

Small Enterprise Development in Egypt

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June 1, 1992

A Report on the Development of the Small and Micro Enterprise Project (263-0212), the Credit Guarantee Corporation under Private Enterprise Credit (263-0201), and the Small Enterprise Credit Project (263-0228)

This report is written in fulfillment of Contract # 263-102-S-90-8055-00. It is to be submitted to PPC/CDIE/DI, ACQUISITIONS, Room 209, SA-18, Agency for International Development, Washington, D.C. 20523

PREFACE

The following report is intended to be more of a historical report rather than an analytical report. Most analysis and recommendations by this consultant are contained in the technical sections of the Small and Micro Enterprise Project Paper (263-0212) and its pending project paper amendment for expansion, the Small Enterprise Credit Project Paper (263-0228), and in the Guarantee Finance Facility Agreement with the Credit Guarantee Corporation. Further technical recommendations are contained within the cooperative grant agreements that resulted from the projects mentioned above. Most technical direction to the various clients was delivered through constant interaction between them and this consultant. The intent of leaving a historical report is to assist those who will be responsible for the implementation of all of the projects in the future, and I wish them well.

All of the projects developed during the period of this consultancy have had the benefit of the growing body of information that AID and other donors have developed in the field of small and micro enterprise development. The key issues of outreach to the borrower, simplification of applications and approvals, utilizing end-use interest rates or fees that can help to insure the long-term viability of the institutions carrying out these projects, and the establishment of modern management information systems have been taken into account. To the degree possible in the Egyptian context, these projects are set-up to be world class models, albeit through various approaches based on the capabilities of the various implementors and the extant situations.

THE SMALL AND MICRO ENTERPRISE PROJECT

BACKGROUND

This consultant's services for the USAID Mission in Cairo under this contract began in May 1988. The Mission had decided in mid-1987 to pursue development of a project that would benefit small and micro entrepreneurs in the metropolitan areas of Alexandria and Cairo. This general decision was reached, at least in part, because no broad scale assistance had been delivered to this sector, the population of Alexandria and Cairo makes up over 25% of Egypt's population, and it appeared that the highest proportion of productive small and micro enterprises probably were located within these two metropolitan areas. One of the tasks of this consultant was to operationalize the political commitment that was made by the Mission. It should be noted that the development of the Small and Micro Enterprise (SME) Project (263-0212) was facilitated greatly by strong support of both the previous AID Director, Marshall Brown, and the previous Ambassador, Frank Wisner.

PROJECT DEVELOPMENT

The services of the National Cooperative Business Association (NCBA, also known under the corporate name of Cooperative League of the United States of America, CLUSA) and the local firm of Environmental Quality International (EQI) were obtained to perform a

feasibility study of delivering assistance to small and micro enterprises. The main consultants involved in this study were Robert G. Blayney, Peter Bittner, and William Tucker of NCBA, and Dr. Mounier Nematah, President of EQI, along with some of his staff. The feasibility study was carried out in April-May 1988. The results and recommendations of that study played a major role in the overall design of the resulting project.

It was clear during the preliminary design phase that no Egyptian banks were willing or capable to provide credit to very small borrowers. The avenue of utilizing private, non-profit foundations to act as intermediate credit institutions presented itself as being the option with the greatest possibility of success. This also fit with the Mission's emerging strategy of greater involvement with the private sector, both as implementors and beneficiaries. It was with those conditions that the project design was established.

The project paper was written during the summer of 1988, during the same period as negotiations were being simultaneously carried out with the Alexandria Businessmen's Association (ABA), the Egyptian Small Enterprise Development (ESED) Foundation, and the Ministry of International Cooperation (MIC). The project paper was authorized by the Mission in September 1988 shortly before the grant agreement was jointly signed with the MIC.

Negotiations with each of the three parties noted above were difficult. The MIC had to be convinced on three major points.

1. The MIC had primarily dealt with AID delivering assistance to the public sector, and the fact that AID wanted to deliver assistance to the private sector, through the private sector, was a major point of negotiation.
2. There was (as still is) very little hard statistical data on the existence of the small and micro enterprise sector. They generally do not appear in common measures such as the CAPMAS (National Statistics Bureau) or under registries such the Department of Corporations. The SMEs targeted for assistance were "institutionally invisible".
3. The successful approaches that have evolved over the past several years of worldwide experience in dealing with small and micro entrepreneurs were totally unfamiliar to the MIC. These approaches include utilizing market interest rates for credit, on-site loan development and supervision, and treating the small borrower as a financially responsible entity.

However, MIC eventually agreed to the approach described in the project paper and signed the grant agreement. That grant agreement allowed AID to enter into direct grant agreements with the two foundations and to a direct contract for technical services.

Negotiations with the two Foundations¹ were also protracted, although most of it was conducted in a spirit of cooperation. The two Foundations, being totally separate entities, both had to develop their understanding of the technical imperatives of small enterprise credit delivery and collection, along with the demands that AID has in order for them to become a qualifying entity with which AID can enter into a formal agreement. One of the most difficult hurdles that the Foundations had to clear was to get themselves registered as a private, non-profit organization under the Ministry of Social Affairs.² In both cases, particularly with the ESED, the facilitating role of the FSN Project Specialist, Magdy Khalil, with the Ministry of Social Affairs, cannot be overstated.

The Foundations were successful in meeting the requirements of both the Government of Egypt (GOE) and the United States Government (USG). This included both their official registration with the GOE's Ministry of Social Affairs and compliance with USAID rules and regulations. A key point for AID to be able to "recognize" the two Foundations was to have a blank set of books set up for each Foundation by a local consulting firm. With considerable assistance from AID's office of Contract Services, particularly Orion Yeandel, the original cooperative grant agreements with the ABA and the ESED were signed in April and May 1989, respectively.

The contract for technical services is a direct contract. The request for proposal (RFP) was released in October 1988 with all bids received by February 1989. The RFP called for a United States-based prime contractor with an Egyptian sub-contractor. The winners, the National Cooperative Business Association as the prime and Environmental Quality International, the sub-contractor, were awarded the contract in April 1989, again with considerable cooperation between the technical office, which is now Finance and Investment, and the Office of Contract Services. The original thirty-month contract required the services of one long-term expatriate advisor, two long-term Egyptian advisors, and sixty

¹ It is important to note that the two foundations have different backgrounds. The ABA was already in existence at the beginning of the project, it was made up of over 200 private sector members which then formed an Executive Committee to carry out most of its decision-making. The ESED had considerable input from AID in its formation and lacked some of the social cohesion (initially) that already existed within the ABA. This has had some effect on project implementation. The proposed project amendment requires that new foundations that will implement the project be already in existence and be registered with the Ministry of Social Affairs.

² A good analysis of Law 32, which is the governing law for non-profit foundations, is found in Small and Micro Enterprise Development: A Study of the Regulatory Framework, Integrated Development Consultants, Cairo, November 1991. This study was commissioned by the Small and Micro Enterprise Project, and is on file with the Office of Finance and Investment at USAID/Cairo.

months of a range of short-term assistance. Following the initial thirty month contract, the contract was extended for an additional year, and is currently effective until October 1992.

The period from May-December 1989 was primarily dedicated by the Foundations to identifying and training appropriate staff, locating and procuring headquarters, and equipping the offices. The initial management information systems work was carried out during this period also, although that work did not near completion until late 1991. End-use lending began in Alexandria in January of 1990, with the first loan releases taking place in Cairo in November 1990. A chart showing the growth of lending is attached at the end of this report. Detailed reports of lending, broken down by business type, gender of borrower, loan size, loan duration, and location of borrowers are on file with TI/FI.

OBSERVATIONS

The project has been observed by a range of interested observers and analyzed by a range of experts in various aspects of microenterprise development, including a mid-term evaluation,³ and by specialists reviewing particular features of the project including the role of women⁴ and the efficacy of the funding mechanism being utilized.⁵ The project is generally judged as a success at this point in time.

The project is still in its early stages when compared with more mature small and micro enterprise activities such as the *Grameen* Bank in Bangladesh, the *ADEMI* activities in the Dominican Republic, and the various approaches being implemented in Indonesia such as the *Kredit Usaha Rakyat Kecil* (KURK) in East Java, the *Badan Kredit Kecamatan* (BKK) in Central Java, and the nationwide small enterprise delivery system, *Kredit Usaha Pedesaan* (KUPEDES) being operated by the Bank Rakyat Indonesia, but compares favorably. The project has experienced no default to date, late payments are generally no more than 2-3% of outstanding balances, and the portfolio is still growing rapidly; in the recent months the ABA has been extending nearly one million Egyptian pounds and ESED has been exceeding

³ Small and Micro Enterprise Development Project: Midterm Evaluation, GEMINI Technical Report No. 30, Katherine Stearns, ACCION International, March 1992.

⁴ An additional study, partially funded by the SME project and partially by the Office of Women in Development in Washington, was carried out over nearly a year. The final report, Egyptian Women and Microenterprise: The Invisible Entrepreneurs, GEMINI Technical Report No. 34, Jean Weidemann and Zohra Merabet, contains information relevant to the SME project itself along with larger implications for assistance to women entrepreneurs in Egypt.

⁵ Analysis of Funding Mechanisms for Small and Micro Enterprise Development Project, (DRAFT), Kenneth Angell and John Porges, Development Alternatives, Inc., May 1992

LE 500,000 per month. This is an indication of the increasing skills of the Foundations' respective staffs.

The challenge for both of the Foundations at this point in time is to increase both their number of loan officers and the required number of support staff, and to maintain their focus on timely repayments. The MIS established by the project gives Foundation management timely information on repayments, and immediate follow-up of any late payments will remain critical to the long-term success of the project. Establishment of more branch offices will also require the further development of middle management such as branch office and financial managers.

The challenge to USAID/Cairo is whether or not they have the wherewithal to expand the project to other areas. If the will exists on the part of management, contracting both expatriate and Egyptian technical assistance will have to be undertaken immediately. The services provided to date have been outstanding. The evidence of mutual cooperation among the contractors, the Foundations' management, and USAID staff is the success that the project has achieved to this point in time.

It is important to note for future project development that providing funding for international observational tours was critical to the development of this project. Experience with small and micro enterprise credit systems was extremely limited in Egypt previous to the implementation of this project. The initial trips made to Indonesia and the Dominican Republic were crucial in allowing the Foundations' management teams to observe successful credit projects. Although the systems that have emerged in Egypt are unique in many respects, they have greatly benefitted from direct observation of other projects in other countries. Future projects implementation should include funds for project management, both USAID and the Egyptian counterparts, to attend international conferences or specific visitations to selected projects.

SMALL ENTERPRISE CREDIT PROJECT

BACKGROUND

A rural credit project, the Rural Small Scale Enterprise (RSSE) Pilot Credit Project was initiated under the Local Area Development (LD II) project in the Delta area governorates of Damietta and Sharkiya. Initial design work for the project began in September 1987; end use lending in the two governorates began in October 1989. The pilot project was implemented through the National Bank for Development (NBD). The project focussed on making short-term (4-12 months) that were primarily working capital loans. A broad range of borrowers were included who represented the service, trade, and light manufacturing industries. The project used a methodology of weekly visitations to borrowers, and featured variable principal repayment schemes combined with a rebate system for all borrowers who repaid on-time and in-full. Repayment levels approached 100%. An

evaluation⁶ was carried out in November 1990 that essentially declared the pilot project a success.

PROJECT DEVELOPMENT

Based on the results of the evaluation and other evidence, USAID/Cairo Mission management decided to move ahead with a project design that would use the same basic methodologies as had the RSSE project, but to design the project to be implemented in the metropolitan Cairo area.

A sense of urgency in getting the project designed developed, primarily because of initial discussions with the World Bank sponsored "Social Fund". The Social Fund was to be a multi-donor sponsored activity; The Bank managed to obtain pledges in excess of US\$500 million. The preliminary planning indicated up to \$150 million to be allocated to "Enterprise Development", much of it in the form of credit. Because of the involvement of a broad range of GOE Ministries unfamiliar with the basic precepts of successful small enterprise lending, it was feared that large amounts of poorly supervised and under-priced credit might become available which would have a negative effect on the projects that USAID/Cairo had carefully nurtured.

Although there were delays in getting the SEC project fully negotiated so that cooperative grant agreements could be issued, the Social Fund encountered its own delays in becoming operational. The project paper was authorized in April 1991, and the grant agreement was signed by the MIC in September 1991. A contract with Agricultural Cooperatives Development International, which had provided services under the RSSE project, was signed in April 1992. It is expected that the cooperative grant agreement with the NBD will be signed in June 1992.

The project is designed to work through the NBD, utilizing twelve to fifteen branches in the metropolitan governorates of Cairo, Giza, and Kalyubiya. Each of these branches will serve as the "home base" for approximately nine loan officers and six to seven support staff. The loan officers will reach out to the borrowers, with most loan transactions and supervision taking place in the borrowers' residence or place of business. Market interest rates are to be utilized, and savings services to be offered to the borrowers.

OBSERVATIONS

The project is becoming operational as this report is being finalized. The persons responsible for implementation will face a number of challenges, but have an excellent opportunity for success. The expatriate advisors are both experienced in Egypt, and the

⁶ Technical Assessment: Rural Small-Scale Enterprise Pilot Credit Activity in Egypt, GEMINI Technical Report No. 5, John Gardner and Jack Proctor, November 1990.

NBD has the experience of the RSSE project from which they can base their further development. However, the project is designed to hire up to 350 new staff, get them trained in a relatively short period of time, and to get loan funds flowing to the end-use borrowers within a few months of the beginning of project implementation. This will demand a strong degree of cooperation among the technical assistance contractors, the National Bank for Development, and USAID/Cairo. The commitment voiced by NBD's Chairman and the National Project Manager will have to be passed on to the large number of staff that will implement the project.

CREDIT GUARANTEE CORPORATION

BACKGROUND

The Credit Guarantee Corporation had a long development phase, but may be emerging as one of the most effective institutions in Egypt in helping deliver formal finance to small businesses in Egypt. Technical assistance was provided through the Private Enterprise Credit Project (263-0201.3). Although some preliminary work was carried out in 1987, basically desk research on guarantee systems in other countries, effective development of the CGC began in late 1988. Technical assistance to project development was provided through a core grant buy-in with the US-based firm of National Cooperative Business Association (NCBA) and the local firm of Arab International Consultants (ARICON), along with the services of this consultant.

The primary idea behind the development of the CGC is to provide a guarantee on a portion of loans made to small businesses, primarily those requiring loans in the LE 20,000 to LE 1,500,000 range, which will expand a given business's capability to borrow with the same amount of collateral. Following formal incorporation of the CGC and initial extension of guarantees to small enterprises, the Corporation was modified somewhat to provide guarantees to private health practitioners.

PROJECT DEVELOPMENT

The CGC had a long gestation period. Like the projects described above, it was (and is) unique in Egypt. The idea of using a guarantee mechanism to reduce the collateral required by local banks, and to share the loan risk with a guarantor, is not new. However, that fact that it had not existed in Egypt, and that the CGC was set-up as a private corporation, made development of the CGC a rather arduous task. In order to attract funds and support, paid-up capital was attracted from nine banks and one insurance company. The original charter had to be written, discussed with the shareholders, and amended as needed. Headquarters had to be identified and equipped, the participating banks had to be accredited, and bank chairman, managers, and credit officers were trained over a three year period. Approximately 2,200 bank employees were trained.

The same period of time also involved the development and installation of a management information system, the development of manuals of operations, and the identification of staff. Continuous negotiations with various members of the Government of Egypt and the Central Bank had to be pursued, but it finally resulted in the formal incorporation of the CGC in December of 1989. The subsequent year was primarily devoted to operationalizing the CGC, and obtaining the agreed upon loan from the Special Account.

The funding of the CGC at present comes from the paid-up capital, the first tranche of LE 20 million from the Special Account in the form of a long term, soft loan (50 years at 4% per annum with a ten year grace for the first principal repayment), and another LE 32,000,000 from the Cost Recovery for Health Project (263-0170).

The CGC began its guarantees for small scale enterprises in January 1991, about one month before the IMF came to agreement with the GOE to impose credit ceilings on local banks. Despite this limitation, the CGC has seen rapid expansion following a difficult start up period. A table at the end of this report shows guarantee issuance to date and shows an indication of that growth over the first seventeen months of operation.

OBSERVATIONS

Although it is difficult to quantify, many of the problems in setting up the CGC were directly related to the GOE's unfamiliarity in working with the private sector. There was resistance on the part of the Ministry of Finance to approve CGC as a corporate entity, and the organizers of the CGC had a difficult time finding their way through the labyrinth of Egyptian laws regarding establishment of a private, for-profit corporation. However, the CGC has attracted some of the best talent available from the banking sector. This is true both of top management and the recently-hired staff.

One of the most useful activities carried out recently was the formation of a corporate budget and planning exercise. The CGC should be encouraged to repeat this planning exercise near the end of each calendar year. It will be sometime before they can become very accurate with their budget planning and targeting because they are currently in a period of very rapid growth. However, it is during this dynamic period that they must pay close attention to the amount of guarantees they can "afford" to back, as well as how soon they can have sufficient resources to expand their staff.

GEMINI PROJECT

This consultant was requested by the Office of Finance and Investment to comment on the availability of short-term technical assistance following the period of this consultancy. As is noted in this report, the Cairo Mission has utilized the services of the Growth and Equity through Microenterprise Investments and Institutions (GEMINI) project on a number of occasions, particularly for the Weidemann report, Egyptian Women and Microenterprise: The Invisible Entrepreneurs, the Stearns Mid-Term Evaluation Small and Micro Enterprise

Development Project, and most recently on the Angell/Porges Analysis of Funding Mechanisms for Small and Micro Enterprise Development Project.

The GEMINI project has a wealth of technical services that it can obtain. The key contact, one that we may have over-utilized but have certainly appreciated, is through Ms. Elisabeth Rhyne, PRE/SMIE, Phone Number (202) 647-2727, Fax Number (202) 647-1805. Ms. Rhyne has been an outstanding manager of the GEMINI project from the AID side, and has continually been able to either find a way to contract specific personnel that we have requested, or been able to identify people that would serve our purposes. Many of the times The GEMINI project will still be active through 1994, and it is the sincere wish of many of us in the field to see that type of centrally-funded project to continue to be available.

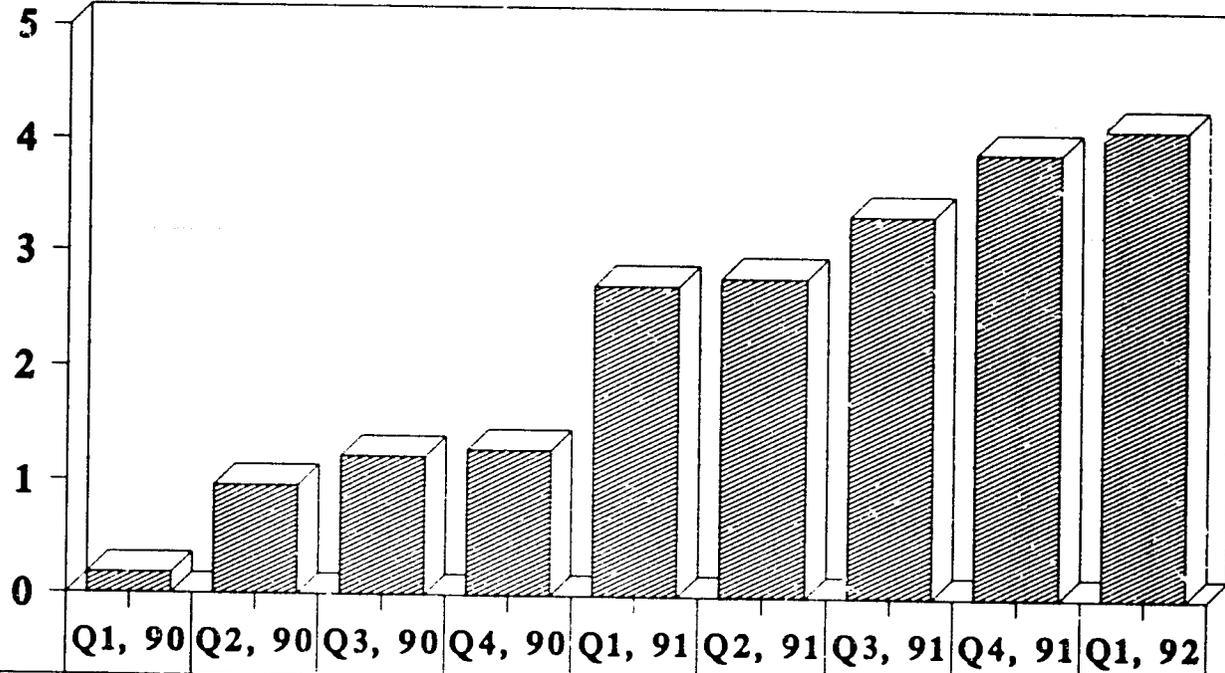
SUMMARY

The USAID Mission in Cairo has made great strides over the past four years in developing the initial models for a successful microenterprise program. The "Foundation approach being utilized under the Small and Micro Enterprise Project has achieved success in initiating lending in a responsible manner, and has given private sector supported activities a very positive reputation with the GOE. The Credit Guarantee Corporation is emerging as the next rung on the ladder for people who might normally be excluded from the amounts of credit from formal financial institutions that they require. The National Bank for Development, under the pilot RSSE project and the current Small Enterprise Credit project has the chance to be the first bank in Egypt to provide credit directly to micro and small enterprises. The success of these projects will continue to hinge, at least in the near future, on the clear cooperation of AID and other donors working in partnership with the types of Egyptians that have shown what their commitment and dedication can achieve.

SMALL AND MICRO ENTERPRISE PROJECT

Loan Issuance Growth (CY 90-92)

LE Millions



	Q1, 90	Q2, 90	Q3, 90	Q4, 90	Q1, 91	Q2, 91	Q3, 91	Q4, 91	Q1, 92
Quarterly Total	0.185	0.96	1.225	1.29	2.725	2.802	3.349	3.913	4.132

ABA & ESED

Quarterly Total

GUARANTEE ISSUANCE for CREDIT GUARANTEE CORPORATION

Period	Small Scale Enterprises			Health Practioners			TOTAL		
	Credit	Guarantees	No.	Credit	Guarantees	No.	Credit	Guarantees	No.
Jan - Dec 91	13,108,558	5,837,755	92	1,252,000	884,500	26	14,360,558	6,722,255	118
Jan - May 92	21,042,558	10,328,991	176	10,431,690	7,183,152	208	31,474,248	17,512,143	384
TOTAL	34,151,116	16,166,746	268	11,683,690	8,067,652	234	45,834,806	24,234,398	502

Guarantee Issuance
Jan 91 to May 92

