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Capital Markets Assessment Egypt

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ACRONYMS

AIMR	Association for Investment Management and Research (U.S.)
ANNA	Association of National Numbering Agencies
AUC	American University of Cairo
CACE	Center for Adult; and Continuing Education (division of AUC)
CAOA	Central Agency for Organization and Administration
CASE	Cairo and Alexandria Stock Exchange
CBE	Central Bank of Egypt
CMA	Central Market Authority
CMD	Capital Markets Development project
CML	Capital Markets Law
CRS	Central Registry Service
DT2	Development Training Two project
EAS	Egyptian Accounting Standards
EU	European Union
EBDA	Egyptian Bond Dealers Association
ECMA	Egyptian Capital Markets Association
EIMA	Egyptian Investment Management Association
EIPS	Egyptian Investment Performance Standards
GDR	Global Depository Receipt
GIPS	Global Investment Performance Standards
GOE	Government of Egypt
IAS	International Accounting Standards
IOSCO	International Organization of Securities Commissions
IPF	Investor Protection Fund
IPO	Initial Public Offering
ISA	International Standards of Auditing
IT	Information Technology
MOFT	Ministry of Foreign Trade
MOF	Ministry of Finance
MCSD	Misr for Clearing, Settlement, and Depository
NASD	National Association of Securities Dealers (U.S.)
OST	Observational Study Tour
SGF	Settlement Guarantee Fund
SLB	Securities lending and borrowing service
SRO	Self-regulatory organization
UAS	Unified Accounting Standards
US	United States
USAID	United States Agency for International Development

EXECUTIVE SUMMARY

1. Introduction

A four-person team evaluated the Capital Markets Development Project. Following the Scope of Work, the team assessed:

- The main deliverables of the contractor over the nearly four years of the project;
- Training programs with the five Institutional Partners;
- Levels of satisfaction among the Institutional Partners; and
- Public awareness programs.

The team also has made recommendations about potential future work for the Project and the desirability of additional USAID projects in the financial services industry.

Over 50 project participants, private sector leaders, and other government officials were interviewed, dozens of project reports were reviewed, and training and information technology activities observed during the four-week in-country evaluation. At the close of the fieldwork, debriefings were held with the client, USAID, the Project staff, and the leaders of each of the Institutional Partners.

The team found that the contractor, Chemonics Inc. has done excellent work considering the complexity of the Project and the constraints of the environment. The team finds that the contractor's work is of sufficiently high quality that they should be considered for additional work in this field in Egypt. Moreover, the team feels that USAID's assistance to this sector should continue beyond the next year, but ought to be broadened to include the financial services industry, not just capital markets.

2. Legal and Regulatory Reform

The team found that the assistance that the contractor provided for legal and regulatory reform was excellent and appreciated by the Institutional Partners. The fairness, openness and transparency of Egypt's capital markets have improved as a result of the Project's legal and regulatory effort. However, the technical assistance given to the Cairo & Alexandria Stock Exchange (CASE) in their efforts to improve Board membership and listing rules was not up to the high standards of work done for other Institutional Partners.

Much remains to be done in assistance in legal and regulatory reform. The closure of the capital markets for over 30 years in Egypt has eroded their infrastructure. It will take significant additional work to bring Egypt to a completely fair, open, and transparent market. Since the Project has demonstrated that it is capable of first class work in legal and regulatory reform and because it has earned the trust and respect of its Institutional Partners, the Project is positioned to perform additional work that will assist in the transformation of the Egyptian capital markets. The evaluation team believes that there are several additional areas in legal and regulatory reform that should be the focus of attention for USAID. The top priority areas are:

- Licensing and regulation of salespersons for brokerage firms;

- SRO status for MCSD, CASE, ECMA, and EIMA;
- Margin, short sales, securities lending, and net capital rules; and
- Institutional strengthening for CMA, MCSD, and CASE legal departments.

Other areas for additional work include provision of technical assistance to:

- Establishing the Investor Protection Fund;
- Creating new financial instruments;
- Reconciling domestic accounting standards with Internationally Accounting Standards;
- Restructuring the ownership and organization of CASE; and
- Reform of bankruptcy law.

3. Automation and Information Technology

The evaluation team also reviewed the automation and information technology assistance given to five Institutional Partners. For the Cairo & Alexandria Stock Exchange (CASE), the Project provided workstations and servers to increase the capacity of processing trades. However, the Project will probably not be asked to provide needed technical assistance in disaster recovery planning for reasons outside of its control. CASE, like the other Institutional Partners, would also benefit from technical assistance in strategic planning of information technology applications.

The CMD provided book-entry software, technical assistance, and training in the processing of Treasury Bills to the Central Bank of Egypt (CBE). However, additional work is needed to accomplish the same for Treasury Bonds. The Delivery versus Payment (DVP) vulnerabilities of the book-entry system seem to be well understood by the Central Bank staff. However, considering the time lag between trade and settlement and the fact that the participants' clearing accounts reside on a separate computer system in a different department, it will be prudent to review all manual and automated procedures in the settlement cycle to ensure Delivery-Versus-Payment.

For the Misr for Clearing and Settlement Depository (MCSD), the Project provided hardware, training, and technical assistance in the establishment of the network management systems and the firewall security system. Like CASE, the MCSD is financially self-sufficient and is able to acquire technology based on technical and business decisions unencumbered by the strict USAID procurement regulations to which the CMD project is subject. The specific issues that gave rise to MCSD dissatisfaction with the Project appear to be mostly a matter of configuration settings and fine-tuning of complex software components from different vendors. It was also clear that MCSD has strong preferences as to the local service providers, ample financial resources and little patience with what they perceive as substandard services. This partiality is understandable in private sector organizations, but it imposes serious constraints on the CMD project's ability to assist the MCSD in the IT area. The CMD project may be of greater assistance in the provision of expert IT consulting services than in the procurement of hardware and off-the-shelf software.

Even though the Project has invested in numerous interventions and continuous support, the Central Markets Authority's (CMA) capabilities in information technology remain institutionally weak. There is, in fact, a high risk that the various IT investments made in the CMA may yield a

very low return given the institution's inability to attract and retain competent IT personnel. The inadequate civil service salary structure is the source of this problem. The Project has provided hardware for the firewall and surveillance systems and for the document archiving system, as well as training and technical assistance to enable these systems and others. The evaluation team recommends increased technical training of CMA staff and exploration of alternative compensation schemes to attract and retain competent IT staff.

The Egyptian Central Markets Association (ECMA) also received well-regarded but limited assistance in the development of a membership database and a tracking system and the procurement of hardware and software for basic office automation.

4. New Financial Instruments

The introduction of new financial instruments has been the least successful of all of the Project's activities. Most of the effort to date has been in the preparation of thoughtful reports about possible new financial instruments. Delaying attention to this issue until the latter stages of the project made sense in many respects, since improvement in market structure and institutions should have had the highest priority. One outcome of the project's work at the Central Bank is the new recognition of Treasury Bills with 15-day maturities as cash in the calculations of bank reserves.

The evaluation team recommends that new product proposals and technical assistance should be more grounded in the realities of the Egyptian legal and financial systems than has been the case so far. The CMD project can play an important role as honest broker between the private sector and its creative ideas and the CMA's regulatory methods.

5. Public Outreach

Several of the Institutional Partners have initiated public outreach programs supported by the Project. One of the most successful has been the training and orientation of print and broadcast journalists in the basics of economic and financial reporting. The Press Forums, sponsored by the CMA and the Project, have included the equivalent of classes in fundamental issues of the capital markets as well as exposure to national political figures and international experts discussing topical issues. The Observational Study Tours have had a profound impact on the participant-journalists.

The short-term Hill and Knowlton consultant's report should become a starting point for talking with the Institutional Partners about public communication programs. An important element of any such programs, which has not been included to date, is the testing of materials with the target audiences before production. In addition, public communication strategies should keep in mind the size and other characteristics of the target audiences before beginning the design and production of materials.

Another element of a communication program for the capital markets is communications to the brokerage industry, especially the sales force. As a result of laws and decrees soon to be enacted, the brokerage industry will undergo profound changes. This will be an opportunity through

communication and training to professionalize the sales force and improve standards for compliance in many areas.

6. Training

Finally, the evaluation team reviewed training activities and outcomes in most of the Institutional Partners. With few exceptions, these interventions were welcomed by the Institutional Partners. The CMD has provided more than 60,000 person hours of formal training spread among all the Institutional Partners and the private sector. There also have been countless hours of on the job training. This has had a profound effect on some of the institutions such as the CMA where the need for training is the greatest, much less so on the CASE where the staff is better educated. Most of the formal training was managed by DT2, a USAID contractor. This arrangement has produced mixed reviews because of its inflexibility and sometimes "customer unfriendly" style, but it has freed the CMD staff for other matters.

One of the best examples of formal and on-the-job training has been the training of the surveillance section of the CMA. The Chairman of the CMA had indicated from the outset of the Project that strengthening market surveillance was a high priority for his agency. The Project assisted the CMA is building out office space for the surveillance unit and in acquiring monitors for the staff. More importantly, the Project funded an Observational Study Tour to the United States for the purposes of training and motivating the surveillance team. In an unusual strategy, the counterpart staff from the CASE also participated in the OST. For both groups this was the first time that they worked together.

Informal and on-the-job-training for the CMA continued when the staff returned to Cairo. The surveillance staff members also participate in brokerage firm inspections. The evaluation team observed the group at their work place and interviewed them individually. They are informed and enthusiastic. The section supervisor told the evaluation team that cases brought of unusual trading activity noted by the staff had increased about 50% since the training had been completed.

The evaluation team recommends that training remain a central component of the Project's continuing work in capital markets. English language training should continue to be an important element of the training design. It is the language of international finance and it is essential if the trainees are to take advantage of overseas study opportunities. The evaluation team felt that this is particularly important for CMA staff.

INTRODUCTION

1. Background and Description of the Project

Egypt has had stock and commodities markets for more than a century, but they had been moribund throughout the period of nationalization – from 1959 to early 1990's. Less than thirty shareholder-owned firms and only a handful of stockbrokers survived this era. However, with the economic reforms of 1992 and global interest in markets (particularly in developing markets), the Egyptian stock market began a period of increasing volume and activity. This was bolstered by the privatization of several formerly state owned corporations. While these developments stimulated market growth, they also threatened market gridlock, rampant speculation, and opportunities for market irregularities, corruption, and criminal activity.

As reported in the USAID/Egypt Results Package, dated 1997, several areas lent themselves to intervention by outside technical assistance, training, and information technology procurements. In the first place, the Capital Markets Authority, which had been given authority to regulate the markets in ways similar to the US Securities and Exchange Commission, lacked trained staff. Moreover, the rules and regulations that would facilitate oversight and enforcement were largely absent. Information management systems were inappropriate to the task. Corporate disclosure was spotty and incomplete and, as well, clearing and settlement of transactions was cumbersome, sometimes taking 15 days.¹

In the second place, a corporate and government bond market scarcely existed. If investors were to have the opportunity to diversify their investments, debt instruments needed to be available for the retail markets. Corporate borrowers also needed to wean themselves from the bank lenders whose inclinations were to lend short-term for long-term projects.

Thirdly, the brokerage industry was characterized by only a few companies with professional staff and adequate financing. The professional organization of the brokerage industry, the Egyptian Capital Markets Association, was poorly financed, lacked SRO status, and did not provide any self-regulation nor training for members.

The fourth point is that the Cairo and Alexandria Stock Market needed information systems upgrades and staff training. With its own resources the CASE was acquiring a more modern software package which would enable it to handle increased trading volume, but hardware, (including workstations) were antiquated. While the education and technical training of the CASE staff was of a generally high caliber, additional training was needed to handle the anticipated trading and listing activities. Moreover, the stock exchange needed improved listing and membership rules and other elements of a Self-Regulatory Organization.

Finally, financial page journalists for the leading newspapers and magazines as well as televisions journalists and presenters had limited knowledge of the stock market and other financial and economic issues. The public was largely uninformed about investing.

¹ The current international standard for settlement is T + 3 or trade date plus three business days.

There were already assistance efforts through agreements with U.S. Department of Treasury and the Securities Exchange Commission for some training and technical assistance. The European Union had also been providing technical assistance. However, a more systematic approach, involving all of the major market participants, was called for if the Egyptian markets were to continue to attract domestic and foreign investors and if they were to become an engine for capital formation and allocation of resources.

In August 1998 a contract was signed with Chemonics, Inc. to provide this systems-wide approach. It has had the following objectives: "(a) improved efficiency, transparency and stability of the capital market's architecture (including automated trading, clearing and settlement systems for the stock and bond and money markets); (b) strengthened institutions, including partner organizations such as the Capital Markets Authority (CMA), the Egyptian Stock Exchange (ESE) (sic.); the Egyptian Capital Markets Association (ECMA), the Misr Clear, Settling and Depository Corporation (MCSD), the Central Bank of Egypt (CBE), and the brokerage industry; (c) a strengthened regulatory environment for the capital markets, including greater self-regulation and improved disclosure; and (d) the development of secondary trading in new financial instruments, particularly money and bond market instruments."²

By September 1998, Chemonics had staff in Cairo. By the end of the year, the contractor had prepared a work plan with Egyptian Institutional Partners, and a professional staff of eight expatriots and 12 Egyptians was in place. The contract made clear that the much of the assistance was to be demand driven and that the approach was to be flexible. Nearly all training was to be coordinated through DT2. The contract between Chemonics, Inc. and USAID/Egypt expired in August 2001 and was extended for one year. USAID/Egypt is contemplating an additional extension to the summer of 2003.

2. Evaluation Objectives

The purpose of this evaluation is to assess the performance of the technical assistance contractor with regard to the contractor's contribution to five components of the project: (1) legal and regulatory reform; (2) automation upgrading; (3) institutional development; (4) public outreach; and (5) introducing new financial instruments. In this regard, the evaluation assesses the quality of the deliverables of the contractor. These products, which range from comments on draft laws and decrees to technical assistance and procurement of equipment for information technology in several agencies are reviewed in this evaluation report.

In addition, this evaluation reviews training programs with each of the institutional partners and the public awareness programs conducted by the Institutional Partners with assistance from the contractor. The evaluation team also assesses the overall satisfaction of the Institutional Partners with the Project's work. Finally, this report identifies areas in the Egyptian capital markets that may require additional assistance and provides recommendations.

² Section C, Description/Specifications/Work Statement, paragraph C. 1, Contract No. 263-C-00-98-00067-00.)
MANAGEMENT SYSTEMS INTERNATIONAL
MSI Project 4314-001

3. Evaluation Approach and Methodology

The Chemonics technical assistance, training, and commodity procurement Capital Markets Development project (known throughout this report as the Project or CMD) has worked with six Institutional Partners, has produced nearly two dozen “deliverables” over the course of nearly four years, many other reports by staff and short term consultants, and by the contractor’s own count provided more than 60,000 person hours of formal technical training. Countless hours of on-the-job training have also been supplied. The four-member evaluation team reviewed reports produced by the contractor, by the Institutional Partners and related organizations. Interviews were held with Project personnel, senior officials and staff of Institutional Partners including trainees, and other organizations in the capital markets. Training was observed, and information and automation technology was observed in operation.³ With each respondent, the evaluators inquired about the need for additional outside assistance over the next few years.

The evaluation team consisted of three US professionals: a securities lawyer, experienced in market operations and regulations; an information technology specialist, experienced in market and banking automation; and a securities specialist, experienced in marketing, market operations, training and communications. The team was joined by an Egyptian professional experienced in Egyptian privatization efforts and market operations.

Evaluation team members drew upon their own expertise to address elements of each task in the Evaluation Statement of Work. This report is organized according to the major goals of the project: legal and regulatory reforms; automation upgrading; introduction of new financial instruments; and public outreach.

This evaluation does not attempt to assess all of the activities of the contractor. After nearly four years the output of the contractor’s staff and the influence that it has had in many of the Institutional Partners have been substantial. The evaluation team selected the most significant elements of the contractor’s work, including those specifically mentioned in the evaluation scope of work.

4. Methodology for Evaluation of Training Programs

Over the course of the Project hundreds have been trained in a wide variety of courses, including Observation Study Tours to the United States and elsewhere. The project has estimated that over 45,000 person hours of DT2 technical training, 19,000 of non-DT2 technical training, and 25,000 hours of English language have been offered. Even more on the job training has been provided. Since the total professional staff of the CMA and relevant sections of other Institutional Partners does not exceed 1000, certainly many of the staff participated in multiple training activities. Training hours per staff member were not collected by the Project. Nevertheless, for several of those interviewed, the language and professional training was described as “life changing.”

Given the breadth of the training, the evaluation focused on two training efforts: training of journalists from local newspapers and the press relations staff in some Institutional Partners, and

³ Appendix A: Information Sources for the Evaluation.

the training of the surveillance staff of the CMA. An evaluator interviewed six participants from each group using an open-ended interview method, probing for strengths and weaknesses of the training and the impact that the respondent perceived in his or her job performance as a result of the training. In addition, the evaluator sought reactions of others to the changes in job performance by trainees of these two groups.

In addition to these interviews, all evaluators of the information technology and legal and regulatory activities inquired about staff experience with formal and informal training. Thus, the evaluation gained impressions about the effectiveness and relevance of training from each of the Institutional Partners. Finally, the evaluation team reviewed the annual training plans and needs assessments prepared by Chemonics staff or DT2 staff and reviewed selected evaluations of training by the DT2 staff.

5. Methodology for Evaluation of Public Outreach Programs

Public outreach programs in the CMA, MCS D, ECMA, and CASE were evaluated through review of reports provided by the CMD either in the CD-ROM or in hard copy after the team arrived in Cairo. In addition, translations of communication materials such as brochures and video programs were examined. Interviews with the public affairs staff of CMA, MCS D, ECMA, and CASE were conducted. One of the most important and effective outreach programs has been the training of journalists, which is discussed above in the section of evaluation of training.

6. Methodology for Evaluation of Legal and Regulatory Reform

The project's activities in legal and regulatory reform were examined using the following methods:

- Review and analysis of all written documents (laws, regulations, commentaries, research reports, manuals, training materials, etc.) generated by the Project;
- Review and analysis of selected additional documents, particularly the Capital Markets Law 95 of 1992 and its Executive Regulations and the CASE Monthly bulletin;
- Interviews with key Project staff concerning their activities in the field of legal and regulatory reform; and
- Interviews with key personnel at the Project's Institutional Partners (CMA, CBE, MOF, MCS D, CASE, ECMA, and EIMA) to discuss their interaction with Project staff and their assessment of the scope and quality of the Project's work.

7. Methodology for Evaluation of Information Technology and Automation Programs

The information technology component of the CMD project evaluation focused on the review of major IT-related activities with the following institutional partners: CMA, CASE, MCS D, CBE and ECMA which are primary beneficiaries of the Project's IT budget.⁴

⁴ Appendix ____ Other Institutional Partners such as EIMA, MOFT, and MOF did not receive significant IT input.

The evaluation methodology included: (a) review of the IT sections of the CMD reports delivered by Chemonics on CD and delivered in hard copy during the mission in Cairo; (b) review of the contractor's yearly work plans and quarterly progress reports; (c) interviews with IP staff responsible for the implementation of the IT components in each institution; (d) review of the functionality of the information systems provided by the CMD project through demonstrations at the CBE (book-entry systems) and the CMA (document archiving system); (e) site visits to assess suitability and usefulness of equipment and off-the-shelf software procured under the project at CASE, CMA, MCSD, and CBE; and (f) occasional follow-up interviews to clarify any inconsistencies that may have surfaced during the course of the evaluation.

8. Major Conclusions and Findings

Within four months after contract signing in 1998, the contractor had 20 professional staff, a work plan developed with the Institutional Partners, and programs underway. This intensity and dedication has been sustained until the present. The project began and continues to work on a numerous fronts simultaneously, addressing long-term and short-term objectives. The CMD began work with five Institutional Partners, each with several major objectives and numerous sustained activities. The evaluation team finds that professionalism, determination and ingenuity have characterized the contractor's work. The contractor has done an excellent job in designing and executing the project.

The Project has made substantial contributions to: (a) improved efficiency, transparency, and stability of the capital market's architecture; (b) strengthened institutions, including partner organizations such as CMA, and others, and (c) a strengthened regulatory environment...." Relatively little progress has been made in "(d) the development of secondary trading in new financial instruments."⁵

Hardware procurements, training and technical assistance have made important contributions to the operations of CASE and MCSD. However, these financially independent organizations need rely much less on outside assistance than does the CMA, ECMA, and CBE. CMA in particular continues to need staff training in many areas.

This has been a difficult environment in which to work. The contractor has had no control over constraints such as a broad recession, a stalled privatization program, and a falling stock market. Other constraints, such as strong-willed personalities at the main Institutional Partners, present special challenges. Another constraint was that the formal training budget and program have under the control of the DT2 whose cumbersome regulations limited the flexibility of the Project. On the other hand it did free up Project staff for other tasks. A demoralized brokerage community, smarting from charges of corruption from the government and of incompetence from the investing public, has been a difficult partner on this contract.

⁵ Contract No. 263-C-00-98-00067-00, Section C Description/Specifications/Work Statement, paragraph C.1 "Objectives."

One of the constraints that the evaluation team identified is the lack of qualified IT professionals to receive technical and hardware assistance. This is particularly true in the CMA. CMD training programs have begun to address this need, but government personnel policies limit long-term impact. Work is just beginning with the ECMA in strengthening this important institution.

LEGAL AND REGULATORY REFORM

1. Findings and Analysis of Major Project Activities and Deliverables

The Project's activities in the legal and regulatory area were examined using the following methodology:

- Review and analysis of all written documents (laws, regulations, commentaries, research reports, manuals, training materials, etc.) generated by the Project;
- Review and analysis of selected additional documents, particularly the Capital Markets Law 95 of 1992 and its Executive Regulations, CASE annual yearbook and monthly bulletin, etc.;
- Interviews with key Project staff concerning their activities in the field of legal and regulatory reform; and
- Interviews with key personnel at the Project's IPs (CMA, CBE, MOF, MCSD, CASE, ECMA and EIMA) to discuss their interaction with Project staff and their assessment of the scope and quality of the Project's work.

All documents reviewed and persons interviewed are listed in Appendix A to this report. This section of the MSI Evaluation Team's report is organized by IP as the most logical structure. Some legal and regulatory issues (*i.e.* bankruptcy law reform) cut across IP boundaries as discussed below.

In general, the Project has done an excellent job in assisting its IPs with a very few exceptions as noted below.

2. Misr For Clearing, Settlement And Central Depository

The Project played an active role in the strengthening of MCSD. Legal and regulatory assistance was rendered in the areas of:

- Creation and implementation of the SGF to protect investors from their brokers' failure to complete settlement of securities transactions in a timely fashion;
- Commenting on Law 93 (on central securities depository and registry) which was drafted by other foreign experts and drafting the executive regulations under that law;
- Reorganizing the corporate structure and recapitalizing MCSD;
- Drafting a standard form contract between MCSD and its users; and
- Conducting legal training seminars on bankruptcy and negotiable securities for MCSD and other participants in the capital markets invited by MCSD.

MCSD has been a very successful IP in the Egyptian capital markets. It is generally well-regarded by the other participants in the securities markets and has developed some innovative services, such as automatic and free notification to individual investors by e-mail, mobile telephone, or fax whenever shares are bought for or sold from their accounts. The Project's efforts have contributed materially to MCSD's success and received praise from Mr. Reda Farahat, head of MCSD's 12-member legal department.

The implementation of the SGF has demonstrably reduced the risks faced by investors and has been a remarkable success. The number and value of transactions for which securities or cash were not delivered or were delayed dropped a remarkable 60% to 70% in 1999-2000. Only 8 brokers (5% of SGF members) had to draw on the SGF in 2000 and only 0.10% of all transactions by number (.01% by value) had to be covered by the SGF.⁶

3. Egyptian Capital Market Association

Founded only six years ago, ECMA has grown to approximately 200 members, primarily brokerage firms but also including banks, insurance companies, lawyers, accountants and others with an interest in the Egyptian capital markets. The Project has provided significant assistance to ECMA in advising it on transition to SRO status, development of membership criteria, and internal structure and governance of the organization as an SRO. The Project has also assisted ECMA in developing an excellent Code of Ethics and Rules of Professional Conduct for its members.

4. Egyptian Investment Management Association

As with ECMA, the Project has also advised EIMA on its membership structure and criteria for membership. The Project also rendered significant and valuable assistance to EIMA, with the assistance of a short-term expert from AIMR, in constructing an Egyptian Performance Standard (EPS) for members of the investing public to use in evaluating the past performance claims of portfolio managers. A uniform national standard enables prospective investors to make intelligent comparisons among the competing claims of investment management success made by portfolio managers. The initiative for development of EPS came from EIMA and its members. AIMR approves performance management standards for each country, which must be consistent with AIMR's global performance standards, and has now done so in Egypt in consultation with EIMA and the assistance of the Project. After lengthy discussion and several meetings, the resulting EPS were approved by EIMA's members. EIMA has now submitted them to the CMA with the request that CMA adopt them by regulation as the only performance standards allowed to be used in advertisements and promotional literature issued by portfolio managers in Egypt.

Development of EPS in this fashion is a classic example of exactly how an SRO is supposed to work in conjunction with industry experts and its regulators, a new concept in Egypt. The Project deserves great credit for having contributed to this accomplishment.

5. Capital Market Authority

Comments on draft new capital market law. One set of (undated) comments on this new draft law prepared by the Project and attached to it are more a summary of the law than a commentary on it. With a few exceptions, the "Commentary" simply summarizes the provisions of the new law without contrasting them with either prior Egyptian law or the laws of other jurisdictions, and without coming to any conclusions on the merits of the new law. As such, the "Commentary" is of little utility.

⁶ CMA 2000 Annual Report pp. 14-15

On the other hand, the Project's other paper, "Comments, Questions, and Proposals on the New Draft Capital Market Law" (March 2001) is an extremely good, thoughtful and detailed analysis of the new law. It contains specific recommendations for amendments to various provisions of the new law and a discussion of the rationale for each recommendation.

CMA Annual Reports. There has been a very noticeable improvement in both the quality and quantity of information published in the CMA's annual reports for 1998, 1999 and 2000 (the last year available), not to mention the appearance and reader appeal of the report over that period. Publication of Annexes C and D (detailed checklists used by the CMA to verify reporting companies' disclosure and the CMA's inspection guidelines for brokerage and portfolio management firms) in the 2000 Annual Report was particularly helpful and should encourage investor confidence. These improvements were largely attributable to the Project's efforts, and that the CMA will now be able to maintain this level of quality in future years. This is a significant accomplishment.

Surveillance and Investigation. Interviews of senior and junior CMA surveillance personnel and the CMA's legal department found that they had had a very positive experience with the Project's efforts in this area. They singled out the Surveillance Manual and accompanying checklists, prepared and translated into Arabic by the Project, and the study tour of the US for particular praise. The number of cases the Surveillance Department investigated and resolved had increased 40% to 60% during the last 5 years, and the CMA staff attributed the increase largely to the Project's efforts.

The Surveillance Manual prepared by the Project is excellent. It received very favorable comments from the CMA surveillance staff. A minor flaw is that it relies heavily on US legal cases, principles, and authorities, although this is perhaps understandable in light of the fact that there is no established body of Egyptian statute or case law dealing with insider trading, front-running, market manipulation, and similar securities law issues. It would have been much more helpful had it been drafted after surveying current practices, procedures, and problems in Egypt. The Manual contains a thorough explanation of what constitutes a suspicious transaction and how to investigate the different types of suspicious transactions fully and prepare reports on the investigation. While thorough, it is written in a clear and readily understandable style and has been put into practical use by the CMA staff. The Manual represents excellent and well-received work by the Project.

The evaluation team observed the surveillance staff in operation in their project-built offices. Using computer terminals supplied by the CMD, the staff visually follow stocks during the day to detect variations in trading that would suggest trading violations. They seemed knowledgeable and enthusiastic about their work. They communicate with their counterparts in CASE.

The evaluation team also observed a training session of the CMA staff that conducts brokerage firm inspections as part of their jobs. The men of the surveillance staff also participate in inspections. (Women are not allowed to participate in inspections because of the likelihood of keeping late hours that would appear to compromise the women.)

The training was conducted by a CMD short-term consultant. Its shortcomings underscored the evaluation team's recommendations in a number of areas: thoroughly ground the training and

training manuals in the Egyptian realities; bring the consultants to Egypt in plenty of time to allow orientation. Even though language is a serious barrier, use local examples of inspection reports, forms, etc. to illustrate the points of the presentation.

Settlement Guarantee Fund. See discussion under MCSD.

Self-Regulating Organizations. See discussions under MCSD, ECMA and EIMA.

Rules on Margin, Short Sales, Securities Lending And Borrowing, and Net Capital. These rules are at a preliminary stage and were just turned over in final form by the Project to the CMA during the first quarter of 2002. They are of good quality. As these rules contain several concepts which are completely new and unfamiliar to the IPs, substantial training will be required to put them into practice and to inspect the brokerage firms and other IPs to ensure full compliance with them.

Miscellaneous Rules. In 2001 the Project delivered a set of draft rules on eight miscellaneous subjects (venture capital, underwriting, rulemaking, securitization, etc.) to the CMA. These rules vary in quality - for example, the venture capital rules and the rules on rulemaking are quite good, but the rules on securitization are poorly thought out and unduly restrictive. The CMA does not appear to have done anything with them since they were delivered.

Investor Protection Fund. The IPF will protect investors from the risk of loss of their cash or securities held by their brokers due to the broker's bankruptcy. (The IPF will supplement the existing protection against settlement failure provided by the SGF). The Project has done significant work on the creation of the IPF and has clearly articulated what risks the IPF will and will not cover in its "Draft Decree for the Creation of an Investor Protection Fund" (March 2002) and its earlier study, "The Elements of an Investor Protection Fund in Egypt" (October 2000). Both are of excellent quality. The 2000 "Elements" study is noteworthy for having included non-US perspectives on this issue by examining not only the US-based SIPC but also its UK and Canadian equivalents, lending a very helpful international and comparative dimension to the analysis and discussion which was not found in other Project deliverables.

The Project is actively pursuing implementation of the IPF by the CMA at the time of this report. The draft decree for the formation of the IPF was delivered by the Project during the first quarter of 2002.

Training Judges and Prosecutors. The CMA must work very closely with prosecutors and judges to enforce the Capital Market Law. It has found the Project's prior and current training of prosecutors and judges very valuable and expressed the hope that this effort would continue. Prior to the Project's training, the CMA found it difficult to work effectively with judges and prosecutors who had little or no familiarity with securities law concepts. The Chairman of the CMA and the head of its legal department stated that the Project's efforts in this area were already beginning to pay significant dividends and very much hoped this training would continue. See the discussion under "Recommendations".

Miscellaneous. The Project also deserves credit for declining to participate in two ill-advised initiatives of the CMA: undue reliance on liability insurance for brokerage firms in lieu of

regulation and inspection, and the institution of the flawed "bookkeeper" system in a hasty overreaction to a fraud problem. While the Project has been responsive to the legitimate needs of the CMA (and other IPs), it deserves credit for saying "no" when that was appropriate.

6. Cairo and Alexandria Stock Exchange

General Relationship. For various reasons the Project has not enjoyed a good working relationship with CASE. A significant player in the capital market, CASE jealously guards its autonomy and has independent financial resources. These factors enable CASE to pursue its own agenda without regard for the goals or positions of other IPs and to hire its own expert advisers who work solely for CASE in pursuit of its own goals.

CASE has also reported significant personal friction with DT2 personnel (whom CASE does not seem to recognize are separate from the Project) in making logistical arrangements for certain study tours, and other conflicts with Project personnel. The existing relationship is a significant constraint on the ability of the Project to assist in the improvement and development of CASE. Establishing a good working relationship between the Project and CASE will be a major challenge. It may not be possible to do this without a significant change in CASE's attitude which is largely beyond the control of the Project.

Board, Membership and Listing Rules. There is some confusion about whether the Project actually drafted the board, membership and listing rules for CASE or only commented on them. The Project has stated that it drafted them.⁷ This is strenuously disputed by CASE itself which claims that the Project only commented, along with other interested parties, after the draft rules were transmitted by CASE to the CMA and then exposed for public comment by the CMA.⁸ These rules were subsequently forwarded to the CMA by CASE for final approval and are currently at different stages of the approval process.

In any event, it is not clear how much, if any, consultation was done with CASE or the CMA before these rules were drafted or who is responsible for doing the lion's share of the work on them. The quality of the rules is poor. They contain several inappropriate and poorly-drafted provisions - one of the very few legal and regulatory documents produced by the Project which the evaluation team found of unacceptable quality. The Listing Rules, for example, are unduly abbreviated and lack necessary detailed guidance when compared to the listing rules of other exchanges. While the CASE Listing Rules, to be appropriate to the circumstances of the Egyptian economy and CASE, need not be as lengthy or as detailed as the NYSE listing rules or the UK "Yellow Book," these draft Listing Rules are insufficiently detailed and of poor quality as a review of the listing rules of other exchanges in comparable environments would rapidly

⁷ Project's QPR 2000-03, pages III-1 to III-3 and CMD QPR 2000-04, pages III-1 to III-3; interview with Garrett Dorer, CMD Project, May 30, 2002

⁸ letter dated December 14, 2000 from Nazre Dastgir, CASE, to Barry Gray; interview with Dr. Shahira Abdel Shahid, Head of Research and Market Development, CASE, May 28, 2002

disclose.⁹ A more detailed description of listing criteria (akin to the schedule set forth in Annex C to the CMA's 2000 Annual Report, for example) should be included in the Listing Rules.

A detailed analysis of the defects of these draft CASE rules is set forth in Appendix H to this report.

7. Central Bank of Egypt

The Project has assisted the CBE in developing a book-entry system for trading, settling, and clearing government securities. It is difficult to evaluate the work done by the Project in this area as the system has not yet become operational (it will begin operations in mid-June).

The Project has also assisted the CBE and MOF in developing a ministerial decree and implementing regulations for primary dealers in government securities, discussed under MOF. Both are of excellent quality.

8. Ministry of Finance

The Project drafted a Ministerial Decree (No. 480 of 2002) concerning the licensing of primary dealers in government securities. The decree is quite short (four pages; nine articles). Although the MOF is given the power in the decree to spell them out, no standards are set forth in the decree for the MOF to apply in the licensing, regulation, and supervision of primary dealers. The detailed "Proposal for the Establishment of Primary Dealers in Egypt" prepared by the Project in July 2000 is quite good, although it does not seem to have been followed through in the draft decree. MOF and CBE are currently drafting, with the assistance of the Project, regulations to implement the decree and criteria for licensing applicants to become primary dealers. Approximately 8 banks (4 government and 4 private sector) have shown an interest in becoming primary dealers.

9. Conclusions

In general, the Project has done an excellent job of achieving its objectives. The fairness, openness, and transparency of Egypt's capital markets have improved as a result of the Project's legal and regulatory efforts. The overall quality of the Project's work has been very good, with the few exceptions as noted above. The Project has earned the praise, trust, and confidence of its IPs, with the exception of CASE. As a result of these accomplishments, the Project has built a solid foundation in Egypt for further assistance to its IPs, which is still needed as discussed below.

10. Recommendations

Although much has been accomplished by the Project, much remains to be done. Closure of the capital markets for over 30 years in Egypt has eroded their infrastructure. It will take significant

⁹ See, for example, the Stock Exchange of Singapore Listing Rules and Manual, available at www.ses.com.sg, and the Stock Exchange of Mauritius Listing Rules at www.semindex.com

additional work to bring Egypt to a completely fair, open, and transparent market. Having demonstrated that it is capable of first-class work and earned the trust and confidence of most of its IPs, the Project is ideally positioned to perform this work and continue to assist the transformation of the Egyptian capital markets as originally contemplated.

The Project and its IP would benefit from taking a more comparative international approach (see the discussion under "CMA-IPF" above) to its tasks. The US approach to securities law and capital markets issues is often, but not always, the best available approach. A few of the documents reviewed concentrated too heavily on American laws, concepts and jargon at the expense of a wider analysis. In addition, the quality of the work of short-term advisers and their value to the Project's IPs would be significantly increased if all short-term advisers were brought in approximately one week earlier than has been the case so far to give them time to (a) assess and understand local conditions better and (b) revise their curricular materials and other documents accordingly.

Areas for future work by the Project include, in the approximate order of importance, the following:

Licensing and Regulation of Salespersons for Brokerage Firms. At present, only brokerage firms, their managing directors, and their "floor brokers" (those who trade securities on the floor of CASE) are required to be tested, licensed and approved by the CMA. Sales representatives employed by brokerage firms, who sell securities and investment advice to members of the public, are not. This is a task of significant urgency and importance. ECMA and CASE should also be involved in putting an appropriate licensing, regulatory and SRO framework in place. The Project did a preliminary paper on this subject in 1999 but no additional work seems to have been done in this area since then.

SRO status for MCSD, CASE, ECMA and EIMA. All of these organizations (except CASE) have requested the Project's assistance in: (1) amending the Capital Markets Law to recognize the concept of self-regulatory organizations (SROs); (2) designate them as SROs in their respective areas; (3) design training courses and licensing examinations for new members of these SROs; and (4) assist them in creating internal structures for governance, investigation, and sanctioning of their members in accordance with the general principles of operating as an SRO. This is a large task involving three or four rather diverse IPs with differing needs and responsibilities within the securities industry. While significant progress has been achieved by the Project, much remains to be done in this vital area.

Margin, Short Sales, Securities Lending, and Net Capital Rules. The Project has already done substantial work in drafting rules and regulations and studying these important areas. The remaining work required to complete the task of fully implementing them in Egypt would be an appropriate task for the Project.

Margin lending, or the ability to borrow funds against one's share portfolio has several desirable effects. Margin accounts at a brokerage firm are perceived to be flexible, and therefore a more attractive place to invest funds, as cash may be raised for urgent or short-term personal financial needs without liquidating one's shares, thus avoiding both the transaction costs involved in a

sale, and possibly having to sell at an unfavorable price. Loans secured by shares would be available to the investing public at lower interest rates than unsecured loans.

At present, no mechanism for margin lending exists in Egypt. As noted above, draft margin regulations were delivered by the Project to the CMA in the first quarter of 2002. Creation of a procedure for margin accounts requires coordination with CMA, MCS D, the bookkeepers who maintain account records for investors, brokerage firms and possibly commercial banks. The CBE or CMA would also have to regulate the maximum percentage of an account's value available for a margin loan from time to time. Changes to Egypt's bankruptcy and secured transactions laws would be involved. Securities account record-keeping would need to be modified to accommodate and enforce margin loans. A significant public awareness and education campaign would be required to encourage investors' and brokerage firms' responsible use of this new technique. It would be a valuable addition to the current securities industry framework.

Short sales (borrowing shares one does not currently own and selling them, while promising to return the shares to their owner at a later date by buying them back at their (hopefully lower) future market price) are not currently authorized by Egyptian law. Short selling adds liquidity to markets; allows investors to profit from market declines when they currently have no other means of doing so; and builds up demand for shares whose prices are declining, often halting and reversing the price decline earlier than would otherwise be the case.

Implementation of a short-selling regime requires significant legal and regulatory amendments to Egypt's securities laws and regulations. Regulation of short sales (such as, for example, the US rule that a short sale may be made only immediately following an "uptick" in price) may be desired by the CMA. Changes in account record-keeping by MCS D and the bookkeepers will be required. A public awareness and education campaign would also be required to fully realize the benefits of allowing short sales.

Securities lending by brokerage firms also adds liquidity and flexibility to the market.

Net capital rules should increase the financial strength of brokerage firms, reduce bankruptcies and other failures, and thereby increase public confidence in the capital markets.

As noted above (see the discussion under "CMA"), all these rules contain novel and entirely unfamiliar concepts. Consequently, the Project will have to not agree not only on their final form with the CMA and other IPs but also engage in a substantial training program to make sure these new rules are properly and uniformly applied in practice.

Institutional Strengthening of CMA, MCS D and CASE Legal Departments. In many respects the Project has functioned as the legal department of several of its IPs since 1998, engaging in such activities as drafting laws and regulations and model contracts; conducting legal training; commenting on legal issues affecting the IP; advising senior management of the IP on legal issues, etc. even though CMA, MCS D and CASE have their own legal departments. An appropriate task for the Project would be to provide institutional strengthening for the IPs' own legal departments so they could begin to perform all these tasks.

CMA has approximately 10 lawyers, all civil servants, in its legal department. None of them met by the evaluation team speaks English well or has had any exposure to international securities law concepts other than through the Project. They are involved in prosecuting violations of CMA's rules and regulations (*i.e.*, corruption) by its internal staff and violations of CMA's rules by capital market participants. The department's other duties include investigating allegations of violation of the Capital Markets Law and preparing files to send to the prosecutors who will present them in court. CMA legal department staff also consult, as experts, with prosecutors in preparing for trial or settlement of such cases. Staff attorneys represent the CMA when it is a party in a civil suit in the State Council (which hears appeals from sanctions imposed by the CMA). The Chairman of the CMA stated that the senior lawyer in the CMA's legal department also sat on the committee of senior CMA staff which reviews draft laws and regulations.

MCSD has a legal department of 12 attorneys, headed by Reda Farahat. Many speak English and have had international education or experience.

CASE has lawyers on its staff but they have not participated actively in the Project's work.

Institutional strengthening of the legal departments of these IPs through training and otherwise is important to enable them to fully serve the current needs of their organizations. This will become even more important for MCSD and CASE as they become SROs.

Investor Protection Fund. The Project has already done some work on this task, an initiative of the CMA, and delivered a draft decree to the CMA in the first quarter of 2002. Full implementation will require the cooperation and support of brokerage firms and the Project's other IPs even after the decree is formally adopted by the CMA.

Training of Prosecutors, Judges, Arbitrators, and Lawyers in Private Practice. In addition to the prosecutors and judges with whom the CMA interacts in enforcing the Capital Market Law, there are approximately 200 to 300 judges and lawyers in private practice in Egypt who have either occasional or regular cases involving securities law issues. Several IPs have indicated that their current standard of knowledge about these issues is minimal. The Project could conduct local training courses and workshops on securities law issues for the benefit of these practitioners. The Project might also assist its IPs and the Egyptian bar in creating an arbitration center to resolve securities law disputes and training its arbitrators. (All of MCSD's contracts, and many brokerage firms' standard form contracts, require arbitration in lieu of litigation to resolve disputes).

Increasing Public/Private Communication and Trust. The Project has earned the trust and confidence of both the public and private sector participants in Egypt's capital markets. This is a significant accomplishment given the high level of mistrust and misunderstanding between these two sectors which we found. Market participants from the private sector are fully aware that the Project advises their counterparts in the public sector (and vice-versa), a channel of communication which has been very valuable in several instances.

The Project should consider sponsoring more joint training and workshops on matters such as, for example, CASE rules which will ultimately have to be approved by both CASE (private sector) and the CMA (public sector), or training in surveillance which is a function of both

entities. Conduct of such joint activities could help bridge the current gulf between the Project's IPs.

Accounting Standards. This task was part of CMD's initial proposed scope of work but has not been implemented. At present there are material differences between EAS and IAS. Substantial work, including training of Egyptian accountants and auditors in IAS, will be required to bring listed issuers into full compliance with periodic reports to CMA conforming to IAS.

Restructuring the Ownership and Organization of CASE (Privatization and De-mutualization). At present, CASE is 100% owned and controlled by the GOE which also appoints 6 of its 11 directors. The other 5 directors represent brokerage firms. Its exact legal structure, control, and ability to manage its own finances are matters of some doubt and uncertainty. Serious consideration should be given to restructuring CASE through privatization and de-mutualization.

In most countries the securities exchanges are fully privatized. (In fact, the new draft Capital Markets Law expressly contemplates the chartering of such private exchanges by the CMA). Although regulated by the government, the exchange is owned by the brokerage firms who are its members and is operated for their mutual benefit. Such private, though mutual, ownership forces the exchange to focus on efficient and cost-effective operation, development of new business, and other typical efficiencies of private ownership.

A weakness of this form of "mutual ownership" is that the exchange's owners are also the major customers for its services, leading to inherent conflicts of interest between the exchange as the seller of services and its owner/members as their purchasers and a consequent distortion of the exchange's fee-setting process.

To avoid this conflict and for other sound reasons, many exchanges have taken the next step to full privatization, also known as "de-mutualization". Ownership of the exchange is opened to all investors, like any other corporate shares of stock, and is not restricted to brokerage members of the exchange. Members no longer own transferable property rights in "seats" on the exchange. Rather, they are licensed by the exchange to use its facilities after complying with membership regulatory standards and payment of the appropriate annual and per transaction fees established by the exchange. This "de-mutualization" results in both the perception and the reality that an exchange is no longer an insiders' club and leads to market-driven pricing of exchange services and more efficient operations.

The advantages of both privatization and de-mutualization for CASE should be studied and, if acceptable to GOE and IPs, implemented.

Even if CASE is not restructured, a significant area for study and implementation is restructuring the board of directors of CASE to include representation beyond the GOE and brokerage firms to encompass other constituencies which are served by CASE – law and accounting firms, listed issuers, and the investing public. Input from these constituencies would help eliminate the perception of CASE as an insiders' club.

Expanding CASE Membership Categories and Regulatory Jurisdiction. At present, following the traditional model of a stock exchange, only brokerage firms are members of CASE. In other

jurisdictions, the concept of “membership” has been significantly broadened and divided into different categories. Brokerage firms may remain traditional “trading members”. However, other types of firms involved in the listing and ongoing compliance process (particularly law and accounting firms) become “listing members”. (Brokerage firms may elect to become both trading and listing members). Only listing members are allowed to draft prospectuses, financial statements, periodic reports and other documents filed with the exchange, forcing firms which desire to do this type of work to submit to regulation by the exchange and to contribute to the funding of its operations through the payment of membership fees. Expanding membership in this-fashion would also give CASE additional regulatory jurisdiction over these firms, essential to make sure they obey CASE’s regulations and properly assist the listed issuers they serve in complying with their initial and continuing obligations to the exchange.

Increasing CASE Listings. CASE could be making a more active marketing effort to attract high-quality issuers to list on CASE. The GOE’s privatization initiative has supplied some listings, but there is no reason why CASE should rely solely on the GOE’s privatization timetable to bolster its listings.

A study should be made of why firms have chosen not to list on CASE. Seminars and workshops for corporate CEOs and CFOs of unlisted companies explaining the advantages of listing and the procedure to become a listed company could be conducted. Emphasis could be placed on the advantages to potential issuers of listing corporate debt and other securities as well as common stock. Where necessary, CASE’s listing and ongoing compliance requirements might be amended and streamlined to attract additional listings – as long as the quality of listings is maintained. The Project could conduct such a study in conjunction with CASE and assist CASE’s outreach efforts.

Secondary Listings. Special expedited and simplified provisions should be made in the listing rules to allow, on application by the issuer, the “secondary” listing and trading of securities already listed on another exchange (the “primary exchange”). Primary exchanges must be formally recognized in advance by CASE as a credible and reputable exchange, as the primary exchange remains the main regulatory and reporting body for the listed securities, with copies of all announcements and filings made to the primary exchange to be made simultaneously (or immediately afterward) to CASE. A secondary listing procedure is very useful in attracting well-qualified issuers to CASE (for example, the six Egyptian companies currently listed on the London Stock Exchange). Secondary listings may expand the shareholder base of the issuer and increase its trading volume, although by permitting securities to be traded on more than one exchange may sap liquidity. Careful selection of recognized exchanges is essential in this area for quality control purposes. (Recognition need not be mutual).

Bankruptcy Law Reform. Egypt's bankruptcy law has, with one minor exception, remained unchanged since 1883. Of particular concern to the securities industry are provisions concerning the rights of the beneficial owners of securities whose shares are held in the name of their broker, MCSD, or another record owner when that record owner goes bankrupt, or when bankruptcy affects one party to a trade after the trade is agreed but before it is settled or cleared. If such bankruptcies are allowed to affect the rights of beneficial owners or non-bankrupt parties to a trade, their confidence in the capital market is adversely affected. Clarity and reform in this area are also essential if Egypt is to meet G-30 and BIS international standards in this area and if

securitizations (which must be “bankruptcy-remote”) are to be pursued as a new financial technique.

A broad overall revision and modernization of the bankruptcy law is currently under discussion. The IPs in the securities industry in Egypt are anxious to make sure that their interests are expressed and form part of the new law. The Project has made a good start in this area with its discussion paper and workshop in 2000 (“Bankruptcy Law and the Capital Market: An Assessment” (June 2000), but needs to broaden the participation in this effort to include all its IPs and more representatives from the private sector.

Separation of Regulatory and Promotional Functions. Clearly delineate within CASE for example the compliance and disciplinary functions as separate from marketing and promotion of the exchange and its listing and trading functions. Similarly, distinguish responsibilities between institutions, for example CASE to promote listing and provide trading platform, while all compliance, surveillance and enforcement functions to be performed by CMA. Although this is inconsistent with the US model for capital markets, it is the norm in other countries. For example, in the UK the processing and approval of listing applications is now performed by the FSA, the regulatory body, rather than the London Stock Exchange.

CMA Licensing and Certification of Portfolio Managers. This is an initiative by EIMA, which needs Project support in designing examinations and licensing regulations to certify portfolio managers.

AUTOMATION UPGRADING AND INFORMATION TECHNOLOGY

1. Findings and Analysis of Major Project Activities and Deliverables

The information technology component of the CMD project evaluation focused on the review of the major IT related activities at the IPs (CMA, CASE, MCSD, CBE and ECMA) that are the primary beneficiaries of the bulk of the project's IT budget and expenditures (Appendix C). Other IPs, namely EIMA, MOFT and MOF did not receive significant IT input.

The evaluation methodology used included:

- Review of the IT sections of the CMD reports delivered by Chemonics on CD and delivered in hard copy during the mission in Cairo (Appendix A);
- Review of the contractor's yearly work plans and quarterly progress reports;
- Interviews with CMD project staff involved in the IT components of the project;
- Interviews with IP staff responsible for the implementation of the IT components in each institution;
- Review of the functionality of the information systems provided by the CMD project through demonstrations at CBE (book-entry system) and CMA (document archiving system);
- Site visits to assess suitability and usefulness of equipment and off-the-shelf software procured under the project at CASE, CMA, MCSD and CBE; and
- Occasional follow up interviews to clarify any inconsistencies that may have surfaced during course of the evaluation.

2. CASE – Cairo and Alexandria Stock Exchange

The primary contribution of the CMD project to CASE was the successful procurement of the hardware and network management software (Appendix D) necessary to host the EFA Software Services Ltd. trading system that had already been procured independently by CASE. The equipment procured consisted of seven high capacity servers and 180 trading workstations distributed among the floor brokers and other staff in the premises of the exchange.

The workstations are utilized by the floor brokers and CASE staff. Although the exchange has already upgraded them at their expense with flat screen monitors, in general they are being utilized to their full potential. The servers, on the other hand, are considerably underutilized. The original rationale for the high capacity and the large number of servers was based on the projected growth in trading volume when the purchase was budgeted at the peak of the market in 1998. The servers were meant to be allocated as follows: (a) two to run the EFA trading system (main and stand-by); (b) one for disaster recovery at an alternate site; (c) one as communication server at the Alexandria branch; and (d) three as communication servers to feed real time market data to CMA and MCSD and financial information providers Reuters and MIST.

As it turns out, the Alexandria server is still in Cairo with no immediate plans to transfer it; the disaster recovery server is still on the exchange premises; given the very low trading volume,

the communications servers are barely utilized; and the applications servers have plenty of excess capacity.

The CMD project's intervention at CASE in terms of IT has been limited to this hardware procurement of approximately USD 1 million because the trading system had already been purchased by CASE. The hardware specifications were constrained by the application requirements and were meant to accommodate trading volume growth estimated on the basis of recent trends at the peak of the country's privatization campaign. Instead, trading volume has declined in recent years to 30% of peak. The excess capacity offered by the equipment is not likely to be utilized effectively in the foreseeable future.

Conclusion

The CMD project has been severely constrained in its ability to assist CASE in the information technology area beyond the procurement of the trading hardware. The reasons for this are mostly outside the Project's control. These constraints range from the fact that this specific hardware procurement was designed into the budget from Project inception at the specific request of CASE, to the fact that CASE, being financially self-sufficient and able to hire and retain technically competent staff, is seemingly unwilling to request technical assistance from the CMD project.

While there may be other areas where the CMD project could offer technical assistance to CASE, such as reducing their vulnerability to service interruption due to insufficient disaster recovery measures, it is quite unlikely at this stage that assistance will be sought.

Recommendations

Review with CASE management areas in which the CMD project can arrange for specialized technical assistance such as disaster recovery planning.

3. CBE – Central Bank of Egypt

The primary IT contribution of the CMD project to the CBE has been the development of the book-entry system for Treasury-bills and bonds amounting to approximately \$64,400. The book-entry system design was based on the two-tiered United States' model of primary dealers and banks participating in the primary market and reselling to their retail customers. It is implemented on a Windows 2000/Oracle 8 platform with an Arabic user interface. Development had been completed and the system is currently being tested with actual data. Users are being trained. It is intended to allow the primary participants to send and receive bids and confirmations through the SWIFT messaging system to which the CBE and most commercial banks already belong. Currently the system can process the bi-weekly auctions and secondary market transactions in Treasury-bills. There are plans to include functionality for Treasury-bonds that are currently being traded over the counter at CASE and settled at MCSD. Arrangements for SWIFT connectivity are being finalized. Approval from the authorities for dematerialization of the securities that will allow full deployment of the system is expected in a matter of weeks.

The development of the book-entry system was delayed due to lack of institutional buy-in at the beginning of the Project. However, due to changes in the CBE management, the situation was reversed and this task was eventually initiated and is currently near completion.

However, there is the likelihood of operational and settlement risk due to a disconnect in the DVP (Delivery-versus-Payment) processing cycle. There is no electronic connection between the receipt of the buy/sell orders in the front office to the back office where cash is transferred among the clearing accounts on the books of the CBE. The CMD project has addressed the DVP issues in general and those associated with the settlement of corporate securities through MCS D in particular and presented recommendations by payment systems experts (DVP Assessment, Part I and II, May 2001). Specific DVP issues identified in the original design documents related to the book-entry system within the CBE (see CMD report: Book Entry System Requirements, June 1999) may have to be reviewed.

IT support for the book-entry systems is currently being provided by the CMD project and user and technical training is being provided to the CBE staff. Current plans call for a total transfer of responsibility to CBE staff over the next four months.

Conclusion

The book-entry software application seems to satisfy the requirements of the CBE as defined to date for the processing of Treasury-bills. Processing of Treasury-bonds will require further progress on inter-institutional arrangements but it is not expected to be a technical issue of much import. DVP vulnerabilities of the book-entry system seem to be understood and properly addressed, but considering the time-lag between trade and settlement and the fact that the participants' clearing accounts reside on a separate computer system in a different department, it will be prudent to review all manual and automated procedures in the settlement cycle.

Training of the front-office staff and technical training of the support staff seems to be adequate at this stage, although it is recognized that internal IT support may remain weak due to salary constraints in the Civil Service.

Recommendations

Review manual and automated procedures in the settlement cycle to ensure DVP and eliminate or reduce settlement and operational risk.

4. MCS D – MISR for Clearing Settlements and Depository

The major IT contribution of the CMD project to MCS D to date has been the procurement of hardware and off-the-shelf software amounting to approximately \$273,000 (Appendix E) consisting of: (a) application server upgrade; (b) five firewall servers and software; and (c) a network management system. Additionally the CMD project has arranged for various security assessments and studies by experts in network security and disaster recovery.

MCS D is responsible for the clearing and settlement of all securities transactions in Egypt and runs a fairly sophisticated IT operation supporting approximately 500 simultaneous users in five branches on a private WAN (Wide Area Network) of internal staff and other stakeholders

(banks, brokers, capital markets institutions, data providers, etc.). The hardware, operating systems, and telecomm are quite sophisticated and all application software has been developed in-house.

The CMD project has endeavored to satisfy the needs of the MCSD in the IT area by providing the services of security experts and the equipment and software necessary to improve network security with firewalls. The Project has also provided technical assistance and equipment for network management systems and to ensure business continuity in case of disasters. In the area of disaster recovery in particular, it will be necessary to work out in detail and finalize a robust disaster recovery plan.

During the evaluation visit MCSD expressed dissatisfaction with the performance of the local vendors who support the firewalls and the network management systems. MCSD had not renewed their yearly maintenance contracts claiming that the vendors' technical staff had not been able to solve various technical problems. In addition, MCSD felt that the training and support offered was inadequate. Upon further investigation and discussions with the MCSD, CMD and the vendors, it was apparent that, while the vendors' technical performance may have been lacking, their willingness to be responsive to MCSD and to take corrective measures was clear. Yet MCSD is still not keen on renewing the maintenance contracts.

Conclusion

MCSD is financially self sufficient, hence they are able to maintain competent technical staff and to acquire technology based on technical and business decisions unencumbered by the strict USAID procurement regulations to which the CMD project is subject. The specific technical issues that gave rise to MCSD dissatisfaction with the support appeared to be mostly a matter of configuration settings and fine tuning of complex software components from different vendors so that they could work together. Nevertheless, it was also clear that MCSD has strong preferences as to local service providers, ample financial resources, and little patience with what they perceive as substandard services.

This partiality is understandable in private sector organizations but it imposes serious constraints on the CMD project's ability to assist MCSD in the IT area. While exceptions and waivers can sometimes be justified, as was done with the sole source procurement for the existing server upgrade, the CMD project must select IT suppliers according to impartial technical criteria, specific procurement procedures, and within predefined budgets, hence the CMD project may be of greater assistance in the provision of expert IT consulting services than in the procurement of hardware and off-the-shelf software.

Recommendations

Explore areas where specialized IT experts can be of assistance such as in finalizing a robust disaster recovery plan, designing and performing an exhaustive set of disaster recovery tests and keeping the test plan current.

5. CMA – Capital Markets Authority

The CMD project has supported the CMA with a number of IT procurements (Appendix F) including workstations and network equipment, training equipment, computer facilities improvements, firewall hardware and software, web servers and software, and a document archival system.

The document archival system is currently under implementation; a local contractor has been selected to provide the hardware and software to scan an initial set of 500,000 pages by August 2002 and to train the CMA staff in its operation. The equipment has been recently installed, but document scanning has been underway with loaned equipment and so far approximately 160,000 pages have been imaged.

The amount of documents at the CMA has been estimated to be over 26 million, however a large number of these are duplicates or documents of no importance. It is still not clear what is the exact volume of pages that should be imaged and retained, but the CMD project has introduced procedures to select, classify, and prioritize the documents to be scanned. In this context, the CMD project has also prepared a process model for the CMA in order to better understand the document workflow and as input to any future business process reengineering effort and organizational restructuring recommendations.

Additionally, the CMD project has assisted with the implementation of the existing CMA web site. Recently, a new site that will provide dynamic content and secure access to the CMA various databases has been proposed. Design specifications have now been prepared and the RFP has been published.

Conclusion

Notwithstanding the numerous CMD interventions and continuous support, the CMA remains institutionally weak, particularly in the IT area where appropriate technical and management skills are crucial. There is in fact a high risk the various IT investments made in the CMA may yield a very low return given the institution's inability to attract and retain competent IT personnel due to the inadequate Civil Service salary structure.

Recommendations

Explore methods to strengthen IT skills within the CMA including increased IT training and alternative compensation schemes to attract/retain competent IT staff or outsourcing alternatives to ensure competent IT support.

6. ECMA – Egyptian Capital Markets Association

The contribution of the CMD project to ECMA in the IT area has been the provision of hardware and software amounting to approximately \$30,000 to implement a membership database, training tracking system and provide basic office automation. The system was developed in MS Access and is functioning as expected. ECMA finds it very useful and is very pleased with it.

Conclusion

While the original CMD project design did not include a significant IT investment in ECMA the project's contribution was quite successful.

Recommendations

Continue providing assistance with information systems as necessary, especially if ECMA's functions and responsibilities in the development of the Egyptian capital markets increase.

7. IT Training

IT Training has been provided to the staff of all the IPs in specific technical subjects such as Oracle programming or database administration or network management, directly related to the hardware/software products acquired (Appendix G). This training has been very useful to the IPs since it has enabled their IT staff to ensure proper operation of the information systems. At the managerial level, training in strategic planning is planned for the CMA staff.

Conclusion

Given the continuous changes in IT, constant and highly specialized technical training for internal staff is essential for all IPs. The CMD project is doing its best to provide it within the constraints of the arrangements with the DT2 program. Additional training at the management level in IT strategy planning and IT project management are necessary and plans are being made to meet those needs.

Recommendations

Continue providing specialized IT training to all IPs and arrange for IT management training in project management and information systems strategic planning.

NEW FINANCIAL INSTRUMENTS

1. Findings and Analysis of Major Project Activities and Deliverables

The Project considered the need and demand for new financial instruments from the outset. Indeed, it was a need identified in early planning documents. Moreover, as the volume and interest in individual equities diminished from 2000 onward, the need for alternative investments to maintain the volume of the stock market and income of the brokerage firms was apparent. Nevertheless, the local firms developed few new products. According to one source, the larger local investment and brokerage firms are looking outside Egypt for business rather than creating opportunities at home. Others report that nearly 30% of their income had been derived from the "bookkeeping" operations that have now been dismantled.

The CMA's Annual Report for 2000 included the following information:

"To meet the diverse needs of investors, the CMA encourages the development of new types of investment funds managed by experienced professionals. Additional instruments will increase investment options and the willingness of foreign and domestic investors to participate in the marketplace, and will make the markets more attractive to institutional investors."

2. Project Activities

The project sponsored four papers about new products. The first paper, "Unit Investment Trusts in the Egyptian Market," October 1999 was prepared at the request of the Chairman of the CMA. In its conclusions, the author noted the constraints and next steps to be addressed. These included the dominance of the debt market by thinly or un-traded government bonds, the lack of a broker dealer system, and finally the uncertain legal and regulatory constraints confronting such a new product. The report recommended that the Chairman of the CMA investigate the significance of these legal and regulatory issues as a first step in considering the usefulness of unit investment trusts in the Egyptian market. The evaluation team was not able to find any other reference to this report or to the recommended action by the CMA. The broker dealer issue is being addressed by the Central Bank.

The second paper, "New Financial Instruments," 2001, discusses exchange traded funds, convertible and exchangeable debt, and Global Depositary Rights. The third paper "Securitization of Assets," 2002 discusses asset-backed securities and other instruments that have become in the United States popular methods of spreading risks of mortgages and commercial debt among many lenders and investors. These thoughtful papers were presented to the CMA Chairman in whose office they have stayed for many months without formal or informal response to the Project.

"Securitization of Assets" was also presented to several of the investment banks and brokerage firms in Cairo. According to Project staff, the paper generated some interest among the private sector in Cairo. However, most of these players are unwilling to invest their time and money in developing these ideas until there is a clear signal that the Chairman of the CMA would give approval to innovations. As an example of the reasons for this caution, one of the portfolio

managers told us that six months ago he took one of his largest clients to the CMA for an interview with the Chairman, seeking permission from the CMA for a stock buyback in the client's company. Since the date of that interview, there has been no word from the Chairman of the CMA.

The fourth paper is entitled "Negotiable Certificates of Deposit," by John Noonan (no date). It is an interesting paper and may be a useful concept, but it fails to mention the constraints in the law, regulations, and structure of the Egyptian banking system. Negotiable or brokered Certificates of Deposit were developed in the United States in 1961, but did not become widespread until FDIC insurance was increased to \$100,000. CDs from Federally insured banks are traded as securities so that investors need not hold a five-year CD to maturity, but could sell it to an investor who wanted, for example, the last six months of the CD. Federal insurance, which is not now available in Egypt, was essential to this product's development and acceptance.

Apart from the paper on unit investment trusts, the evaluation team was not able to find out why these particular new product ideas were the subject of CMD studies, as opposed to others such as options on stocks currently traded on the CASE or other instruments that would permit investors to hedge their investments in Egyptian securities.

One of the most promising ideas presented in the papers is the development of closed end mutual funds, or exchange traded funds. These could be comprised of equities such as the thirty most active stocks during the past year, the largest companies, the components of the EFG Hermes Index, or some other basket of stocks. It could also include bonds – a mix of Egyptian government and corporate debt, and until there are enough issues to fill the portfolio, high-grade foreign debt could be included.

Just days before the departure of the evaluation team, it was learned that EFG Hermes had presented an idea to the CMA and had received tentative approval to move forward on an ETF that would include factored instruments from Egyptian firms. This is indeed promising, but the team's conversations with the Chairman of the CMA and with the office within CMA dealing with this product led the team to believe that there many unanswered questions about this product. Since the evaluation team found out about this product development from sources other than the CMD, the team assumes that the CMD was not involved in the development of the product or its assessment by the CMA.

3. Debt Markets

While these papers discussed ideas for the future, the Project has already made a significant contribution to the potential development for the market for domestic, local currency denominated government debt. The Project's assistance to develop the broker-dealer and the book entry programs has consisted of legal and regulatory assistance to the Central Bank of Egypt in drafting the bond dealer decree and information technology to set up the book-entry system. When operational this system will have changed all Treasury-bill transactions to electronic format, doing away with the certificate system of today. It may bring the government debt market out of institutions and into the hands of the retail market. Combining this development with the products mentioned above could pull idle assets out the banks' savings

accounts and into a more liquid market. The impact on government bonds is academic right now since there are only two maturities issued at present: 2003 and 2007, hardly enough to warrant a "bond trading system."

Another new product for which the Project deserves some of the credit is the willingness of the Central Bank of Egypt to recognize Treasury-bills with maturities of 15 days or less as cash for purposes of maintaining bank reserves. This change in policy may free up bank deposits for other purposes.

These are significant accomplishments and the Project deserves much of the credit for the patience and tenacity their staff has shown in this endeavor. The development of the broker dealer and book entry systems is also discussed in sections II and III, above.

Mortgages on residential properties have been recently authorized under new legislation. Several respondents in the evaluation team's interviews mentioned the opportunities for new investment products that may be derived from securitized mortgages. However, banks are not actively marketing mortgages nor is there any tradition of consumers borrowing long-term for home purchases. Moreover, Egypt lacks many of the institutions associated with mortgage lending such as rating systems for borrowers, underwriting regulations, and bank supervision of consumer lending.

4. Conclusions

The capital markets in Egypt need new investment products to attract new investors and additional funds. The brokerage firms are withering away because of the lack of volume or are turning to foreign investments, which do little to aid the capital markets in Egypt.

The private sector is reluctant to invest time and money in the development of new investment products as long as they perceive the CMA, the principal gatekeeper, as being resistant to new ideas. The private sector, on the other hand, is viewed by the CMA with suspicion.

The Project has not invested the same time and funds in the development of new products as it has in other aspects of their objectives. Quite correctly, they decided that the strengthening of market institutions and architecture deserved a higher priority. Nevertheless, the Project has sponsored several papers that could be the basis for needed new products. These ideas, with one exception, have not been systematically shared with the private sector.

5. Recommendations

The CMD needs to invest time and the creative energy of its staff in encouraging the industry to put forward new products. Strengthening the CMA staff to analyze product proposals should also be a high priority.

The Project would benefit from adopting a more methodical, rigorous, and structured approach to the exploration of new products. The evaluation team suggests that CMD sponsor a series of roundtables, calling together all Institutional Partners to discuss their needs and their perceptions about the constraints to new product development. For example, there are

significant barriers to developing negotiable CDs, including the lack of depository insurance. Inter-institutional task forces are one approach to the solution of this and other barriers.

Other similar roundtables need to include the private sector – including the CASE - to discuss demand, need and constraints to development of new products.

The Project should take the initiative in preparing research documents about the role of their Institutional Partners such as the Central Bank in the development of mortgage markets and in the development of derivative investment products.

Not all new products need to be developed by the industry. For example, the options market needs to be *permitted* as does short-selling. Currently, there is no way for investors to hedge their positions in the Egyptian stock markets. This is an area in which the CMA could rightly take the lead, with technical assistance and training from the CMD.

Mutual funds – both open-ended and exchange-traded – offer an appropriate means for attracting individual investors back into the markets. The CMD should invest time and perhaps technical assistance in strengthening the investment banking and fund management industry and the CMA's ability to respond to new ideas.

Training programs should be tailored to the staff at the CMA, CBE, and if possible at the CASE, that analyze new investment ideas. Specialists from the Securities and Exchange Commission would be ideal.

PUBLIC OUTREACH

1. Findings and Analysis of Major Project Activities and Deliverables

At the beginning of the Project, the staff identified several activities that would strengthen the ability of the CMA to reach out to the financial community through the mass media and to educate and inform the investing public about the financial markets. These included developing and training the staff of an office of press and public relations at the CMA, training and orientation of journalists, preparation of materials that could be distributed to the public, the development of television programs on investing, and an internet strategy with an attractive, interactive web site.

As the Project developed, opportunities for strengthening the communication capabilities of other Institutional Partners arose. For example, the MCS D needed assistance in producing its annual report that is widely distributed throughout the investing community. ECMA, the investment community's professional organization, sought assistance in improving its image with the public and with its members.

The evaluation team concentrated its efforts on examining the program for training journalists and in assessing materials produced by the project and their distribution to the general public. In this regard journalists were interviewed at length and one of the forums was observed. The three largest brokerage firms were visited as well as the ECMA.

2. Journalists

The Chairman of the CMA related to the evaluation team that within a few weeks of the Project's start he told them that an important objective was to improve the financial literacy and the understanding of the capital markets by the financial and economic reporters from the nation's magazine and newspapers. As he put it bluntly to the evaluation team, he was tired of being blamed in the press for the decline in the stock market and the drop in particular stocks. He also felt that the reporters did not understand the basics of economics and finance.

In response to his challenge, the CMD organized a series of activities that have continued throughout the project period: forums, workshops, and later two Observational Study Tours. These activities have had the objective of increasing the professionalism, journalistic skills and financial knowledge of the participants.

The forums met 12 times from May to December 1999, regularly attracting 20-30 journalists, less frequently after that for a total of 16 forums. The speakers at these forums ranged from visiting short term CMD consultants to cabinet level officials. CMD also organized two DT2 sponsored courses at the Arab Academy of Alexandria covering financial and capital market topics. A third workshop was led by the journalists themselves, leading to more participation. Topics included national coverage of local and international issues, international TV business coverage and using the Internet. Finally, a major training investment of the project was two OSTs for a total of 39 journalists and spokespersons from Institutional Partners.

The evaluation team met with six journalists from the leading Cairo daily government-owned newspapers and from the only newspaper and magazine (public or private) devoted to financial news. The respondents had attended most of the forums and had been participants in the OST. The evaluators also met with press spokespersons from the CMA and MCSD. Finally, the evaluators met with the leading television presenter of financial and stock market news. Data was also used from post-training DT2 reports and CMD reports describing press forums and workshops and their evaluations. Finally, the evaluators met with market participants and asked about the impact of the quality of financial reporting.

Without exception, participants said that the forums and workshops had provided them with outstanding opportunities to meet national and international leaders of finance and the economy. Not only were these opportunities for stories for their papers, but equally important they learned new insights about their craft. They felt that the program gave them more credibility with their readers. In addition, they felt more confident in asking probing questions of corporate and government spokespersons. All gave the study tour high marks for relevance to their own situations. Several said that they learned always to verify their stories and not just accept what they are told in a press release. Some were particularly impressed with the way in which corporate spokesman briefed them and the role of government spokespersons in the communication policy of the SEC.

The evaluators observed that the journalists tended to see their roles as reporting about the movements in the stock markets rather than looking at financial news more broadly. None of them reported that they saw themselves now or in the future as writing about personal or corporate finance and money management issues. They seemed to view their jobs as reporting the news rather than educating or persuading.

Through both DT2 and CMD evaluations, the participants gave the project's training high marks.

The Chairman of the CMA has been particularly impressed with the program of training journalists. He told the evaluation team that he thought that the quality of financial journalism had improved significantly in the past two or three years. He said that the number of investor complaints had risen over the past few months. He attributed this rise and the quality of the complaints to the content and approach of the financial journalists. He felt that investors were learning more about their rights as shareholders and were less likely to bring trivial complaints to the CMA.

In interviews with owners and managers of brokerage firms, the evaluators received mixed messages: some could see no difference and told stories of reporters being scolded by government officials when their questions showed their ignorance about financial basics. Others felt that the reporters were more accurate and less likely to report unsubstantiated rumors.

Conclusion

This has been one of the most consistent programs throughout the Project. It has had a profound impact on the participants, especially the journalists who participated in the Observational Study Tours. When compared with the level of financial reporting at the beginning of the

project, the financial journalism today has experienced significant improvements. Although stock market results are reported on television, there has been little progress in persuading the government-owned television stations to broadcast analytical or educational programs on finance and investing.

Recommendations

The journalist training programs should continue. In the next year, the CMD should spend time and resources transferring to others their skills in managing the logistics of this program. The CMA is the logical choice to manage the press forums, since the idea for them came from the Chairman. The Project should assist the CMA to search out sources of funding for these forums so that they will continue after the close of the Project.

3. Institutional Partner Communication

A second communication objective addressed by the CMD was to strengthen the skills of institutional partners to reach out to their target groups. The CMA, MCS D and ECMA all have been challenged to convince the investing public that their institutions deserve its trust and confidence. The CMA has the additional need to convince the regulated entities that it is fair, vigilant, and efficient in pursuing its duties. These institutions and the Cairo and Alexandria Stock Exchange have determined that there is a need to educate the public in the basics of investing in the stock market.

4. Capital Market Authority

One of the early activities of the CMD at the CMA was to assist it in publishing the 1998 Annual Report. CMD staff prepared the first draft of the report, received approval of the Chairman, and arranged for printing in the United States. In each successive issue, the CMD involvement declined as the skills of the CMA staff increased. The report for 2001 has been prepared entirely by the CMA staff and at the time of the evaluation, a first draft of the text and charts had been sent to the CMD for comments. The CMD expects that it will assist in some of the layout and graphics and relations with the local printer, but that the lion's share of work will be done by the CMA staff.¹⁰

Another element of the strategy of strengthening the institutional capabilities in communication was to train press spokespersons at the CMA and MCS D. CASE did not request this assistance. Two professional staff from CMA and one from MCS D attended all press forums and the OST. Additionally, the press spokespersons from CMA received training in corporate finance. The Project has seconded one of their staff to the CMA to provide on the job training to the press office of the Chairman of the CMA. This staff person's professional and personal skills have been instrumental in building a more mature and strengthened press strategy of the CMA.

¹⁰ Additional comments about the annual report are found in Part II, Legal and Regulatory Reform, above.)

In addition, the CMD's short-term advisor from Hill and Knowlton prepared a report for the CMA which addressed the communication staffing requirements.¹¹ The thrust of the report was to recommend that the CMA employ a chief spokesperson/strategic counselor, a senior staff person in whom the Chairman would have great confidence and who could speak for the Chairman. This person would be supported by two other communication team members.

At the time of the evaluation, the CMA had employed two young and increasingly skilled press relations persons but not the senior staff person recommended by the report. They have participated in the Cairo-based financial training, the press forums, and the OST. In spite of their lack of seniority, press contacts with foreign media are gradually being transferred to their hands. Nevertheless, much of the press relations remain firmly in the hands of the Chairman. The evaluation team finds that this continuing responsibility for communication of the Chairman means that he has less time to devote to supervising the important inspection, surveillance, and enforcement functions of the CMA. This is a work in progress and the evaluation team believes that if the new press relations officers remain at their posts, they will gradually assume much of the press relations now done by the Chairman.

Conclusion

The CMA has a special communication responsibility: to assure the investing public and the industry participants that it is ever-vigilant, fair, and efficient in its enforcement of the rules of the market place. One of the ways that other investment industry regulatory agencies achieve this objective is by sending a message through the press about the vigorous and very public enforcement of the law. The evaluation team could not find any evidence that this was the explicit strategy at the CMA.

Recommendation

Because of the lack of confidence by the general public in the market (as a result of the market crash and some recent, particularly egregious violations of securities law) the CMA should include in their communication strategy the systematic publication of investigations, penalties, and prosecutions. Securities law and its enforcement are certainly appropriate topics for the press forums.

5. Misr for Clearing, Settlement and Depository

The MCSD has recently employed an assistant public relations director, a former employee of the CMD. He is very able and has begun regular communications to the brokerage industry and other members of the investment community about the activities of the MCSD. He publishes a quarterly journal sent MCSD shareholders and others in the industry. He also communicates to the industry through "blast faxes." Because many of the functions of the brokerage firms – securities deposit, custody and dividend payment – have been taken over by the MCSD this regular communication is especially important. The CMD project is planning to produce with

¹¹ "CMA Communications Function: Recommended Organizational Structure and Job Descriptions," December 2001.

the MCSD a "Guide to Services" and a question and answer booklet for more general circulation. The MCSD, however, does not view the investing public as part of their target group according to this assistant director.

Conclusion

This viewpoint is a mistake, in the opinion of the evaluation team. In most countries the clearing and settlement procedure is invisible and the organization is anonymous. In Egypt, the MCSD will have a high profile since the custodial arrangements of the past will change to a system in which the MCSD will be the only place in which customers can find track their holdings and in which all securities must be deposited. It is conceivable that customers may have more personal contact with MCSD than they have with their brokers. Under these circumstances, the customer traffic in and out of the MCSD offices and correspondence beg to be used as opportunities for educating the public about investing. If the MCSD is able to conduct its important functions efficiently and free of scandal they may become one of the respected and well-known institutions in the investing community.

Recommendations

The MCSD and its public relations staff should be offered additional training in public affairs and advertising. They should be part of any strategic decisions made by the investment community about communications with the public.

6. Materials for the Public

A final element in the strengthening of the communication capabilities of the institutional partners that was examined by the evaluation team was the development and distribution to the general public of materials about the basics of investing. There were several different elements to this effort. The first was a series of four brochures that addressed the basics of investing.¹² The content of these booklets and the treatment of the information are suitable for the target group of educated and motivated potential investors. The purpose of the brochures is to convey information and facts about investing such as: What is a stock, bond or mutual fund? What is the stock market? How do I calculate my net worth? What are the aspects of securities research that I should know? Why should I diversify my investing?

There were 10,000 copies produced of each of the four booklets. They were distributed through ECMA that sent them to their institutional and individual members. These include the brokerage firms and many of their employees, insurance agents, accountants, executives in the banking industry and others. When the evaluation team visited ECMA's office we could see the benefits of the CMD early assistance to that organization. Computer workstations were operating and able to retrieve names and addresses of members. The database has been invaluable in making the distribution of these materials.

¹² "Introduction to Investing in Egypt," "Preparing to Invest," "Choosing Investment Instruments," and "Managing your Investments.")

The materials were also sent to the journalists who have been attending the press forums, training programs, etc. Several of the newspapers summarized these booklets in the financial sections of the daily papers, thereby increasing the distribution of the materials.

Another publication is "How To Read a Financial Statement," an Egyptian version of the well-known Merrill Lynch publication of the same name. Approximately, 10,000 – 12,000 copies of this publication have also been prepared. Like the Merrill Lynch publication, it has become popular with university business students and instructors. It is also being distributed under the name of ECMA.

Under development by CMD are "Guide to Corporate Finance" and a "Guide to the Egyptian Capital Market." Each will be about 65 pages and will have 5,000 to 10,000 initial circulation.

For the CMA, the project produced "A Guide to Minority Shareholders' Rights Under Egyptian Law." The Chairman of the CMA attributes the publication with an increase in the number of informed complaints made to the CMA in recent months.

Television is widely watched in even the smaller towns using cable and satellite feeds. Egyptian stations are owned and operated by the government. The project has tried, as have others in the investment community, to develop business programming that would reach this wide and affluent audience. However, the stations will only broadcast a five-minute segment on business news at the end of the evening news. No analysis is permitted nor the mention of any company name which according to the station managers would constitute advertising. This would cause the television company to charge the company for a mention of its name. That attitude by the managers constitutes a powerful barrier to access.

Nevertheless, the CMD has prepared several video segments in which government and private market participants are interviewed. Though the segments, or any part of them, could be used in broadcast television, the CMD plans to distribute these segments through ECMA to universities, schools and others. The segments' content and treatment is very similar to the brochures-informative rather than motivational and didactic rather than entertaining. As far as the evaluators could determine, the segments have not been tested with members of the target audience – university and high school students, or with members of the sponsoring organization – ECMA.

The effort that has gone into the design, production and distribution of the materials mentioned above is quite significant in the overall effort of the CMD. It remains to be seen how widely these materials will reach into the target audience.

Conclusion

When the evaluators visited the offices of ECMA, hundreds, maybe thousands of copies of the brochures were literally gathering dust in the office. The Executive Director of ECMA did not have any data on any requests for restocking by the brokerage firms and other members who may have been distributing these brochures to their clients. However, even if all the brochures were distributed and could be found in the offices of all the brokerage firms in the country, they would be reaching only the existing investors. Brochures such as these are durable, contain

messages that will be relevant for many months, but are very expensive materials. The video segments, if duplicated and widely distributed through the universities and high schools, community groups, used by brokers for educational lectures might achieve a mass audience of new investors.

Although the four brochures for the public were produced under the name of ECMA, its staff was not involved in the production of the materials. As far as the evaluation team was able to find out, the design and production were the work of the Project. This was a lost training opportunity for ECMA staff and board members.

The production and distribution of the brochures were an important effort by the CMD public affairs staff. However, the materials were not tested with the target audience prior to publication to test for acceptance, comprehension, persuasiveness, etc. Nor has there been any follow-up with participating institutions such as brokerage firms to assess the distribution, impact on clients, reactions by the brokers, and others. This should be an activity of the ECMA with guidance from the Project.

Television and radio - and perhaps cinema - remain unexplored and unexploited media resources. The costs of production are significant, but if access to the media is achieved the reach of the messages to the target audiences will be widespread.

The already prepared video materials will be useful in classrooms and in presentations before motivated audiences. However the text is dull and didactic and the presentation is soporific.

Recommendations

The CMD and the ECMA need to do research and thinking about the target group for existing and future public outreach programs. After discussions with several journalists, the publications staff of the CMD, leaders of three brokerage firms, and public affairs staff at the Institutional Partners, the evaluation team concluded that there was no clear understanding about the demographics of the target group. Out of the 12-15 million households in Egypt, perhaps there are 3-4 million that are potential investors. Where do they live? What newspapers do they read? Where do they invest? What about ages, income, education, media habits, authority figures - who would they believe if they became the public spokesperson on investing? The evaluation team believes that marketers of consumer products, credit cards, automobiles, etc. know the demographics of their target groups.

The CMD should consider the production, in collaboration with ECMA or other Institutional Partner of print materials that are less expensive and have the potential of reaching a wider audience. These might be distributed through banks (which are to become the custodians of securities), at the counters of the MCSD, education programs conducted at schools and other community institutions in up-scale neighborhoods, and "statement stuffers" for utility bills or communications from brokers and MCSD to their clients. The evaluation team did not have time to visit any radio stations to assess their usefulness in reaching this target audience.

A suitable investment of Project funds would be the study of actual barriers to broadcasting financial news and analysis via television. The evaluators heard several different stories about

why the government-owned stations would not broadcast education programs. In addition, access to the private cable stations should be explored.

Another investment of Project funds would be in providing training in mass communications for staff from the CMA and MCSD or board members of ECMA. Press relations staff from the CMA would benefit from an internship with the public affairs and education division of the Securities Exchange Commission.

7. Communication for the Brokerage Community

The evaluation team visited the ECMA offices, had a lengthy interview with the Executive Director, and visited the offices of three of the leading stockbrokerage firms in Cairo. The CMD has helped the ECMA acquire the equipment for training of its members that also could be used for seminars for the general public. It has also provided a workshop for ECMA members on training methods led by a CMD short-term consultant. The workshop was well attended at the outset, but attendance dropped by almost 50% by the program's end. The evaluation team did not find any assessment of the trainees' reasons for lack of attendance.

The interviews with the brokerage firms and with others that know the community confirmed the team's assessment that stockbrokers are essentially order takers. Moreover, in most firms they can offer clients only investments in individual stocks. There are practically no bonds traded on the exchange, except for institutional trades. Mutual funds are sold through banks or by a few brokerage firms that have their own funds. There are no money market funds and a new decree in January 2002 removed from the brokerage firms the ability to have custody of customers' securities. This will soon mean that brokers will not have an electronic record of their clients' holdings. Finally, new net capital adequacy rules for brokerage firms will result in a consolidation of the industry, eliminating dozens of small and marginal firms or the creation of a two-tier brokerage firm arrangement.

Conclusions

These formidable constraints are a challenge to the industry. If ECMA is to survive and increase in stature through SRO status, then it must be the leader in enabling the brokerage industry to change its vision for itself.

ECMA should take the leadership in the development of broker certification. This is the necessary first step to professionalization of the sales staff of brokers. The Series 7 examination conducted in the United States by the National Association of Securities Dealers (NASD) should be the model. As the products that brokers offer become more varied and complex, the need for training will be even greater.

A second step is to become a center of training for back office staff. At this time, there are no professional standards for minimum levels of record keeping and compliance procedures. ECMA could take the lead in this regard through collaboration with CMA.

Both organizations will be better served by a professionally trained sales and back office staff.

Recommendations

CMD should intensify its assistance to ECMA to develop its sources of funding, the strengthening of its staff, and its capabilities as trainer of trainers for its members.