange rates should be another incentive built into the program to entice banks to participate. Furthermore, the fact that participating banks obtain U.S. Dollars and then grant loans in LE is a very attractive option since it will increase their deposits base (and CBE's deposit base) in FX which is always much smaller than the one in L.C. Furthermore, based on information obtained from several private sector entrepreneurs, it has become quite evident that it would be totally unacceptable to them that the exchange rate is determined at the time of loan repayment. No businessman will be willing to take the risk for any fluctuations in the exchange rate.

4. Currency of Repayment by SSE's

SSE's are granted loans in local currency for financing their working capital. Repayment of loans is also undertaken in LE.

5. Period of Repayment by SSE's

The proposed SSE's "Working Capital Credit Program" is designed to fill a tremendous need for working capital financing which is short term by its nature. Thus, the period of repayment for this credit program should not exceed one year.

6. Down Payment

No down payment should be specified in the working capital credit program. The justification for this stipulation is the fact that this credit program is proposed to alleviate the liquidity problems that SSE's are experiencing.

7. Collateral Requirements

Beneficiaries of the proposed working capital credit program should not have to pledge assets or personal collateral whose value exceeds the loan size in order to obtain a working capital loan. Keeping in mind that a large percentage of SSE's do not own either the land and/or the buildings where their factories are located. These two real assets are the most important collateral used by Egyptian banks to determine the credit worthiness of their customers. This fact would automatically exclude SSE's from the credit worthiness status. Hence, prevent them from obtaining the bank credit they desparately need.

It is suggested that participating banks receive a guarantee from a special "Guarantee Fund" to reduce the stiff required collateral which are pledged by borrowers which sometimes reach 300% of loan sizes.(1)

It is worth pointing out that if it is left to participating banks to determine the security, collateral requirements and service charges, the proposed credit program will never get off the ground. The reason being that Egyptian banks have been extremely conservative in their lending practices requesting collateral which may reach 2 to 3 times the amount of the requested loan. Past history indicates that the majority of SSE's have been unsuccessful in providing banks with the required guarantees and collateral. Thus, SSE's were unable to obtain the needed bank credit.

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(1) More details on this "Guarantee Fund" will be outlined below.

These arguments do not exclude the notion that banks prefer to grant large loans than small ones because the former are more beneficial and less risky from banks' point of view. These large loans are usually requested by a clientele which can provide a bank with the required collateral and have usually established a good credit track record with the banking industry.

Based on all the above, it is suggested that beneficiaries of the "Working Capital Credit Program" do not have to pledge collateral in excess of loan size prior to loan approval.

8. Funding Limits

It is suggested that loans from the proposed "Working Capital Credit Program" should not exceed LE 70 thousand. On average, loan values are expected to be around LE 40 thousand.

It is worth pointing out that the smallest loan granted to end-users through the Production Credit Program was for LE 12 thousand. Furthermore, DIB's short term loans to SSE's in 1984 averaged about LE 50 thousand. Thus, the LE 70 thousand upper limit more than makes up for an inflation rate which was estimated by international organizations at around 17% for FY 83/84.

9. Criteria For Banks Selection

The selection of banks for participating in the proposed "Working Capital Credit Program" should be based on the following criteria:

i) A lending history showing willingness to respond to the credit needs of SSE's.

ii) The charter of the bank should allow it to conduct business in local and foreign currencies.

iii) The bank should have demonstrated its adoption of developmental objectives by its lending practices. Thus, Public and Private Sectors development banks should be primary candidates. In addition, Private or Public sector banks may also be considered if they fit this criterion.

iv) The selected bank should have several branches in areas other than Greater Cairo and Alexandria to ensure maximum reach to SSE's located elswhere. SSE's located in areas other than the two above metropolitan areas may have been deprived almost completely from bank credit.

v) It should be considered as an advantage for bank's selection, past history of participating in previous AID credit program and demonstration of good performance. This may imply quick disbursements, rapid processing of loan applications and fewer complaints to AID's representatives about the bank.

vi) The selected bank should be willing to commit the necessary personnel, time and effort to the proposed credit program. In addition, the bank should have the capacity and ability to process the 100 working capital loans through the proposed credit program.

vii) The selected bank sould be willing to commit time and its own funds for promoting, marketing and administering the proposed credit program.

It is worth pointing out, that banks selection should not require fulfillment of each and every criterion from the seven stated above. The five selected banks for the proposed credit program should fulfill as many criterion as possible.

10. Proposed Banks For Participating in the Working Capital Credit Program

The following is a list of banks which should be seriously considered for participating in the proposed working capital credit program:

i) The Development Industrial Bank (DIB)

ii) The National Bank for Development (NBD)

iii) Misr Iran Development Bank (MIDB)

iv) Arab Investment Bank (AIB)

v) Banque du Caire (BDC)

vi) National Bank of Egypt (NBE)

vii) Bank of Alexandria (BA)

viii) Bank Misr (BM)

ix) The Principal Bank for Agriculture Development and Credit

x) The Credit Foncier

The DIB should be at the top of the list of participating banks because its past lending history has demonstrated its willingness to extend credit to small firms, i.e., artisans, VSSE's and SSE's. It may be even stated that since the establishment of DIB it has granted more loans to SSE's than any other Egyptian financial institution. Furthermore, DIB has always been very cooperative with USAID's representatives by providing them with necessary statistics which make the job of designing credit programs much easier. Finally, DIB has one of the best record keeping systems in Egypt. This has been demonstrated several times by providing the requested information either immediately or within one single day. In addition, DIB fulfills the majority of the outlined criteria.

The National Bank For Development should be another prime candidate for program participation. The major advantages that this bank may bring to the proposed credit program are:

First, it has a network of 17 Governorate banks located all over Egypt. This will ensure maximum reach to SSE's located in areas other than Greater Cairo and Alexandria. Furthermore, NBD is a development bank, thus its lending practices should reflect its developmental nature. Furthermore, since NBD began operations, it has demonstrated its complete willingness to assist SSE's with their credit needs. Finally, the NBD fulfills most of the criteria outlined above.

The four mentioned Public Sector banks have demonstrated their willingness to respond to some SSE's credit needs. This has been demonstrated by previous surveys and by conversations with banks high ranking officials. Furthermore the 4 Public Sector banks have branches located in areas other the two major urban centers. Moreover, the 4 Public Sector banks fit most of the criteria for bank selection outlined above. Three other banks are cited for possible participation, if five banks cannot be selected from the previous six, and agree to participate in the proposed SSE's credit program. These three development banks are AIB, MIDB and the PBACD. These three banks would fulfill some of the criteria for bank selection outlined above.

The Credit Foncier has made small loans to micro-SE's. Thus, it has demonstrated an understanding of the credit needs of SSE's. Hence, it is suggested that it participates in the proposed credit programs.

It is believed there should be at least five banks from the above-cited ten banks which will agree to participate in the proposed credit programs designed for SSE's. On the other hand, in the unlikely event that five banks cannot agree to participate, the options are as follows:

1st: either reduce the number of banks while increasing the funding size per bank;

2nd: approach other banks for program participation.

It is worth pointing out that any credit program designed for SSE's should include some very attractive features in order to encourage banks participation.

B. MEDIUM TERM CREDIT PROGRAM

a. Introduction

The credit needs of SSE's can be classified into two major categories:

1) Short Term Working Capital Financing

2) Medium Term Financing of Machinery and Equipment.

The outline of the proposed SSE's "Working Capital Credit Program" were presented in the previous section. In this section, an outline of the proposed "Medium Term Credit Program" will be discussed. The need for a Medium Term Credit Program specifically designed for SSE's has been demonstrated in the previous studies. In addition, various interviews with SSE's managers/owners, and bankers have also supported this particular need for the proposed medium term credit program.

Furthermore, a large number of SSE's are operating with old and oudated machinery which break down quite often. This situation has affected the productivity of SSE's, as well as, the quality of their products. Thus, the proposed Medium Term Credit Program will enable SSE's (its beneficiaries) to replace their outdated and worn out machinery. Thus, assisting SSE's to increase their productivity and improve their products quality. Moreover, it should also provide the necessary funds to those SSE's who would like to increase their productive capacity with the procurement of new additional machinery and equipment.

b. Purpose

The purpose of the proposed Medium Term Credit Program is to provide SSE's with the necessary funds for the procurement of equipment and machinery, as well as, intermediate goods which cost more than the upper limit of loans under the proposed Working Capital Credit Program. This Medium Credit Program is designed specifically for end users (i.e., SSE's). It is not meant for the use of Traders.

One of the major constraints which have prevented a large number of SSE's from operating at full capacity is the length of time of machine breakdown. The majority of SSE's are operating with old, worn out, but functional equipment. A large number of machines are idle either because they can no longer be repaired due to their old age, or because spare parts cannot be purchased due to the lack of personal funds. This problem is further aggravated by the fact that the majority of SSE's who seek bank credit do not have the necessary collateral (often valued at more than twice the value of the loan). Thus, their loan requests are quite often turned down. These combined problems have forced a large percentage of SSE's to operate approximately at 50% below capacity.

Furthermore, the lack of a recognized, stable and continuous source of medium term financing have prevented other SSE's from expanding their productive capacity by the acquisition of additional space and equipment. It has also left SSE's, which are operating below capacity, wondering where they can find this recognized source of medium term financing which is not highly collateralized in terms its lending practices.

It is worth pointing out that the use of old and worn out machinery, by the majority of SSE's have detrimentally affected the overall quality of their products. It is expected that the proposed "Medium Term Credit Program" will enable SSE's to replace their old and highly depreciated machinery with new ones. Thus, on one hand assisting SSE's in the overall improvement in their products quality. On the other hand, SSE's which need to expand their existing capacity by the procurement of new machinery will be able to do so by using medium term credit available through this proposed program.

c. Project Description

US-AID would provide $20 million to be divided equally between five banks. Hence, each bank would be allocated about $ 4 million to be used for financing the procurement of U.S. machinery and equipment for SSE's (as specified under "Beneficiaries of SSE's Credit Programs").

Based on data obtained from the DIB, it was determined that the average SSE's medium term loan in foreign currency was for LE.99,303 during 1984. DIB's medium term foreign currency loans to VSSE's averaged LE 69,861 during the same year. This implies that the average size of medium term foreign currency loans to both VSSE's and SSE's is about LE 85,000. The average loan size would imply that each participating bank may grant about 47 loans under funds allocated to it through the proposed "Medium Term Credit Program".

The funding size per bank can be justified on the following basis:

1) A smaller funds allocation per bank may not encourage program participation.

2) DIB's average loan granted to VSSE's and SSE's in 1984.

It is expected that SSE's would use this medium term credit program either for replacing old and worn out machinery and equipment and/or for acquiring more machinery to expand their existing capacity.

d. Principal Terms

1. Procurement

Each participating bank uses its allocated funds under the SSE's Medium Term Credit Program for on-lending to small scale firms as specified under "Beneficiaries of SSE's Credit Program". These loans are made in US $ for a single purpose only: the importation of U.S. manufactured machinery and equipment. Thus, the source and origin of the imported commodities should be the U.S.A.

This credit program should be available only to end-users, i.e. owners of small scale industrial firms who will use the imported machinery in their own factories to replace old and worn machinery or to expand their existing productive capacities. No other uses of funds available through the proposed Medium Term Credit Program should be permissible.

2. Interest Rate

In order to assist SSE's to achieve their growth and productivity objectives, the interest rate charged by participating banks should be the prevailing market rates for industrial activities at the time the program becomes effective as specified by the Central Bank of Egypt. Currently the interest rates for industry are between 11% and 13% per annum.

Furthermore, it is suggested that participating banks do not collect from SSE's any additional service charges greater than 1/2 to 1% of the size of the loan. Participating banks shall benefit from other features of the proposed Medium Term Credit Program. These benefits should offset the high administrative costs usually associated with relatively small loans, as claimed by bankers.

3. Exchange Rate

In order to assist the SSE's industrial sector achieve its developmental objectives which are compatible with the overall development strategy for the Egyptian economy, it is suggested that the exchange rate for this credit program be lower than the market rate. This will be an incentive to borrowers (SSE's) for using the proposed credit program. In addition, the lower exchange rate is an indication that US-AID recognizes the importance of the SSE's sector, in terms of the number of firms, share of industrial output and employment. It is also a recognition by USAID that the role played in the Egyptian economy by SSE's can be improved upon with the proper credit and technical assistance programs. The benefits which can accrue to the Egyptian economy from such programs should include higher growth rates in GNP, total and per capita incomes, employment, productivity and investment.

It is worth pointing out that currently, funds from the Production Credit program are disbursed at the rate of $1 = 1 LE. This exchange rate is lower than the official exchange rate of $1 = 1.34 LE., approximately. It is suggested that the exchange rate for the proposed SSE's Medium Term Credit Program be lower than the official exchange rate

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for the reasons outlined abobe. Furthermore, it is suggested that the exchange rate for loans be determined at the time the loan agreement between the borrower and banks is signed. Past history has demonstrated that credit programs designed specifically for SSE's have not been successful when the exchange rate was determined at the time of repayment.

4. Currency of Payment and Repayment

SSE's are granted loans in U.S. dollars for importing American manufactured machinery and equipment. Repayment of loans is undertaken in Egyptian currency at the official exchange rate prevailing at the time the loan agreement is signed between the borrower and the bank. This stipulation is suggested in order to assist SSE's in achieving their overall goals of operating at full capacity, improving their products quality and increase their contribution to industrial output, investment and employment.

5. Grace Period and Period of Repayment by SSE's

It is suggested that the Period of Repayment for the proposed Medium Term Credit Program be 5 years exclusive of the "Grace Period". Furthermore, it is suggested that the Grace Period be no greater than 2 years.

It is believed that a two years grace period is sufficient for bringing on stream the usage of the imported machinery and equipment. Moreover, medium term foreign currency loans available to DIB clients for the past several years stipulated grace period of up to three years. Furthermore, the maturity of foreign currency loans, available at DIB from international organizations, was up to 10 years excluding grace

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period. Thus, the suggested five years as repayment period for the loans available through the proposed Medium Term Credit Program are within the general practice.

6. Down Payment

Ideally, no down payment should be required by SSE's who are the beneficiaries of the proposed Medium Term Credit Program. The reason being that a large number of SSE's operate below capacity because of a liquidity problem. Thus, a 25% downpayment as it is currently specified under the Production Credit program for end users, may add to the liquidity burden of SSE's.

On the other hand, a down payment of 10%-15% is suggested. This downpayment is below the 25% currently stipulated under the Production Credit Program.

7. Collateral Requirements

Beneficiaries of the proposed Medium Term Credit Program should pledge the imported machinery and equipment as collateral for obtaining the loans. Complete ownership of machinery and equipment financed through the proposed credit program should remain with the participating bank until the loan is repaid in its entirety.

The establishment of a Credit Guarantee Fund should be used as additional security to the lending institution. The high collateral requested by Egyptian banks have prevented the majority of SSE's from obtaining the loans they need. Participating banks are expected not to insist on more collateral than the ones specified through this credit program.

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It is worth pointing out, that the issue of collateral is a very sensitive issue from banks' point of view. A dialogue between US-AID's representatives and participating banks officials should bring lead to concensus between all parties concerned on this sensitive issue.

8. Funding Limits

It is suggested that medium term loans from the proposed credit program should not exceed LE 120 thousand. This funding limit is compatible with DIB loans for VSSE's and SSE's during 1984. Furthermore, the upper limit take into consideration an inflation rate of approximately 15%. While the lack of lower limit specification allows the relatively small firms access to the credit program. On average, loans are expected to be in the range of LE 80 to LE 90 thousand.

It is worth pointing out that the average loan through the Production Credit Program was for LE 179 thousand. These loans were for end users with maturity not exceeding three years.

e. Criteria for Banks Selection

The criteria for banks selection for the "Medium Term Credit Program" should be identical to the ones specified under the working capital facility.

f. Proposed Banks for Program Participation

It is suggested that Banks which should participate in the proposed Medium Term Credit Program should be different from the ones selected for the Working Capital Program. The reasons for this suggestion are:

1st: to establish the widest possible linkage between SSE's and as many lending institutions as possible. The reasons for this being that once such linkage is established through the proposed US-AID programs, it is expected that these credit programs will prove successful and continue in the future even as AID's role gradually diminishes.

2nd: since the size of loans are relatively small, implying that the number of loans from each fund are expected to be numberous. Thus, the absorptive capacity of banks participating in the Working Capital Program, may have been exhausted. Hence, the reason for involving other banks in the Medium Term Credit Program.

The banks which sould be approacned first are the remaining banks from the Production Credit Program. Other Egyptian banks may also be invited to participate in order to bring the number of banks in the term lending program to five as previously suggested.

g. Participating Banks Function and Role

It is suggested that US-AID develops some clear and specific and complete guidelines governing all issues for loan applications and approvals, as well as, other issues pertaining to the proposed credit programs. Hopefully, such stipulation should expedite processing and specific criteria for approvals or rejections. Issues of staffing and their daily obligations would necessitate minimum US-AID's involvement in the supervision of the two proposed credit programs.

C. US-AID Options For Encouraging Banks Participation in SSE's Credit Programs

a. Introduction

Past history has demonstrated that Egyptian Banks have been quite reluctant in meeting SSE's demand for credit. Moreover, the smaller the firm, in terms of its number of employees and the value of its fixed assets, the more likely that it has been exluded from participating in credit facilities at formal financial institutions. This problem becomes even more complex by the fact that small enterprises do not usually keep

good financial records, or do not keep them at all. Thus, based on these records, or the lack of them, financial institutions cannot establish the credit worthiness of SSE's when they apply for loans. Furthermore, the complexity of the SSE's credit worthiness is further aggravated by the fact that a large percentage of SSE's do not own the land nor the buildings where their businesses are located. Thus, the two most important collaterals, from the bank's point view, i.e., land and buildings are not owned by SSE's loan applicants. This fact leads to the rejection of most SSE's loan application by financial institutions which are extremely conservative in their lending practices. It is worth pointing out that Egyptian banks lending practices rely very heavily, if not solely, on collateral, with value on the average, equal to 200% - 300% of the loan amount. Based on all these facts and others previously outlined in this study, one may conclude that Egyptian Banks will not participate in credit programs designed specifically to meet the needs of SSE's unless they are "encouraged" to do so. Hence, in order to attract banks participation in the two proposed credit programs, some incentives should be provided. Some of the incentives and/or features of credit programs designed to serve the needs of the Egyptian SSE's sector are briefly suggested below.

b. Option 1: <u>The Interest Rate Spread</u>

A possible option which may be considered to entice banks to participate in the two proposed credit programs is the interest spread approach. This implies that each participating bank will be lent the

allocated funds for on-lending. Each participating bank will be charged an interest rate on the undisbursed funds. This rate of interest charged to participating banks must be lower than the market rate charged to their SSE's clientele as specified in each proposed credit program.

The question which needs to be addressed is the following: how much of an interest spread should participating banks receive? From the banks point of view a 5% interest spread would be considered quite rewarding.

This implies that banks would be lent the allocated funds at about 6% to 8%while they lend it to their SSE's customers at the market rate of interest for industry which are currently between 11% and 13%, a determined by the CBE. Note that suggesting charging the lowest interest rate possible to SSE's can be justified for the following reasons:

(1) To assist SSE's achieve the development objectives of productivity; growth in income, employment and investment; in addition to improving the quality of their products, which should lead to imports substitution and/or exports. In either cases, the Egyptian economy can achieve a higher rate of growth and a better balance of payments and trade.

(2) SSE's which have not sought bank credit have indicated that one of the major reasons was that interest rates were too high.

Note that although a 4% interest spread may not be as attractive as a 5% spread, from banks point of view, but it is believed that it may be still acceptable to banks.

The interest spread option may be justified for compensating banks for the "high" administrative costs associated with small loans. In addition, to encourage banks to participate in the proposed credit programs by making it profitable for them. Based on the assumption that each bank will receive about $ 4 million, this implies that the interest spread option would result in the receipt of between $160,000 to $200,000 by each participating bank. Thus, the overall cost of the "Interest Spread Option" assuming that 10 banks would participate in the two proposed credit programs, would be between $2 million and $1.6 million.

It is worth pointing out that the "Interest Spread Option" may be combined with a grant for training participating banks employees in loan processing, as well as, project analysis, marketing the SSE's credit programs and other training which may be of interest to banks personnel(1).

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(1) The Training Of Banks Personnel Option and the "Credit Guarantee Fund Option" will be discussed below.

c. Option 2: The Reverse Interest Spread

Another option which may be considered for encouraging banks participation in the two proposed credit programs is the "Reverse Interest Spread Option". Under this option, funds will be allocated to each bank according to the current Production Credit program and at the same cost. Banks will lend funds to their SSE's customers at the market rates of interest for industrial activities as specified by the CBE. These rates of interest are currently between 11% and 13%. But it is worth pointing out that the rate of interest on CBE's "Investment Certificates" with 6 months maturity is 13 1/4%. Egyptian banks have to compete with the interest rate on these "Investment Certificates" in order to mobilize customers deposits for term lending. Thus, banks must develop the monetary instruments which can compete with the 6 months "Investment Certificates" by paying a higher rate of interest than 13 1/4%. Hence, funds especially for term lending are costly to banks, which may justify the "Reverse Interest Spread Option" by advocating paying participating banks an agreed upon interest margin to encourage them to participate in a credit program for a clientele which banks have been generally reluctant to accommodate.

A 4% to 5% interest spread may prove to be attractive for banks participation. It is worth pointing out that with an inflation rate of 19% to 15% in the past two years, respectively, the interest margin may be justifiable from the banks point of view.

In order to encourage banks promotion of the proposed credit programs, the reverse interest spread should be payable only on disbursed funds. Thus, encouraging banks for quick disbursement which would make them eligible for collecting their interest margin on the loans granted.

The overall cost of "Option 2" would be between $2 million and $1.6 million. This cost assumes that 10 banks will participate in the two proposed credit programs. Each bank will be allocated $4 million for on-lending to SSE's.

d. Option 3: Percentage for Funds Management

Another option which may be used to entice bank participation in the two proposed credit programs, is the "Percentage For Funds Management Option". This option may be used instead of the two other options suggested above. Participating banks would be allowed a 4% to 5% as a fee for managing the funds allocated to each bank. This percentage for funds management will assist banks in reducing the administrative cost of processing relatively small loans. In addition, "Option 3" should assist banks in the cost of promoting and marketing the SSE's credit programs.

This option is suggested if objections to the concept of interest spread (whether regular or reverse) arise within the Mission. Under Option 3, banks would be allocated funds using a similar mechanism as being currently used under the Production Credit Program.

The overall cost of this option would be between $1.6 million and $2 million. The actual fee for Managing Funds should be finalized through a dialogue between US-AID and participating banks.

e. Option 4: Fee Per Loan Granted

This option specifies that participating banks collect a fee for processing loans to SSE's from the two proposed credit programs. The proposed fee should be between 4% to 5% from the size of the loan. The difference between Option 3 and Option 4 is that in the latter the fee is collected once a loan is processed, while in the former the fee is not specifically linked with disbursements. It is believed that linking fee collection with disbursement would be a sound idea. This will encourage participating banks to promote and market the SSE's credit program for the ultimate objective which is granting loans to SSE's. Option 4 is suggested as an alternative to the previous three proposed options if their concepts are objectionable. The overall cost of Option 4 will be between $1.6 million and $2 million. This cost estimate is based on the assumption that 10 banks will be participating in the two proposed credit programs. Each bank will receive $4 million fo on-lending to SSE's.

f. Option 5: Credit Guarantee Fund

The establishment of a "Credit Guarantee Fund" must be the center pivot of the two proposed SSE's credit programs. The purpose of the proposed guarantee fund is to serve as a mechanism for alleviating the fears of participating banks against default by some SSE's which will use the proposed credit programs. Furthermore, establishing the proposed "Credit Guarantee Fund" should serve to reduce the amount of collateral usually requested by banks in order to approve a loan. As previously stated, the value of collateral usually requested by banks represent more than 200% of the value of the loan being negotiated.

Ideally, both the GOE and US-AID should equally share the cost of establishing the Credit Guarantee Fund. Hence, a dialogue between US-AID representatives and the appropriate GOE officials should serve to emphasize the important role played by SSE's in the Private Sector, in particular, and the Egyptian economy in general. This role has been steadily growing since the adoption of the Open Door Policy of 1974. It is strongly believed that the contribution of the SSE's sector to Egyptian industry may double with the proper credit programs. As previously stated, the majority of SSE's are currently operating at 50% below capacity due either to the lack of liquidity for financing working capital and/or continuous break down of their old and outdated machinery and equipment. Based on the above, the two credit programs, previously outlined, were suggested.

These credit programs should serve to provide the needed short and medium term credit to SSE's so they can operate near capacity All the above arguments should be emphasized to GOE officials for inviting participation in the proposed "Credit Guarantee Fund".

It is suggested that the "Credit Guarantee Fund" should represent between 15% to 20% of the overall funding size of the SSE's credit programs. Based on an estimated funding size of $40 million for the 10 participating banks, the value of the credit guarantee fund would be between $6 to $8 million. Assuming equal contribution to the fund by both parties, US-AID share would represent $3 to 4 million.

It is suggested that the mechanism by which the proposed "Credit Guarantee Fund" would function should be as follows:

As a loan is approved to a small scale firm, US-AID and GOE representatives are informed about the size of the loan. A deposit is made with the participating bank by both the GOE and US-AID. This deposit should represent the previously agreed upon percentage of the loan. It is further suggested that this deposit shall remain with the participating bank until the loan is repaid. This approach should serve to reduce the fears of participating banks of possible default of a minority of their SSE's customers.(1)

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(1) Another alternative is to credit the account of the participating bank at the CBE for the agreed percentage of the processed SSE's loan.

Note that although a range of percentages specifying the size of the Proposed "Credit Guarantee Fund" was suggested, the actual percentages should be agreed upon through a dialogue between the GOE, US-AID and participating banks. Once the size and mechanism of the Credit Guarantee Fund is agreable to all parties concerned, it is believed that it will become the cornerstone upon which the SSE's credit programs would rest. It should also be the missing link for encouraging banks participation. Furthermore, it should reduce the perceived risk, from banks point of view, of participating in an SSE's credit program.

g. Option 6: Training of Participating Banks' Employees

One of the main features of the two proposed SSE's credit programs is the training of participating banks employees. The objectives of "Option 6" is to make it advantageous to banks to participate in a credit program designed for a clientele they have been reluctant to serve. Each participating bank may designate five to 10 employees for training at some good Egyptian institution like AUC, for instance.

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The proposed training of banks personnel should cover the following areas:

Credit analysis, project analysis, marketing and promotion of credit programs with special emphasis on the credit needs of small scale firms. Other training topics may also be added to the program based on the training needs of each participating bank. "Option 6" should be a grant to participating banks. Banks would be willing to participate in the two proposed credit programs because of the benefits which will accrue to them. It should be emphasized that "Option 6" and "Option 5" are key elements for the success of the proposed SSE's credit programs. In addition to "Options 5 and 6" one more option may be selected from the first four proposed options to make the overall SSE credit "program/package" very attractive from bank's point of view.

The estimated cost of training for each bank's employees at AUC, or other similar institutions, would be around $650 per week. Depending on the topics to be covered in the proposed training program, it is estimated that on average this training should require two weeks per year for each bank employee. Thus, the annual training cost per bank would be estimated at between $6,500 to $13,000.

The overall cost of "Option 6" based on the assumption that 10 banks will participate in the two proposed credit programs would be between $65,000 and $130,000 per annum.

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VIII. Conclusion and Summary of Findings

This report had two objectives. The first objective was to assess the role currently played by small-scale industrial firms in the Egyptian economy. The second objective was to propose credit programs which can satisfy SSE's needs and requirements.

These two credit programs were proposed after examining the various credit constraints which have hindered SSE's growth and productivity.

This report has demonstrated that SSE's role in Egyptian industry is important in terms of its contribution to Private Sector industrial output:

1. It is estimated that VSSE's, i.e., firms with 10 to 50 employees, contribute about 61.4% to Private Sector's industrial output. This represents 21% of total industrial output.

2. It is estimated that SSE's contribution to Private Sector's industrial output currently stands at 75%. This represents 25.7% of total industrial production[1].

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(1) SSE's are defined, in this report, as firms employing 10 to 200 workers and the value of their fixed assets not exceeding LE 500 thousand, excluding land and buildings.

This report has also demonstrated the importance of SSE's in the Egyptian economy as represented by their contribution to the number of firms. For instance, VSSE's represent 90.6%, or 11,774 establishments, of the total number of industrial firms which were estimated at 13,000. Furthermore, SSE's represent about 98.6%, or 12,814 firms, of privately owned industrial firms operating in Egypt.

It is worth stating that in order to highlight the role played by SSE's in Egyptian industry, the role played by the Private Sector in Egyptian industry had to be examined. The Private Sector's role in Egyptian industry has been steadily growing since the adoption of the Open Door Policy of 1974. Currently, the Private Sector's contribution to total industrial output stands at 34.3%, or LE 2,929.4 million. It is worth stating that these figures are based on Ministry of Industry's data. However, privately owned Egyptian firms usually under-report the level of their output, their investment and the number of their employees in order to avoid paying taxes. Thus, the real contribution of the Egyptian Private Sector to Egyptian industry should exceed 34.3%. Furthermore, the output of artisinal firms which are involved in industrial type activities is not included in the above figures. This is due to the fact that artisans are not under the Ministry of Industry's supervision.

It is estimated that the output of the 250 thousand artisinal firms represent 15% of total industrial production.

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Based on the above, one can state that Private Sector's contribution to Egyptian industry would exceed 45% when the output of the formal and informal sectors are combined.

The report has also indicated that VSSE's play an important role in each industrial subsector, using Ministry of Industry's classification.

The report has also highlighted the various government regulatory agencies that SSE's have to interact with, from the idea stage and through the life of the company. It appears that SSE's, like other Private Sector firms, have to put up with a lot of red tape and government bureaucracy. This cost firms a lot of effort and time which can be devoted to more productivity within their enterprises. It also seems that Egyptian laws and regulations are designed for controlling economic activity and may often hinder its growth.

The examination of SSE's use of credit indicated that the majority of these firms were denied bank credit. The reasons for this being that the majority of SSE's lack the required collateral mostly requested by banks, ie., land and buildings. In addition, most SSE's do not keep adequate financial records. Hence, their credit worthiness status may not be established.

This problem is further aggravated by the fact that Egyptian banks are extremely conservative in their lending practices. For instance, the value of collateral requested by banks usually represent between 200% and 300% of the loan size. These conservative lending practices have worked against SSE's interests. A large percentage of SSE's raise the needed funds either through relatives and/or friends or by taking additional partners. This report has also indicated that a large number of SSE's are operating at 50% below capacity for the following reasons:

1. The lack of funds for financing their working capital needs;

2. The lack of funds for replacing their old, worn-out and outdated machinery and equipment.

Based on the above, it was determined that SSE's credit needs can be divided into two major categories:

1. Short-term financing of working capital for off-the-shelf procurement of raw materials and intermediate goods.

2. Medium-term financing for importing U.S. manufactured machinery and equipment.

It is believed that the removal of SSE's credit constraints would enable them to operate near capacity; thus, increasing their productivity and growth. The benefits to the Egyptian economy will be realized in terms of increasing the supply of goods, income, employment, investment, etc.

Other constraints which were found to be hindering SSE's productivity can be summarized as follows:

1. Production Constraints:

Production constraints arise because of machine breakdown. Spare parts may not always be available and often have to be "manufactured". This causes delays and results in idle machinery. In many occasions, good repairmen are not available for fixing machine problems.

The lack of skilled workers has also been a constraint affecting SSE's production processes. A large number of skilled Egyptian workers has sought higher paying jobs in Arab countries. Another production constraint is the inability of firms to hire unskilled workers. This may be due to the fact that would-be workers do not want to subject themselves to the discipline that working in a factory would require. Another reason for the lack of unskilled workers is that other work opportunities pay higher wages than small scale industrial firms.

The lack of raw materials in the required quantities and/or qualities also represent a constraint on SSE's production. It is worth pointing out that Public Sector's enterprises remain, in many cases, the sole source of raw materials. The GOE establishes raw material quotas which prevent SSE's from operating at capacity.

2. Labor Constraints:

Egyptian workers do not like to subject themselves to the discipline that working in a factory necessitates. Labor absenteeism and rapid turnover have ill-affected SSE's productivity. Absence without permission after paydays is often practiced. Labor's mobility between competing factories has had a negative impact on SSE's. Egyptian workers often seek lower paying jobs in Public Sector enterprises because of the "perceived" security associated with working in these establishments.

SSE's managers/owners tend to forgive workers all the above-mentioned practices because of their inability to find replacements.

3. Marketing Constraints

Managers/owners do not consider marketing as the major concern of their enterprises. Hence, they relegate marketing t third place in their priorities behind production and finance. The

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majority of SSE's do not promote their products. This is based on their beliefs that demand for final goods exceeds existing supply. Hence, any products manufactured by SSE's can be sold without difficulties.

It is believed that distribution outlets and centers would not be very beneficial for marketing SSE's products. The Private Sector producers would benefit from an organized distribution network, as well as consumers.

4. Other Constraints

Related to Managerial Skills may be of less importance than previous ones. It is quite evident that the majority of SSE's managers lack the proper training in bookkeeping, accounting, modern production techniques and processes, production planning forecasting, cash flows for avoiding liquidity problems, etc.

5. Another constraint is the lack of appropriately priced sites for firms which want to relocate for expanding their productive capacities.

Egyptian Laws and Regulations have also ill-affected SSE's growth and productivity. The lack of stability in Egyptian economic policies often confuse and discourage SSE's plans as formulated by managers/owners.

Based on discussions with various experts on Egyptian industry, it became quite evident that up till our present time, there is no specific government policy for developing the SSE's sector. Moreover, there is no public official spokesman for this important sector of the economy. Furthermore, there is no single definition of small scale firms which have been adopted by the various government institutions. Furthermore, the only two Egyptian institutions which do have specific definitions for the small scale enterprises sector are the DIB and the Institute for National Planning. It is interesting to note that definitions adopted by DIB and INP are completely different.

Due to the lack of universal definitions classifying the SSE's sector, four distinct definitions were suggested in this report. These four definitions take into account a firm's number of employees and the value of their fixed assets, excluding land and buildings. It is hoped that the Egyptian government and its institutions adopt some of the suggested definitions which classify the SSE's sector into various subsectors. Then, begin formulating and adopting economic policies for developing this important sector of the economy.

IX. Recommendations

Based on the objectives of this report, its findings and other credit impediments to the Private Sector, the following recommendations are suggested:

1. To establish the SSE's Working Capital Credit Program for financing the local currency off-the-shelf procurement of raw materials and intermediate products. This program will enable SSE's to solve their liquidity problems. Thus, allowing SSE's to acquire the necessary funds for purchasing the needed raw materials and intermediate products.

The proposed credit program should assist SSE's for operating at full capacity. It is worth pointing out that the lack of sources of credit for financing working capital have resulted in a large number of SSE's operating at 50% below capacity. This idle capacity should be productively utilized to increase the supply of goods to Egyptian consumers, as well as exporting any excess supply.

2. Participating banks would rather be granted U.S. dollars for on-lending, while they lend Egyptian pounds to their SSE's clients. In the event that this procedure is not acceptable to AID/Washington, reflows should be used to establish the proposed Working Capital Credit Program. Similar issues can be finalized through a continuous dialogue between US-AID and banks interested in participating in the proposed SSE's credit programs.

3. Mission management should make a decision on the beneficiaries of the proposed Working Capital facility. Seven different options specifying beneficiaries have been suggested. Based on the recommendations outlined in this report, Mission management should select one of the proposed beneficiaries options.

4. Based on the terms of existing US-AID Private Sector's credit programs, it is suggested that the proposed SSE's Working Capital Credit Program should be a separate program. This is due to the fact that it is a local currency program and its terms differ from other existing US-AID credit programs.

5. Modify the existing Production Credit Program in order to incorporate in it the proposed Medium Term Credit Program. These modifications will render the Production Credit Program suitable to SSE's needs. Moreover, the various suggested options for encouraging banks participation in the proposed SSE's credit programs should prove attractive from bank's point of view.

The terms of the Production Credit Program which need to be amended are:

a. Grace Period and Period of Repayment;

b. Down Payment;

c. Collateral Requirements;

d. Funding Limits;

e. Beneficiaries.

6. The modified Production Credit Program should also include the proposed "Credit Guarantee Fund" and the "Training for Participating Banks Personnel" options, mainly in the SSE's component of the facility. Furthermore, one of the other suggested options should be added to the modified Production Credit Program in order to make the whole SSE's credit "package" very attractive from bank's point of view.

7. US-AID should continue the dialogue with the GOE to reduce the constraints and regulatory climate that SSE's have to confront in their daily operations.

8. US-AID should encourage the GOE to formulate a clear, specific and sound policy for promoting the growth, productivity and general well being of SSE's.

9. US-AID should encourage the GOE and all its institutions to develop a specific, clear and logical definition of SSE's. Suggestions made in this report on the various definitions which classify the SSE's sector into: artisans, "Very" SSE's; "Average" SSE's; "Large" SSE's should be made available to the GOE for possible adoption.

10. Once agreement is reached for specific definitions of the SSE's sector, universal adoption by all Public and Private Egyptian institutions should be enforced. This adoption will be helpful when formulating and/or implementing economic policies related to the SSE's sector as a whole, or one of its subsectors. Moreover, technical assistance programs may be geared for specific subsectors of the SSE's sector which may need this assistance more than other subsectors.

11. US-AID should encourage the GOE to specify an entity which is devoted to the welfare of SSE's.

12. US-AID should also encourage the GOE to designate an individual or a group of businessmen to act in the capacity of SSE's spokesmen. These highly-respected businessmen should express the needs and requirement of SSE's on all issues related to their welfare, productivity, growth, technical and credit assistance.

13. US-AID should continue its dialogue with the GOE on establishing industrial sites with the proper infrastructure to satisfy SSE's needs.

14. US-AID should continue its assistance to the GOE for establishing Vocational Training Schools which should alleviate the shortage of skilled labor.

15. US-AID should finance a study on the labor problem in Egypt. This is based on SSE's complaints about the lack of unskilled workers. Other labor problems identified in this report should also be examined. The recommendations of such a study can help in curing the problems associated with a crucial and essential factor of production, i.e., labor.

16. US-AID should explore the type of technical assistance that can be provided to SSE's by the following Egyptian institutions:

a. The Federation of Egyptian Industries;

b. The Small Scale Enterprise Department at GOFI;

c. The Engineering and Industrial Development Center;

d. Vocational Training Department at the Ministry of Industry;

e. The Small Scale Department at DIB;

f. Engineering and Industrial Development Centers located all over Egypt.

17. US-AID should contiue its dialogue with the Central Bank of Egypt for modifying the current structure of interest rates. The proposed changes in interest rates should make them a positive function of maturity. Thus, banks should be allowed to charge higher rates of interest on loans with longer maturity.

18. US-AID should indicate to the GOE the ill-effects to the economy of the current interest rate regulations requiring banks to charge lower rates for industrial and agricultural activities. It is believed that these regulations did not take into consideration banks' point of view. Moreover, these regulations have encouraged banks to grant the largest percentage of their loans to Trade and Services, since they can charge them higher rates than the productive sectors of the economy. Services and Trade loans are usually for short maturity and result in higher profits for banks.

19. US-AID should begin a dialogue with Islamic Banks in order to find avenues for cooperation among them. It is worth pointing out that Islamic Banks operating in Egypt have mobilized large sums of funds from their depositors and are always eager to find good avenues for lending these funds.

It is worth noting that some SSE's managers/owners do not want to seek bank credit because of their opposition to paying interests which is considered "usury", hence not permissible according to the teachings of Islam. Hence, to these group of individuals the Islamic concept of banking should prove to be attractive. Mutual cooperation between US-AID and Islamic Banks for assisting the Private Sector in general, and SSE's in particular, in its credit needs should be explored through a friendly dialogue.