PROJECT INFORMATION DOCUMENT (PID)
APPRAISAL STAGE

Report No.: PIDA988

Project Name	EGYPT Energy/Social Safety Nets Sector Reforms Technical Assistance (P144305)
Region	MIDDLE EAST AND NORTH AFRICA
Country	Egypt, Arab Republic of
Sector(s)	Other social services (35%), General energy sector (65%)
Theme(s)	Other public sector governance (35%), Infrastructure services for private sector development (35%), Social safety nets (30%)
Lending Instrument	Specific Investment Loan
Project ID	P144305
Borrower(s)	Arab Republic of Egypt
Implementing Agency	Ministry of Energy and Electricity
Environmental Category	C-Not Required
Date PID Prepared/Updated	30-Apr-2013
Date PID Approved/Disclosed	22-Mar-2013, 01-May-2013
Estimated Date of Appraisal Completion	28-Mar-2013
Estimated Date of Board Approval	24-Jul-2013
Decision	Project authorized to proceed to appraisal.

I. Project Context

Country Context

1. As a consequence of the January 2011 revolution, Egypt is undergoing major political, economic and social transformation. Socially inclusive economic development, job creation, poverty, transparency, citizen participation, and governance have come to the forefront of the political and social debate. Experience in other countries suggests that such a transformation, fraught with significant risks and uncertainties, may unfold over a relatively long period of time and that external assistance, supporting a transformational reform agenda, can yield significant social and economic returns.

2. Two years after the revolution, Egypt is still suffering from weak economic activity. Growth remains subdued with Real GDP increasing to 2.2 percent in fiscal year 2012, up only marginally from 1.8 percent the year before. Unemployment is on the rise, at 13 percent in by end of 2012, and social unrest is brewing with frequent strikes and protests. The balance of payments position is highly vulnerable. International reserves declined to US$ 13.4 billion in March 2013 (21/2 months below projected imports of goods and services), representing a loss of more than US$ 30 billion of foreign reserves since the revolution. Large fiscal pressures persist.

3. Public finances deteriorated sharply in FY12 pushing general government debt to over 80 percent of GDP. The overall budget deficit in FY12 reached 10.8 percent of GDP. The higher deficit originates from lower than expected tax revenues due to weak growth as well as higher spending on salaries, pensions, and fuel subsidies. Meanwhile, investment spending declined. The exchange rate has depreciated by about 10 percent since the central bank introduced foreign auctions in late December 2012 and a black market has emerged in response to central bank foreign exchange rationing and regulation.

4. The original budget for FY13 envisaged a decline in the deficit to 7.6 percent of GDP mainly on account of reductions in subsidies for energy products including electricity, LPG, gasoline, diesel fuel, fuel oil, and natural gas, but the budget overrun from last year and the delays in taking adjustment measures implies that the original target is no longer feasible. Fiscal deficit is therefore continuing to increase and may reach 12 percent of the GDP in FY13 absent of strong measures.

5. The Government has been working on containing the economic and fiscal crisis engulfing the country and the deteriorating public services including nationwide power cuts, chronic fuel and water shortages, suffocating traffic and accumulating trash in the streets. More recently, under the pressure of increasing macroeconomic imbalances and the need to seek exceptional balance of payments and budget financing, the Government has developed programs to tackle the legacy of huge energy subsidies that have distorted the economy and led to an unsustainable fiscal situation.

Sectoral and institutional Context

Sectoral and institutional Context

Egypt's total primary energy demand has grown at an average annual rate of 4.6% during the last two decades. This rather high growth is due to the country's economic expansion, industrialization, population growth and change in people's life style. Although all energy forms have been subject to rather high growth, electricity consumption has increased substantially causing serious concerns about the power sector's fuel requirements and an excessive burden on the government budget.

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Oil and Gas Sector

Egypt had a significant level of oil export through the 1980s and 1990s. Total oil production has declined since the country's 1996 peak of about 935,000 barrels per day (bbl/d) to current levels of about 685,000 bbl/d, while domestic oil consumption has increased steadily absorbing almost all oil production since 2006. Egypt has, as a result, become a net importer of petroleum products. In 1976, the Egyptian General Petroleum Corporation (EGPC) was established as a holding corporation. It owns 12 public sector companies and shares in 58-petroleum companies with foreign partners. Over the last three years, EGPC has faced challenges in addressing Egypt's oil and gas needs due to increasing subsidies accompanying the growth in market demand. In 2002, EGPC's total debt stood at half a billion Egyptian Pounds (LE), but has since increased vastly to over LE 100 billion in 2012.

Natural gas has substituted oil both in domestic use and in export of energy. During the 1990s, Egypt made substantial new gas discoveries tripling its proved gas reserves. Gas production tripled from 21 bcm in 2000 to 61.3 bcm in 2010. The rise in gas reserves had led the government to promote the domestic use of gas (representing about 70% of production) and to seek export options

in the form of liquefied natural gas (LNG) and piped gas (representing about 30% of production). It successfully created a domestic market for gas with an estimated demand of about 50 bcm/year, built three LNG trains with a capacity of 17 bcm/year, and implemented the Arab Gas Pipeline system with an approximate capacity of 10 bcm/year.

Although domestic gas prices were low, the government offered international oil companies substantially higher prices in order to create the incentives necessary for upstream producers to develop existing reserves and explore for new gas reserves. Presently, the gas sector is experiencing a supply gap of up to 10 bcm/year. The government is considering importing gas in the form of LNG which would cost in excess of $10/MMBTU. While the economic cost of insufficient gas supply is well understood, the financial viability of a gas import proposition is questionable as long as gas is sold at the negligible price of $1/MMMBTU to the electricity sector, which accounts for about 60% of total gas demand.

Electricity Sector

The power sector's financial performance is in very poor condition. Over the years, the government has invested heavily in expansion of the supply capacity. Consequently, generation capacity doubled during from 2000 to 2010 reaching 24,000 MW, but this is still insufficient to meet peak load demand which is growing at 7 to 8% p.a. The investment requirement for this period was about EGP 46.5 billion ($8.4 billion). A small portion of the investment was undertaken by the private sector but the bulk of the requirements was funded by the public sector and implemented by Egyptian Electricity Holding Company (EEHC). The Government is the sole owner of EEHC and also the National Renewable Energy Agency (NREA) that is currently implementing a number of wind and solar power projects. Lenders to EEHC are concerned about its financial viability.

Power generation capacity includes 12% hydropower while the remaining 88% is based on subsidized natural gas and fuel oil. Reliance on fuel oil increases with shortage of gas supply. Recognizing the need to reform the sector, in the early 2000s, the Government reorganized and corporatized the power sector into EEHC. Generation, transmission and distribution assets were unbundled resulting in six generation companies, nine distribution companies and the Egyptian Electricity Transmission Company (EETC) - all of which are affiliated and controlled by EEHC. EETC operates the transmission system and is the single buyer and seller of electricity. The Electric Utility and Consumer Protection Regulatory Agency (EgyptERA) began operation in early 2002, but its authority falls short of an independent regulatory agency (it does not have the authority to set tariffs). Private sector investment in generation is limited to three Independent Power Producers (IPPs) developed in the 1990s. Despite these initial reform steps, the reform process significantly slowed down as it approached the financial, governance, management and operations performance of the power sector and its utilities.

A new electricity law was drafted in 2008 and approved by the Cabinet of Ministers, but was not presented for Parliamentary ratification. The draft law is expected to be presented for approval during 2013/2014 session, after the new Parliament is elected around September/October 2013. The draft electricity law was designed to allow significant changes in the electricity sector market structure, governance and operations and in how the sector is financed and electricity is supplied to consumers, including emphasis on the development of renewable resources and energy efficiency.

Subsidy Reform

Energy subsidy reform is essential for Egypt because it is no longer the plentiful oil and gas producer and is facing an unsustainable fiscal deficit. Since the 2005-2006 fiscal year, the first time in which subsidies for oil and gas products were accounted for in the budg et, subsidies increased from LE 40 billion (about US$ 7.2 billion) to LE 66 billion (about US$ 11.8 billion) in the 2009-2010 fiscal year and hiked even further to LE 95.5 billion (about US$ 16 billion) in 2012. Recognizing the budget burden of fuel subsidies, the Government recently developed a program aimed at reforming electricity tariffs and fuel subsidies. This program was designed to be implemented in two phases: first phase has been fully implemented, while phase two is under development and is expected to begin later in 2013.

Social Safety Nets

Reforming energy subsidies should go hand-in-hand with reforming Egypt's social safety nets (SSN), whose consolidation is needed for providing better protection to the existing poor and vulnerable families as well as to mitigate adverse impacts of energy subsidy reform. Subsidies reforms pose formidable challenges as the proportional adverse impact of energy subsidy reform is expected to be the greatest for the poor, even though the rich receive the highest share of the subsidy. According to the results of the recent household surveys, energy subsidies represented over 12 percent of household expenditure for the bottom quintile, while the corresponding percentage for the top quintile is less than 9 percent.

The current social safety net (SSN) programs, including the main cash transfer program called Social Solidarity Pension, have many weaknesses, including fragmentation and poor coordination; low coverage of the poor; weak links to promotion of human capital; low poverty impact; and social and economic inefficiency. Beyond economic rationale, there is also political and social pressure for the new government to deliver on the promises of the 2011 revolution. A recent opinion survey shows that Egyptians' satisfaction with their government efforts to help the poor are among the lowest in the region, while the need for government services is among the highest

There is now a strong conviction that the government cannot afford to continue providing energy subsidies at the current level. This in turn converts the electricity and gas sectors into financially unviable businesses based on the prevailing prices of electricity and gas.

The government is very keen to prepare a transformative plan that comprises three interrelated tracks: (i) reforming energy subsidies through a coordinated program of price adjustments; (ii) moving away from a subsidized public supply of electricity and gas to a public-private supply that would operate on commercial basis with transparent and targeted subsidy when and where needed; and (iii) putting in place a social protection scheme that would protect the vulnerable groups of the Egyptian population. These tracks of transformation would need to be prepared and implemented in a well-designed, consistent and calculated manner and as such this proposed technical assistance will be supporting.

II. Project Development Objectives

The proposed project will strengthen the Government of Egypt's capacity to (i) design a comprehensive fuel subsidy reform strategy, (ii) establish concrete measures for improved financial viability of key energy sector actors and (iii) identify households that would be most vulnerable to the impacts of the fuel subsidy reform.

III. Project Description

Component Name

Power Sector Institutional Development and Financial Viability
Energy Pricing and Fuel Switching Reform Technical Assistance
Strengthening Social Safety Nets Technical Assistance

IV. Financing *(in USD Million)*

Total Project Cost:	6.50	Total Bank Financing:	0.00
Total Cofinancing:		Financing Gap:	0.00

For Loans/Credits/Others	**Amount**
Borrower	0.00
MNA VPU Free-standing Trust Funds	6.50
Total	6.50

V. Implementation

The proposed technical assistance will be submitted by the Ministry of International Cooperation for financing to the MENA Transition Fund. The Implementing agency of the technical assistance Grant will be the Ministry of Electricity and Energy.

A multi-sectoral Project Steering Committee (PSC) has been established before the project l to provide strategic direction for the technical assistance and support, coordinate and make resources available for implementation of its components with various line ministries, government authorities and national programs. The PSC will monitor the implementation progress according to semi-annual progress reports prepared by the Project Coordinator, approved by the PSC, and submitted to the World Bank. The PSC will also recommend to the line ministries and government authorities implementation of recommendations and sector strategies that would be developed by the technical assistance.

To ensure timely and efficient project implementation, the Government of Egypt has also appointed a Project Management Team (PMT) headed by a Project Coordinator (PC) who will be the key interlocutor for the Word Bank team and for coordinating the implementation of TA activities with the PSC, line ministries and government authorities. The PMT comprises the technical leads of the technical assistance subcomponents, Procurement Officer and Financial Officer who will be responsible for handling in accordance of World Bank procedures and guidelines all aspects of the financial and procurement issues related to the technical assistance project.

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VI. Safeguard Policies (including public consultation)

Safeguard Policies Triggered by the Project	**Yes**	**No**
Environmental Assessment OP/BP 4.01		×
Natural Habitats OP/BP 4.04		×
Forests OP/BP 4.36		×
Pest Management OP 4.09		×
Physical Cultural Resources OP/BP 4.11		×
Indigenous Peoples OP/BP 4.10		×

Involuntary Resettlement OP/BP 4.12		×
Safety of Dams OP/BP 4.37		×
Projects on International Waterways OP/BP 7.50		×
Projects in Disputed Areas OP/BP 7.60		×

VII. Contact point

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