Statement by Franco Passacantando  
Date of Meeting: July 3, 2001

**Egypt: Country Assistance Strategy**

We support the program as presented in the Country Assistance Strategy (CAS). We appreciate the effort to be selective and to find an appropriate mix of lending and non-lending services.

**Lending scenarios**

The base case, which envisages a lending program of US$450-500 million, is well designed, and in particular we welcome the focus on capacity building rather than on lending. The high case of a US$1.5 billion program appears quite unrealistic on the basis of the recent fiscal performance. We would appreciate further elaboration by Staff on how this large amount of resources would be utilized since no indication is being given except that the resources would be provided mostly through fast disbursing loans. Alternative lending scenarios should be set up taking into account realistic figures and should incorporate feasible and well-defined lending operations.

The report states that the Government has explicitly requested that all new operations should have a grant component of at least 40 percent. We would appreciate further explanation by Staff on: the rationale and feasibility of this “40 percent rule”, particularly in the high case scenario; whether this rule might have an adverse impact on the choice of lending operations and on the effectiveness of the overall strategy; and what are the sources of the grants.

**Triggers**

The proposed Bank program includes a specific fiscal deficit trigger, which calls for a gradual decline from a level of 4.4 percent of GDP in 2001. This level appears quite optimistic looking at the latest projections which point to the possibility of the deficit reaching closer to 5 percent of GDP. In this regard, we wonder whether the starting point is worse than expected at the time of the distribution of the CAS report and what the implications are for the proposed fiscal trigger. Given the vulnerability of the Egyptian economy, we think that compliance with the fiscal deficit requirement is crucial to prevent a deterioration in the confidence of the financial markets.

The key structural challenge now facing Egypt is to find ways to raise the rate of economic growth and employment and to alleviate poverty. Hence, we would have liked more specific triggers relating to steps to foster private sector activity and investment, to enhance the outward orientation of the economy, and to strengthen the financial sector.
We believe the completion of the Poverty Assessment – as a joint product with the Government – should be included as part of the Base Case triggers. A better understanding of the nature and incidence of poverty in Egypt is one of the prerequisites for a larger lending role by the Bank.

**Poverty alleviation**

It is indeed difficult to evaluate the impact of the recent high economic performance on poverty reduction due to the lack of a systematic assessment of poverty trends. However, the latest data does show that the incidence of poverty remains widespread across regions and society. Some social indicators, such as literacy rates, infant mortality and access to health services, have not shown any significant improvement. Gender disparity remains also very wide; particularly in education the progress has remained unevenly distributed across gender lines. While we welcome the fact that that the Poverty and the Gender Assessments are expected during FY02, we regret that the preparation of the Bank Group Strategy could not benefit from such crucial analysis.

**Specific structural aspects**

**Private sector and privatization.** Since 1994 only a third of the core privatization program has been implemented. Progress in this area is of fundamental importance to help the economy recover from the slowdown recorded in the last two years and to avoid an increase in unemployment.

**Financial sector.** Notwithstanding recent improvements in the financial sector, further efforts to lower intermediation costs and to strengthen regulation and supervision are needed. Also, an efficient banking system is crucial to support the development of SMEs. Further strengthening of the financial sector is also key to lower the country’s vulnerability to external shocks. We welcome that the FSAP is expected to be completed during FY03. However, we wonder whether the Government has in fact confirmed its interest in participating in the FSAP and we strongly urge that this work be anticipated to FY02.

**Governance.** To foster private sector participation in the economy it is necessary to create a supportive business environment that also involves changes in the legal and regulatory framework – including reforming corporate law, investment laws, the securitization system, as well as promoting appropriate investment incentives in the most disadvantaged areas.