PCSU

PRIVATIZATION COORDINATION SUPPORT UNIT

The Results and Impacts of Egypt's Privatization Program

Special Study

August 2002

Provided to the
United States Agency for International Development
by
CARANA Corporation
under the
USAID Coordinating and Monitoring Services Project
Contract # PCE-1-800-97-00014-00, Task Order 800

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I. Summary and Conclusions

A. INTRODUCTION

This Special Study, the last in the series undertaken by the Privatization Coordination and Support Unit's, assesses the overall impact of the Privatization Program in Egypt. The study focuses on the industrial and trade Public Enterprises (PE's) organized under Law 203, since privatization activities in the 1990's to date have largely addressed these enterprises. State owned banks and insurance companies, infrastructure and utility service entities, energy, military, local government and joint venture companies, have not been included, largely due to very limited privatization activity in these spheres.

The study assesses the impact of privatization of the Law 203 companies at three levels:

- Macro-economic impact, focusing on results relative to the principal objectives established by the Government for the Privatization Program
- Firm level impact, including corporate restructuring, financial performance, and employment
- Sub-sector level impact including competition, public and private sector market share, and implications for consumers/end users and upstream suppliers.

This assessment is based largely on existing data and secondary literature, supplemented by interviews and data gathering at the Public Enterprise Office, enterprises, and other official Government and international organizations.

B. THE HISTORICAL AND ECONOMIC CONTEXT

1. Evolution of the Public Sector Role in the Economy

After the revolution of 1952, the Egyptian Government began to play an increasingly active role in the economy by nationalizing private business, directly investing in productive and service ventures, and controlling and monopolizing many economic sub-sectors. Whereas in 1952, the private sector accounted for 76% of investment, over the next several decades the government accounted for 80-90% of all investment. By the early 1970's, all but small-scale enterprises and agriculture were controlled and owned by the state.

The Open Door or *Infetah* policies that began in 1974 were intended to revitalize the economy with more private, and especially foreign investment. This spurred a decade of growth, at least partly due to private-public joint venture enterprises, but registered as private companies. The economic dominance of the public sector continued, in 1990 accounting for 37% of GDP, 55% of industrial production, 80% of international trade and over 90% of the financial sector, and with strategic monopolies and heavy government regulation of most sectors.

In 1986 Egypt began to experience serious macroeconomic imbalances and a dramatic fall in growth. Serious fiscal and productivity consequences were characterized by budget deficits of 17% of GDP and very high balance of payments deficits. The average return on capital on the state's investment in the economy had decreased to 5.9% by 1989, at a time when inflation was about 15%. In 1991, Government embarked on a major program of market oriented economic reform and liberalization, in concert with significant financial support from international donors, with privatization as an important feature.

2. The Privatization Program

The Privatization Program started in earnest with the passage of Law 203 in June 1991, further corporatizing public enterprises, with shares held on behalf of the government by 27 holding companies to which the PE's were allocated on the basis of specialization or industry sub-sector. 314 companies were to be privatized while 85 were excluded from the first phase. At this point, 56 enterprises were considered loss making (the rest considered profitable under prevailing accounting practices) and in 1990, the total portfolio showed a profit of LE1.2 billion. However, accumulated losses were LE2.4 billion and total debt was LE47 billion.

The 314 companies to be privatized had assets of about LE68 billion and revenues of over LE60 billion. Employment in the PE's was slightly over one million, representing about 6% of the work force in the early 1990's.

The program started slowly in 1993, but then accelerated until 1999. Since then the number of transactions has slowed down. As of June 30, 2002, 190 of the 314 Law 203 public enterprises had been partially or majority privatized as follows:

Majority Privatization (>51% sold)	Number of firms
Anchor investor	28
Majority IPO's	38
ESA	34
Liquidation	32
Total	132
Partial Privatization/Leases	
Minority IPO's	16
Asset sales	21
Leases	20
Total	57

The remaining Law 203 portfolio has about 185 companies with revenues of about LE33 billion (in 1999/2000) assets of LE61 billion, and about 450,000 employees. 31 of 175 companies with data account for over half of the revenues and assets. The portfolio as a whole shows a net income, but the accumulated losses of the unprofitable companies continue to accumulate.

C. IMPACT OF PRIVATIZATION

1. Macro Level Impact

The Privatization Program began as one of the corner stones of a much broader macroeconomic reform and structural adjustment program (ERSAP). As the indicators attest to, the Program made considerable positive contribution to the government's adjustment and restructuring. The same indicators also point out that without the Program the scenario shows that the government's ERSAP task would have been more difficult and its economic and fiscal achievements made more uncertain.

At the macro level, impact has been assessed relative to the 4 principal objectives established by the Government at the outset of privatization.

- *Reduce size of the fiscal deficit*. Privatization had a very positive impact given that LE14.7 billion in sales proceeds have been collected and LE6.6 transferred to the budget. Since cumulative government fiscal deficits amounted to LE60.5 billion between 1992/93 and 2000/01, the amount transferred amounts to about 10% of the total. The fiscal benefits of privatization were undoubtedly larger through higher taxes from more profitable privatized companies and reducing the debt of remaining public enterprises, but this is impossible to exactly quantify. In addition to the above proceeds, under its assistance programs (SPR, DSP and APRP), USAID made direct disbursements of US$ 321 million to the government between 1995-2002 as privatization program benchmarks were achieved.

- *Improve efficiency in the use of government assets/resources*. In principle, both the transfer of assets to the private sector (.4% of GDP per year) and no further government investments in Law 203 enterprises, should release resources for social services and private investment. However, Government investment between 1992/93 and 2000/01 in Industry and Mining amounted to LE7.7 billion, in Agriculture and Irrigation to LE21.4 billion and construction and Infrastructure to LE 70.4 billion. The consequence is that the public sector remained at about 37% of GDP.

- *Access to markets and technologies*. Direct foreign investment and exports are seen as key indicators. In the case of DFI, 11 anchor sales generated LE4 billion through the purchase price plus additional investments in restructuring the enterprises. This represents a significant part of total DFI flowing into Egypt of between $800-11,500 million per year. However, privatization did not did not generate enough new DFI for Egypt to increase its market share of worldwide DFI going to developing countries. It also did not lead to increased exports.

- *Broadening of ownership*. IPO's and ESA's, as would be expected were particularly important in broadening ownership of companies. There has been some consolidation of ownership through secondary trading, but this is a positive trend since high fragmentation of ownership allowed the Holding Companies and state-owned financial institutions to retain the largest single block of shares in many companies, thus limiting restructuring.

2. Firm Level Impact

In assessing impact at the enterprise level, the focus is on how they have performed under private ownership, and whether they have performed better or worse than they would have under continued state ownership and management. The assessment also considers whether performance varies by privatization approach (e.g. anchor investor, IPO and ESA).

Since most enterprises have been sold in the past few years, it is difficult to draw definitive conclusions, especially regarding financial performance, especially if the enterprises need deep restructuring, a process which can take several years before showing positive financial results. In this assessment, particular emphasis has been given to the extent of corporate restructuring taking place as an indicator of short term firm level impact. The assumption is that new and active management is required for the privatized enterprises to perform better under private ownership than they would have under state ownership.

The analysis demonstrates that:

- Only some of the privatized companies have undergone significant restructuring, and these have mostly involved anchor and/or foreign strategic investors. In cases where the state has remained a significant player (through its residual shares or close relationship with ESA's that have not finished paying for their shares), restructuring has been limited.

- Privatization has generally had a positive result on financial performance, while having very little impact on employment in privatized companies. However, capital expenditures have been limited.

- The corporatization and commercialization brought about by Law 203 has had a positive impact on the performance of state enterprises. With the assistance of an early retirement fund, these have managed to reduce overall employment by half, while managing financial results almost as good as the privatized firms.

3. Sub-Sector Level Impact

Prior to the privatization program, the Egyptian economy was characterized by many sub-sectors in which economic activity was monopolized by public sector enterprises. Since a market economy is based on the principle that competition is the "invisible hand" that promotes efficiency and innovation, neither public sector nor private monopolies can be viewed as positive. Thus, an important test of the impact of privatization is to assess the extent to which both transactions and government policies have contributed to increasing competition, facilitating entry to new companies, and enhancing overall sub-sector dynamism.

Sector level impacts are among the most positive and lasting impacts of the privatization program in Egypt. In most sub-sectors, there have been new entrants, improved technology, expanded product range and availability, and in most instances, improved quality, distribution and service. This means that all Egyptian consumers and end-users of the goods and services involved benefit from privatization. Also, in many sub-sectors, there has been enhanced competition. The review found that the impact on prices were mixed. However, most price increases were attributed to improved product, service and availability than to liberalization.

D. IMPLICATION FOR FUTURE STAGES OF PRIVATIZATION

The principal implication of the impact assessment of the Privatization Program is that Egypt has much to gain and little to fear from continued privatization.

- From a macroeconomic perspective, the sale of the remaining Law 203 companies will not have too great an impact on the overall economy, considering that their revenues and employment represent a small percent of the total. However, more attention needs to be given to other parts of the public sector, especially considering that it remains 37% of GDP, including significant productive assets held by economic authorities, and other state owned entities.

- The remaining Law 203 portfolio, with exception of Pharmaceutical, Housing, Cinema and Tourism, largely consists of companies with declining revenues, high debts and bank over-drafts, and highly questionable future. Their assets are obsolete and have or reached the end of their economic life. The resources required to keep these companies in operation could easily erase the gains of the privatization program to date. Therefore, the divestiture of the remaining companies in the portfolio is urgent.

- Corporatization and commercialization of other public sector entities can have a positive impact, even without privatization, by forcing greater financial discipline. This has already begun in the civil aviation and electricity sectors.

- Privatization has the most positive firm level impact when followed by significant restructuring of management and operations. This is most likely to happen when one investor has majority control. Foreign investors are in the best position to provide additional investment and internationally competitive technologies.

- All Egyptians benefit from the improved services and products, and sometimes lower prices resulting from liberalization policies that encourage subsector competition, new entrants and innovation. The resulting expansion is likely to create more jobs than those lost through the privatization process.

This study has confirms many of the conclusions and recommendations reached in other studies, including several undertaken by PCSU/CARANA. The most relevant findings and recommendations of selected studies dealing with the urgent need for divestiture of the remaining Law 203 portfolio are presented in Appendix 4.

II. BACKGROUND

A. Introduction

This study documents the results and impacts of Egypt's privatization program activities during 1991-2001, as well as presents the impacts of privatization and liquidation, and the performance of the post-privatized public enterprises. The study is descriptive and quantitative in nature, supplemented with qualitative information obtained from secondary sources, previous studies, and interviews. The study synthesizes the rich material available on the privatization program, especially from the PEO, Ministry of Economy and Foreign Trade, other government institutions, the World Bank, IMF, ECES, and special studies and quarterly reviews by CARANA/PCSU on behalf of USAID. Interviews were conducted with the privatized companies, HCs and other relevant sources, and a number of factories were visited. However, there are serious limitations in the availability and quality of data. Thus, measurement of impact should be viewed as indicative of order of magnitude.

B. Emergence of the Public Sector in Egypt[1].

To fully understand the complexities and impact of privatisation in Egypt, it is important to understand it in its historical context. In July 1952, a pro-nationalist military coup led by a group of young officers from the Egyptian army over-threw the faltering monarchy and established a republic. Although the private sector was dominant in Egypt's economy under the monarchy[2], the state began to take an active part in the national economy after the Suez Crisis (1956).

The nationalization of the near century old Suez Canal Company in the summer of 1956, under law 285 of 1956, was followed by the nationalization of the majority of foreign economic assets operating in the country, as well as land, real estate and other economic assets owned by Egypt's private sector.

The Ministry of Industry created before the nationalization in July 1956 was established in order to expand and finance the public enterprise sector and to regulate private industrial projects. The sequestered foreign assets, which included a diversity of enterprises in banking, insurance, chemicals, cement, and textiles were placed under the administration of a newly formed government holding company, the Economic Development Organization (EDO).[3] This was also given control of other enterprises in which the state held shares. By 1957 the EDO was responsible

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[1] **Public Sector Defined.** The term 'Public Sector' is generally used for organizations that operate with government capital, whether national or local, and under all legal forms. Accordingly, the public sector includes infrastructure and services provided by central and local governmental agencies, such as education, health, electricity and transportation. In addition, the public sector includes units established by public capital whose activity contributes in achieving targeted economic and social development.

[2] There was little propensity for the government to promote industrialization and thereby lift society out of its state of backwardness.

[3] Law 60 of 1957 enabled the government to establish Economic Institutions with a mandate for the state to play an active role in economic development.

for a mixed bag of manufacturing concerns, which already represented around 12% of Egypt's industrial output. By 1960, as more public enterprises were established, EDO controlled 64 companies and was entrusted by the state to draw up Egypt's first five-year plan.

By 1964 the state owned or controlled most of the enterprises within the modern sectors of the economy as reflected in the following list:

- All banking and insurance, all foreign trade;
- All "strategic" industries, all medium to heavy industries, infrastructure assets such as the Suez Canal and the Aswan Dam, all major textile, sugar-refining and food processing plants;
- Most maritime and all air transport, all ports and port facilities;
- All public utilities and urban transport, modest public housing;
- Major department stores, some of the urban retail trade, hotels, cinemas and theatres;
- All newspapers and publishing houses;
- All reclaimed land, all irrigation canals;
- All major construction companies.

In 1960s the nationalized companies and newly created public enterprises were initially placed under the administrative responsibility of three giant state-owned holding companies, then re-organized under approximately 40 public holding companies. Each holding company was given managerial responsibility for a group of affiliate public enterprises engaged in a particular branch of economic activity.[4] Each holding company regulated its affiliate firms and was placed under the administration of a line ministry, which oversaw economic activity in its sector.

These new institutions did not practice economic activity on their own. They were considered as 'economic holding units' with affiliated public companies who undertook the economic activity. As the owner of capital, the institutions' role was to plan, monitor the achievement of targeted goals, and evaluate performance of affiliated companies, without interference in their operations.

The activities of the private sector during the period were limited to small and medium-sized enterprises in the industrial, agricultural and internal trade sectors, as well as sharing international trade with the public sector.

Many laws were passed to organize the public sector and designate its responsibilities. The most important were the following:

- Law 60 of 1964 concerning the organization of the general institutions.
- Law 32 of 1966 concerning the general institutions and public sector companies, which included a complete organization for the sector.

[4] The state would control around 500 public enterprises through this method of organisation in the 1960s.

- Law 60 of 1971 in which the public sector was transformed to the type of general specialized institutions, and every institution was dedicated to a certain type of production.

C. Size of the Public Sector

Among indications of the relative size and role of the public and private sectors in economic development before the start of the Privatization Program in 1991, the most striking factor is the relative amount of public to private investment.

The chart below shows that in 1952, the private sector had the largest share of investment, 76% of the total. By 1960, the beginning of the Five Year plan (1960-65), the picture had completely changed, and the public sector handled 94% of total investment. The public sector dominated until 1974.

Figure 1: Gross Capital Formation

	Public Investment		Private Investment		Total Investment
	Value	%	Value	%	(LE Million)
1952	28	24	87	76	115
1960	162	94	10	6	172
1966	349	93	28	7	377
1967	329	92	29	8	358
1973	426	92	37	8	463
1974	615	90	66	10	681
1982	4,000	80	950	20	4,950
1982/83	4,839	81	1,100	19	5,939
1989/1990	11,185	68	5,131	32	16,316

Source: CARANA, Quarterly Review, July-September 2001

The year 1974 witnessed the start of the "Open Door" policy (Infetah), which included many laws to encourage the private sector. The most important was law 43 of 1974 and its amending law 32 of 1977. It is worth mentioning that at the time, the public sector was undertaking almost 90% of total investment, versus 10% for the private sector.

By the end of the period from 1974 - 1983, the public sector was responsible for 81% of total investment, while the private sector share increased to 19%. By 1990, the public sector's share was 68% against 32% for the private sector, although of a much higher total.

By June 6, 1991, the total number of the public sector companies reached 500 which were responsible for almost 55% of industrial production, controlled 80% of total export and import activities and almost 90% of the banking and insurance sectors. In addition, it contributed around 40.6% of total national income. Its manpower reached 1.1 million workers representing 10% of total national manpower. Within the public sector, the public enterprise sector, consisting of some 400 industrial enterprises as of June 1991, was responsible for 10% of GDP, 6% of the labor force employing some one million workers, almost 55% of industrial output.

The implication is that while the Open Door policy contributed to an increase in the relative role of the private sector, in absolute terms the public sector continued to grow graphically. While private investment increased by a factor of approximately 130 times between 1974 and 1990, public investment still increased by a factor of 18 times the 1974 level (in current terms). A detailed breakdown of public and private sector investment development by sector is summarized below:

Figure 2: Breakdown of Public and Private Sector Investment

(LE Billion)				
	1983		**1992**	
	Public	**Private**	**Public**	**Private**
Investment				
Commodity Sectors[1]	2.48	1.9	6.18	6.8
Production Services[2]	1.8	.7	3.5	1.7
Social Services[3]	.8	.8	1.8	3.1
Value Added				
Commodity Sectors	5	7.5	24	41

D. Attempted Reorganization of the Public Sector During the 1970s and 80s

Initial attempts to improve the efficiency of public enterprises, while also encouraging private investment, involved several rounds of reassignment of responsibilities for the enterprises, rather than privatization or fundamental change.

Law 111 (1975) replaced all general institutions with 'supreme councils', which followed the same organization of the general institution, but with a higher degree of specialization.

In 1983, Law 97 was passed to cancel the Supreme Councils for sectors, and replaced them with public sector 'Organizations'. It defined the duty of the Organization to be planning, coordination and follow up of the approved goals for the sector, and was intended to give affiliated companies more management flexibility and independence.

These initial organization initiatives had little impact on the size or performance of public sector enterprises, as will be further reviewed in the indicators below.

The profit rate on invested capital decreased from 8% in 1975 to 5.9% in 1988, while the average interest rate in 1988 was around 14%.

[1] Commodities Sectors are Agriculture, Industry, Mining, Petroleum, Electricity & Construction
[2] Production services are Communications, Transportation, Suez Canal, Trade, Finance, Insurance, Tourism
[3] Housing, Social Services, Education, Health, Other Services

Debt and other financial burdens on the public sector had gradually increased. Debt in public enterprises increased relative to total invested capital, from 30.3% in 1975 to 74.3% in 1988. This led to aggregate losses over the period 1975 to 1988 of around LE 24.5 billion, with total debt reaching LE 80 billion by 1988.

As of June 30, 1991, 399 public enterprises showed:

The average profit rate on total invested capital was 6.39% at the end of FY1991, against 6.35% a year earlier. Moreover, the average of surplus/revenue of the companies declined to 6.5% at the end of FY1991, against 6.6% in the previous year.

The number of companies that suffered from financial difficulties reached 85 out of 399, representing 21% of the total companies. There were 62 loss-making companies out of 399, with 15.5%, with losses amounting to LE 630 million, while the accumulated losses in these companies reached LE 1,841 million.

III. PRIVATIZATION PROCESS

A. The Origin of the Ongoing Privatization Process

1. Egypt's Economic Crisis of the 1980s.

In 1991, the Government of Egypt embarked on an economic reform and structural adjustment program (ERSAP) designed to achieve macroeconomic stability, after recognizing that partial reforms of the early 1980's and the debt rescheduling of 1987 were insufficient. A number of economists have pointed to the fiscal crisis that Egypt was experiencing in the latter 1980s as the main factor underlying the government's decision to engage in comprehensive economic reform. The main elements of Egypt's economic crisis of the late 1980s can be summarized as follows:[5]

- Foreign debt grew from $20 billion to $49 billion in the 1980s
- A deficit on the balance of payments running at $11.4 billion
- A budget deficit of 17% of GDP
- Growth slumping to 2.5%
- Inflation hovering at around 20% annually
- Negative real interest rates
- Foreign exchange reserves covering only around three months of foreign exchange payments
- Official unemployment between 15-20%
- Declining GDP per capita incomes

[5] See Hans Lofgren; "Economic Policy in Egypt: A Breakdown in Reform Resistance?", in The International Journal of Middle East Studies, Vol.25 (3), August 1993, pp.410-11; and The World Bank, Implementation Completion Report, Arab Republic of Egypt, Structural Adjustment Loan, January 22, 1996, p.1.

Given the state of Egypt's economic woes, the international donor community was increasingly able to exercise leverage over the country's economic policymaking strategies. The IMF, the World Bank and USAID would increasingly push the Egyptian government to harmonize its policies with more concerted strategies of economic liberalization. It was largely due to these circumstances that Egypt entered into negotiations with the IMF in 1987 to attempt an agreement over economic reform. The reform package would provide the Egyptian government with a major credit facility to stabilise the economy but commit Egypt to a range of liberalisation measures. These would include:

- Macro-economic reform (anti-inflation measures, stabilization of current account and budget deficits, restoring the country's credit worthiness),
- Public enterprise reform (restructuring and privatization),
- Domestic price liberalization, and foreign trade liberalization.[6]

The fact that Egypt had experienced major social unrest when it flirted with IMF prescribed reform measures in 1977 made the government negotiate with caution. The government feared that price liberalization and the lifting of subsidies would result in significant material hardships for the bulk of the population and in turn threaten domestic stability. Many Egyptian officials also saw other reform measures, particularly privatization, as a threat to social peace.[7] Thus while the Egyptian government and the IMF engaged in several rounds of negotiations, it was not until May 1991 that an agreement on economic reform package was reached.[8]

The May 1991 agreements consisted of two separate arrangements with Egypt's donors:

- An agreement with the IMF comprising a stand-by credit arrangement (SBA) for $400 million to stabilize the economy.

- A second agreement with the World Bank (a loan of $300 million to support structural reform in the economy).[9] In addition, the World Bank

[6] For a fuller description of each of these reform measures, see The World Bank, Implementation Completion Report, Arab Republic of Egypt, Structural Adjustment Loan, pp.2-3.

[7] Their main concern was that privatization would make thousands of public sector employees redundant, severely increasing unemployment and further impoverishing the population.

[8] Negotiations between the Fund and the Egyptian government continued to break down during 1987-89. It was only after the 1990-91 Gulf War, when Egypt's donors rescheduled a large portion of Egypt's foreign debt in return for the Egyptian government's support of their campaign against Iraq, that an agreement was reached.

[9] The World Bank, Report and Recommendations of the President of the International Bank for Reconstruction and Development (World Bank) to the Executive Directors on a Proposed Structural Adjustment Loan in an Amount Equivalent to US$300 Million to the Arab Republic of Egypt, June 1991.

agreement accompanied further assistance of about US$260 million equivalent from ADB and EU.

- Continued support from USAID with greater focus on economic liberalization and privatization.

Public enterprise reform was identified as one of the key components of economic reform, and privatization, as both a reform mechanism and formal policy objective, was to be actively encouraged. The government's public enterprise reform program objectives were to:

- Reduce the size of the fiscal deficit;
- Improve the efficiency of public assets;
- Enhance access to foreign markets and technologies;
- Further deepen the ownership base.

An important motivation behind the privatization effort was to signal a change in the direction of economic policy. The private sector would be the new engine and stimulus of economic development and growth.

2. Adoption of a Concerted Privatization Program.

Although some Egyptian government officials had already advocated selling public enterprises during the 1970s and 80s, privatization, as a policy concept, was given strong momentum in President Mubarak's May Day speech in 1990.[10] In the speech, the President called for increased private sector ownership and management of the public sector.[11] The privatization program was proclaimed necessary due to a severe social crisis brought on by rapid population growth, and was to consist of:

- The sale of around LE 2.6 million of public sector equity in about 240 joint venture enterprises set up during the 1970s;

- The sale of around 2000 small enterprises belonging to local governments;

- The lease and/or sale of unutilized production facilities to the private sector;

- The removal of legal impediments to the sale of public sector shareholding in nearly 400 public enterprises controlled by public sector Law 97, which would hence remove the formal obstacles preventing their privatization.

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[10] In 1988, the Minister for Tourism and Civil Aviation, Fouad Sultan, actually succeeded in pushing through the privatization of three five-star hotels (the Sheraton Hurghada, the San Stefano in Alexandria, and the Meridian in Cairo) to strategic (Arab) investors. However, these transactions are seldom talked about within the context of Egypt's privatization experience and were met with widespread skepticism in political circles. All three hotels were sold largely as a result of Sultan's persistence rather than broadly formulated government policy. The transactions were concluded only after the investors had agreed to the government's conditions, particularly the investors' obligation to invest heavily in the hotels' refurbishment.

[11] The World Bank, <u>Report for the Recommendation on a Structural Adjustment Loan to the Arab Republic of Egypt,</u> p.19.

A high profile government symposium was held under the sponsorship of USAID in September 1990, building further momentum for the adoption of privatization. The Minister for Agriculture, announced his, and the President's, full support for privatization in agriculture during the meeting, as well as his own belief that only defense, railways, postal services and the energy sector should remain with the state. The Minister also declared his intention to sell all public agricultural companies. Other measures announced by the government to promote privatization further included the sale of 100,000 *feddans* of agrarian reform lands to their occupants, and the sale of shares owned by the Ministry of Industry in 32 state firms. However, while it appeared that privatization was supported by Egypt's highest political authorities, the program announced by the President was still devoid of an institutional base. In 1990 Egypt did not have an active capital markets and Law 97 still prevented state-owned firms from being sold to the private sector. Furthermore, three decades of state led economic development and bureaucratic controls deterred investors from contemplating buying into any state-owned firms slated for privatization.

3. Enactment of Law 203 in June 1991

Implementation of one of the provisions concluded as part of Egypt's agreements with the international donors, marked the start of the public enterprise reform program. The law focused on the industrial and trading companies of the public sector. It was designed to eliminate the difference in treatment and level the playing field between public and private enterprises, increase the management autonomy of public enterprises, and exclude them from the state budget. The second article of the law stipulated that 'holding companies' (HCs) would replace the 'Organizations' of the public sector, and 'affiliated companies' (ACs) would replace companies supervised by the replaced organizations.

A total of 314 public enterprises were companies legally restructured as Law 203 joint stock companies and was listed on Egyptian stock exchanges, thereby providing a clearance for their privatization, liquidation or bankruptcy. These were the enterprises that the Egyptian government had now slated for privatization. These companies were put under the control of initially 27, then 17, newly created government owned holding companies on the basis of specialization or industry sector. The holding companies, to be governed by private sector law, were mandated to maximize the present value of the state's portfolio of shares in each group of ACs and were allowed to sell public enterprises either in part or in full.

Under the administrative jurisdiction of the HCs, the managers of the ACs would be fully autonomous of the state in management decision-making and their official objective would be solely defined as profit maximization.[12] These legal reforms and subsequent physical reorganization of the public enterprise sector were a significant change from the previous regime, which

- Prohibited liquidation, bankruptcy and sale of the equity of government enterprises,

[12] The World Bank, Report for the Recommendation on a Structural Adjustment Loan to the Arab Republic of Egypt,p.22.

- Subsidized such enterprises through the state budget
  Gave Ministers a legal mandate by which to control them.

Law 203 further provided for the establishment of a new government apparatus, the Ministry of Public Enterprises that was designed to:

- Assist in implementing and monitoring the re-organization of the government's enterprises.
- Assist the holding companies in preparing their affiliates for privatization.

The public enterprise reform program was further supported by the promulgation of Capital Markets Law 95 of 1992. This law provided the legal framework necessary to stimulate the Cairo and Alexandria Stock Exchanges, which had been largely dormant since the mid-1950s. Details of the laws, decrees and government institutions relevant to and supporting privatization in Egypt are shown in **Appendix 1**. The Ministerial Privatization Committee decisions are shown in **Appendix 2**.

The balance of this report focuses on the results and impacts of privatization of Law 203 companies.

A. PACE OF PRIVATIZATION

1. The Initial Years of the Public enterprise reform and Privatization Program

During the initial three years of the privatization program (1993 to 1995), the pace of privatization was slow.

The government had set ambitious targets for the first phase of the privatization program, which included selling around 40% of the Law 203 portfolio, all public shares in joint venture banks, and one of the "big four" public banks. These objectives were clearly not being met. By 1995 some critics were pointing to the fact that the government would have to either sell or liquidate an average of just less than one public enterprise every week if the original privatization targets would be met by the end of the decade.[13]

Despite the slow pace of privatization, there were 31 majority and minority privatizations conducted through the end of 1995, including:

- 3 Law 203 companies sold to anchor investors in 1994
- 10 Law 203 companies sold to their employee stock associations (ESAs) in 1994-1995
- 10 liquidations of law 203 companies

These transactions represented just 8% of the total asset value of the Law 203 portfolio and earned the government around LE 5 billion in proceeds. In the mid-1990's, the public sector share as a percent of GDP remained at around 37%, and privatization had little impact on the overall composition of the economy.

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[13] World Bank, Arab Republic of Egypt: Economic Policies for Private Sector Development, p.137.

2. Acceleration of the Privatization Program

In 1996, the constitutional court upheld the right of the government to privatize the public sector. After this favorable legal ruling, the privatization program gained momentum, mainly through flotation of shares of public enterprises on the stock market. During the next five years of the privatization program (1996-2000), the Government of Egypt successfully privatized some 170 Law 203 companies.

The government conducted 6 initial public offerings (IPOs) on the Cairo Stock Exchange during the second quarter of the 1996, resulting in the privatization of three enterprises. Two of the companies, Nasr City Housing and The Egyptian Financial Industrial Company (EFIC), were high profile public enterprises and state monopolies in their respective – land development and fertilizer production – markets.[14] The transactions transferred a 75% ownership stake in each company to the private sector and signaled to the investors that privatization had really gained momentum in the country. During the following quarter the government aggressively accelerated its privatization program, privatizing another ten companies out of the twelve IPOs conducted between July and September 1996.[15]

The privatization program rapidly became wide-ranging in scope and encompassed a diversity of sectors of the economy, including:

- Food Industries: Misr Oil and Soap Company, and Al-Nasr Company for Dehydrating Agricultural Products;
- Housing and Construction: Development and Popular Housing Company;
- Engineering Industries: The Arab Company for Radio Transistors and Electronics;
- Cotton Trading: The Arab Ginning Company;
- Flour Milling: Middle and West Delta Flour Mills Company, Upper Egypt Flour Mills, and East Delta Flour Mills;
- Chemical Industries: Kafr Zayat Pesticides and Chemicals, and the Nile Matches and Prefabricated Wood Houses Company.[16]

The government was also diversifying its methods of privatization. Two more companies (Helwan Cement and Amereyah Cement) were sold through the IPO route during the last quarter of the year, while three firms (Al-Ahram Beverages Co., Al-Nasr Public Utilities and Civil Works and the Cairo Sheraton) were divested through anchor sales to strategic investors.[17]

By the end of 1996 the government had privatized 42 of its portfolio of 314 Law 203

[14] For a summary of the IPOs taking place in the second quarter of 1996, see IBTCI, Quarterly Review, USAID Privatization Project, Cairo, April 1 - June 30, 1996, p.3.

[15] IBTCI, Quarterly Review, USAID Privatization Project, Cairo, July 1 - September 30, 1996, pp.5-7.
[16] IBTCI, Quarterly Review, July 1 – September 30, 1996, pp. 5-7.

[17] IBTCI, Quarterly Review, USAID Privatization Project, Cairo, October 1 – December 31, 1996, p.4.

companies, a major turnaround on the pace of privatization during the previous four years of the program. Nineteen of these 42 transactions were completed during a nine-month period in 1996. The period 1996 to 1998 witnessed the privatization of 85 companies and production units. These 85 companies were sold at a value of LE8.548 billion.[18]

Privatization continued at a fast pace through 1999. A total of 137 Law 203 enterprises had been (majority and minority) privatized by the start of the year 2000, along with:

- Public sector shares in 21 joint venture industrial companies,
- 16 joint venture banks,
- 2 joint venture insurance companies,
- Various other entities.

B. PRIVATIZATION ACHIEVEMENTS

Figures 3, 4 and 5 below, show the number of law 203 companies that have been privatized, sales value and method of privatization on a year- by-year basis since the start of the program up to June 30, 2002.

Figure 3: Privatization Achievements: Transactions Summary to June 30, 2002

	Majority Privatization(>51% sold)					Partial Privatization/ Leases			
Year	**Anchor Investor**	**Majority IPO**	**ESA**	**Liquidation**	**Majority Total**	**Minority IPO**	**Asset Sales**	**Leases**	**Yearly Total**
1990				1	1				1
1991				3	3				3
1992				1	1				1
1993				1	1				1
1994	3		7	2	12	1			13
1995		1	3	2	6	6			12
1996	3	14		1	18	6	1		25
1997	3	14	3	3	23	2	1	2	28
1998	2	8	12	6	28	1	3		32
1999	9		5	7	21		4	8	33
2000	5	1		3	9		6	8	23
2001	3		2	2	8		3	2	12
2002			2		2		3		5
Total	**28**	**38**	**34**	**32**	**132**	**16**	**21**	**20**	**189**
Source: PEO	**Majority Privatization Total 133**					**Partial Privatization/ Leases total 55**			

[18] Khatab, Moktar, "The Egyptian Privatization Experience", Statement submitted by the government to the newspaper Al Ahram, October 8, 2001.

Figure 4:

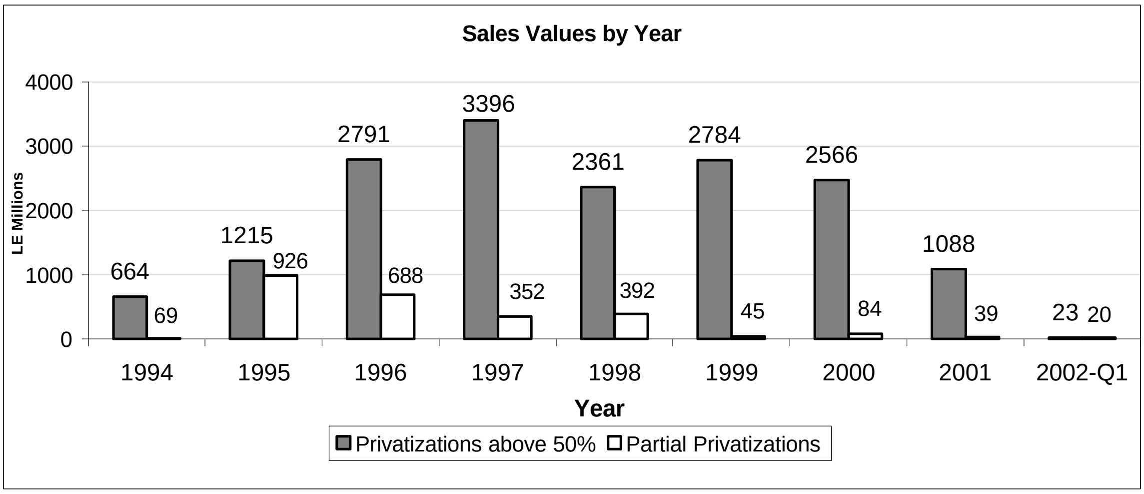
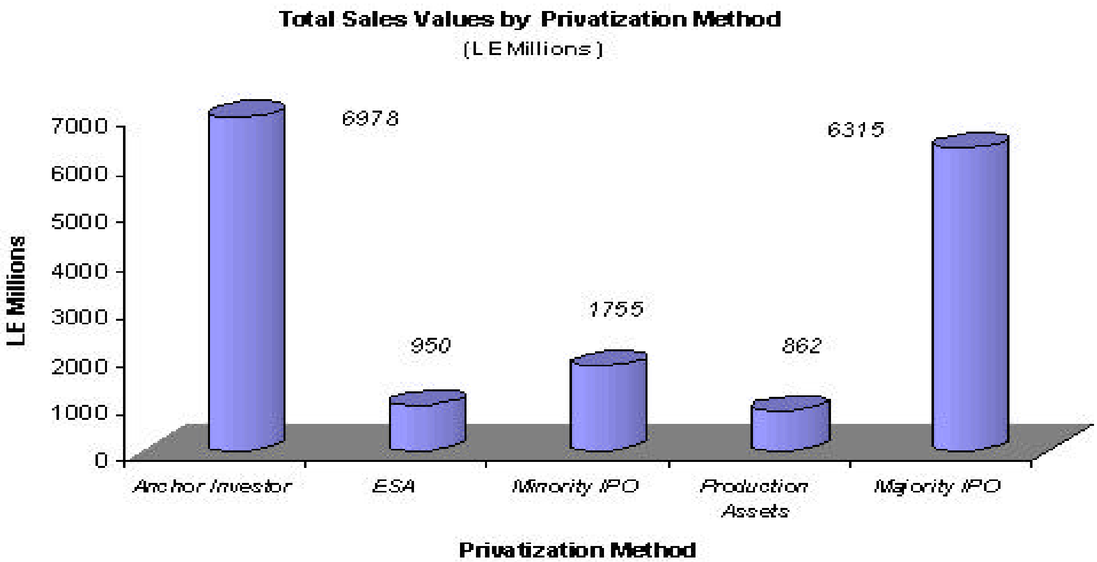


Figure 5:



An Adjustment in the Pace and Strategy of the Privatization Program

Since the late 1990s the Egyptian stock market has generally been in decline. As of year 2000, the government has reduced its reliance on the stock market as a central method employed in privatizing the remaining Law 203 companies. As shown in Figure 3 above, only one majority IPO privatization has been conducted during 2000-2002 (first 2 quarters), while sale to anchor/strategic investor became the preferred method. During the more recent stages of the program, the government seems to be shifting to reliance on anchor investor sales, as well as other methods of privatization, including asset sale and leases with option to buy.

It should also be noted that during the accelerated phase of the privatization program, most of the Law 203 firms privatized were medium-sized financially profitable companies that did not require restructuring prior to sale.

Privatization Program Summary

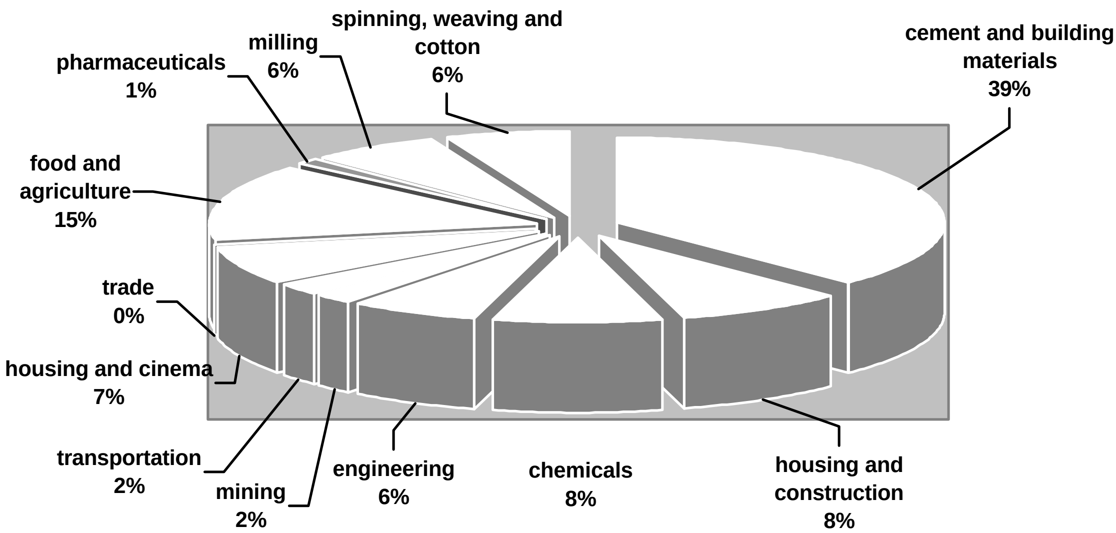
Below is the summary of the Law 203 privatization achievements. Details of transactions for each category are shown in Appendix 2.

- 133 Majority Privatizations and 55 Partial Privatizations
- 38 Companies sold through majority offerings on the stock market for LE 6.3 Billion
- 29 Companies sold to anchor investors LE 7 Billion
- 34 Companies privatized through sales to ESAs for a total of LE 950 Million
- 32 nonviable enterprises liquidated and their assets released to the private sector
- 16 Companies partially privatized via minority public offerings for a total of LE 1.75 billion
- 22 Leases implemented
- 19 Assets have been sold for a value of LE 862 Million

Privatization Activities by Sector

As for accomplishments on a sector basis, privatization of the cement sector and building materials sector realized proceeds of LE5.8 billion, representing 36% of total privatization proceeds through June 30, 2001. This was followed by the agricultural products sector, which privatized companies worth LE2.3 billion, representing 14% of the aforementioned sales proceeds. Figure 6 below represents pr Privatization of Law 203 Companies till June 30, 2001 by Sector.

Figure 6:

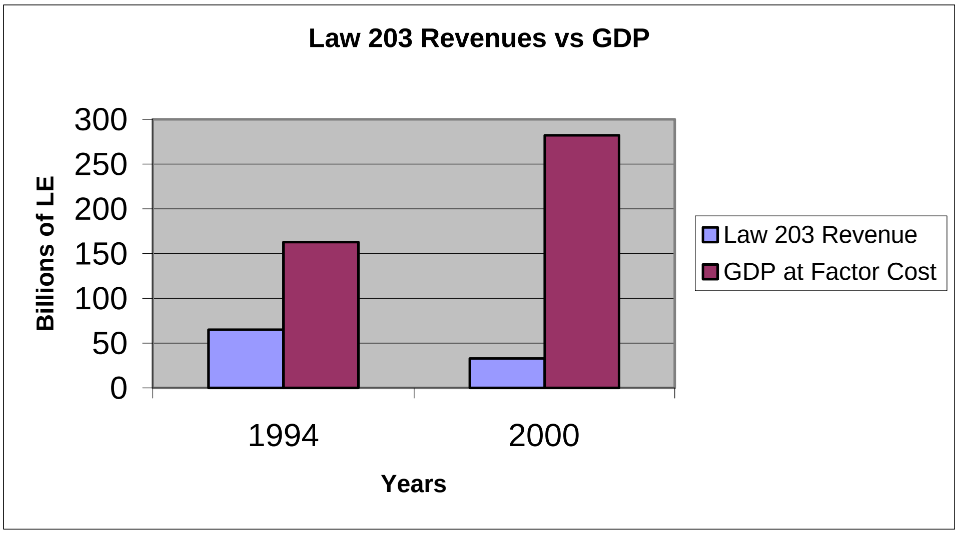


C. THE REMAINING PORTFOLIO AND ITS PERFORMANCE

Law 203 remaining portfolio (assets valued at LE 63.8 billion and total debt and other liabilities of LE 58.5 billion) has become significantly less important to the productive sector of the Egyptian economy. The GDP has grown; sector liberalization has brought new entrants and the revenues and sales of more than half the companies in the portfolio have declined. Consequently, with the exception of the Pharmaceutical, and Housing, Tourism, and Cinema HCs the overall asset quality of the portfolio is declining in income and revenue generation.

Figure 7 below shows the remaining portfolio has shrunk, especially relative to the growing GDP.

Figure 7:



There are about 185 companies remaining in the Law 203 portfolio. Many of these companies are unprofitable and in difficult financial position. 31 companies (out of the 157 with data) represent 56% of the revenues, 50% of the assets and about 35% of the labor force of portfolio's totals. Some 49 Law 203 companies have been recently categorized as "distressed" due to their continued loss making status. As shown in Figure 8 below the trend in recent years indicate that the number of loss making companies will continue to grow.

Figure 8: Percentage of Companies with Declining Revenues

97/98	98/99	99/2000
52%	63%	66%

As noted above individual holding companies have had significantly different performance. Three holding companies reported a net loss in 2000 while two reported healthy profit margins. Return on Assets ranges from –5% to 10%. Accounts receivable (uncollected bills) make up over half the assets in the

Construction Holding Company and over 40% at Trade and Housing, Tourism and Cinema HC's, raising questions on what part of the receivables are collectable and implications for profitability. Figure 9 below highlights the Holding Companies performance in comparison with each other and over time.

Figure 9: Key 2000 Holding Company Data

Holding Company	Net Margin	ROA	Current Ratio	AR/Assets	Salaries/Sales
Trade	-7%	-5%	1.2	45%	8.1%
Textile	-19%	-7%	.71	34%	26.6%
Pharmaceutical	10%	10%	1.8	29%	9.2%
Metallurgical	2%	1%	1	17%	20.5%
Maritime & Inland Transport	14%	7%	1	13%	20.2%
Housing, Tourism & Cinema	20%	8%	1.4	44%	10.5%
Food Industries	3%	4%	1.4	9%	9.3%
Engineering	-23%	-9%	1.2	26%	25.1%
Construction	8%	4%	1.3	54%	11.1%
Chemical	3%	2%	1.2	8%	12.7%

Source: CARANA Data Study

Many of the assets in the remaining portfolio have or are reaching the end of their economic life and large investments would be required to keep these companies operating. This is confirmed by various previous analyses that report that new capital investment has been minimal. Despite the decrease in the number of worker from about 1 million to half a million, the wage bill has dropped only slightly in current terms from LE 4.9 billion to LE 4.1 billion. The debt and interest payments, and bank overdrafts continue to escalate. In short, the remaining companies are increasingly difficult to sell and remain a substantial burden on the government's resources. As of 1998/99, accumulated losses in the losing companies were estimated to have reached Le. 10.3 billion, compared to LE 6.2 billion in 1992/93 when the portfolio was larger. On the other hand, the net profits of the profitable part of the portfolio was up from LE2.5 billion in 1992/93 to LE3.7 billion in 1998/99 (despite the smaller size of the portfolio).

It must be emphasized that the above profile refers to the remaining Public Enterprises in the Law 203, MPE portfolio. It excludes the joint venture companies, the financial sector (including joint venture banks, and the economic authorities, some of which are now being corporatized, and in effect represent additions to the Law 203 portfolio, even though not included among the firms to be privatized.[19]

IV. PRIVATIZATION IMPACT

The impact assessment is divided into three sections: macro, firm, and sector level impact.

A. MACRO-ECONOMIC IMPACT

At the broadest level, it is necessary to assess the impact of privatization in terms of what difference it has made to the overall economy. One way to look at the macro-economic impact is in terms of the Governments principal objectives in launching the current Privatization Program in 1991:

- Reduce the size of the fiscal deficit
- Improve the efficiency in the use of public assets/resources
- Enhance access to foreign markets and technologies
- Further deepen the ownership base

1. Reduce the Size of the Fiscal Deficit

Law 203 with both its commercialization of PEs and the sale of companies and assets has had a significant impact on reducing the burden and drain on the government's financial resources. Before the privatization program the PE' enjoyed, among other advantages, subsidies for losses, preferential access to credit, automatic government loan guarantees, negative real (ex-post) interest rates, subsidized exchange rates and trade protection.

On the fiscal side, privatization has played a significant impact in reducing the drain on the government fiscal resources of public sector losses. Privatization has generated a total of LE15.8 billion through September 30, 2001, of which the collected amount has been LE 14.7 billion. Almost half of the sales proceeds have gone to reducing the budget deficit, about a third to paying off enterprise debt, and the balance for labor compensation and early retirement schemes as shown in Figure 10 below.

[19] For example, the Egyptian Company for Civil Aviation and Egypt Air have both been reorganized as Holding Companies.

Figure 10:

Privatization Achievements: Collected Proceeds and their Utilization

(LE Millions)

Item	December 31, 2000	Activity Between31 Dec 00—30 Sep 01	Sept. 30, 2001
Total Collected Sales Proceeds:	13,100	1,569	14,669
Proceeds Utilization:			
Banks Debts Settlement	4,198	290	4,488
Early Retirement, Pensions and Salaries	2,440	243	2,683
Amount Transferred to the Ministry of Finance	5,822	806	6,628
Restructuring and Other	1,214	-660	5548
Total Proceeds Utilization	12,811		13,585
Balance of Restructuring Fund on September 30, 2001 307			

Source: Public Enterprise Office
Note: There have been two additional lease transactions since September 1991. However, the details of the proceeds and utilization are not available.

As reported by the Central Bank, in 1999/2000, the privatization proceeds provided about 15% of the financing required by the Central Government to cover its budget. In 2000/2001, privatization proceeds going to the Central Government financed only 3% of budget requirements.

Between 1992/93, and 2000/01, total Government deficits added up to LE60.5 billion. If the LE 6.6 billion of privatization proceeds had not been transferred to the Ministry of Finance, the deficit would have been LE67.1 billion. Thus, the cumulative fiscal deficit in these years was reduced by 10% through the sale of assets.

Most of the Law 203 companies sold through the ESA method after the first batch of ESA transactions in 1994-1995 have thus far generated very little revenue for the government. There have been 24 Law 203 companies privatized through the ESA method since 1994-95 (till end of first quarter 2002), with total sales value of these transactions estimated at LE 584 million (Carana Privatization in Egypt Quarterly Review, Jan 2002, p.30). However, the actual amount that the state has gained from these transactions is substantially less, as some of the ESA transactions took place on a credit/installment basis. The deposits paid by company ESAs ranged from 2 to 20%, and the transactions were based on the assumption that the remainder of the amount would be funded in the ensuing 5-10 years, during which time the privatized company would generate sufficient profits to ensure the repayment of its debt to the Holding Company.

However, the post privatization experience of the ESA transactions of 1994-95, where a positive financial performance has been witnessed in only a minority of cases, alludes to the fact that it may be difficult for the more recent batch of Law 203 companies privatized through the ESA route to adhere to the repayments schedule.

Examination of a sample of the results of liquidated companies shows that they carried substantial debts. The liquidation proceeds are used to pay off these debts. In the unlikely event that there are any funds remaining, these go to the Ministry of Finance. Although the holding companies maintain a record of Law 203 enterprises liquidated during the privatization program, there are no collated statistics available listing the total revenues generated from liquidations[20]. To date, however, and as might be expected, there has not been any surplus to transfer to the Ministry of Finance.

The net change in taxes paid as a result of privatization represents an important fiscal impact, but one that is almost impossible to accurately measure without a major effort and econometric model. It can be assumed that Law 203 companies pay more taxes after privatization, based on the fact that aggregate gross profits have increased since privatization. More importantly, sectors where privatized Law 203 companies were in, all have had some degree of liberalization. The result has been more companies in those sectors, expanded product range, upgrading of the technologies and service, and improved quality. The overall effect of these factors has been increased production, sales volumes and in many instances prices, thus more taxes paid. However, a complete assessment of the tax implications would require a complex model considering impact on personal income taxes and relationships with suppliers.

2. Improve the efficiency in the use of government assets/resources

By transferring assets to the private sector, the theory is that these will be more productively employed, and free the government to focus its resources on the services it can best provide. Figure 11 below gives an overview of Egypt's macro-economic indices the 1990s since the launch of the current privatization program. As can be seen, most of the indices are strongly positive. The question is to what extent can privatization be measurably seen as a contributing factor.

[20] Holding Companies maintain a record of the proceeds coming from liquidations, but they do not pass these across for filing at the PEO in any systematic manner. Furthermore, sources in the Egyptian government suggest that it is difficult to ascertain the total value of revenues generated from liquidations due to the fact that assets liquidated are so numerous, and will take substantial time to evaluate.

Figure 11:
EGYPT: Economic Indices—1995 to 2000
LE billion

Description	93/94	94/95	95/96	96/97	97/98	98/99	99/00
Gross domestic product at market value (LE billion)	175	204	229	256	280	302	339
Real growth rate for GDP (%)	3.9	4.7	5	5.3	5.7	6.1	6.5
Unemployment (%)	9.8	9.6	9.2	8.8	8.3	7.9	7.4
Average annual inflation rate	9.1	9.4	7.3	6.2	3.8	3.8	2.8
Total domestic savings as a percent of GDP	15.1	15	12.7	14.5	15.7	15.6	16.4
Total domestic investment as a percent of GDP	16.6	16.2	16.1	17.7	19.5	19.9	19.8
Nominal interest rate	12.0	10.1	9.5	9.8	8.8	8.82	9.09
Total external debt ($ billion)	30.9	32.9	31.0	28.8	28.0	28.2	27.8
Total percentage of external debt to GDP	59.9	54.8	45.9	38.0	34.0	31.7	28.3

The analysis presented in this report suggest that the sale of Law 203 companies has been a positive, but rather minor factor in relation to others. Most importantly:

- The value of privatization transactions has been the equivalent of 0.46% of GDP annually. This represents the percent of GDP transferred on an annual basis from the public sector to the private sector.

- There was virtually no Government investment in Public Enterprises after 1991/92 (LE3.9 billion), except for LE226 million in 1998/99 (as reported by the Central Bank).

- However, the Government made investments of LE 7.7 billion in Industry and Mining projects between 1992/93-2000/01, as well as LE21.4 billion in Agriculture and Irrigation, and LE70.4 billion for Infrastructure and Construction. Thus, it can be concluded that the investments previously made in Public Enterprises were channeled into other public sector entities and projects. This also helps explain why the public sector continues to represent about 37% of GDP.

The Firm Level and Sector Level Impact Sections of this report will indicate that commercialization and privatization have contributed to economic growth and performance, but especially through sector liberalization, price and trade deregulation. As can be seen in the following chapters, markets in many sectors have become more vibrant with new entrants, investments, improved technologies, and some enhanced competition.

3. Enhance access to foreign markets and technologies

Privatization has had mixed results in achieving this objective. Since foreign investors are in a particularly strong position to provide access to foreign markets and technologies, the level of direct foreign investment resulting from privatization is an important consideration. In Egypt, foreign investment has played a major role in 11 (out of 29) anchor sales (IPO's mostly involve portfolio investment), amounting to almost LE 4 billion. In addition, the foreign partners have invested additional resources into most of these companies, although the exact amount is impossible to quantify. For example, an additional $500 million in DFI is believed to have gone into the beverage sector alone.

The significance of the DFI in privatization can also be assessed in terms of total DFI flowing into Egypt.

Figure 12:	1993	1994	1995	1996	1997	1998	1999	2000
$million	493	1256	596	637	888	1077	1500	1,200
DFI/GDP	1.1	2.4	1.0	.9	1.2	1.3	1.6	NA
% DFI to LDC's	.8	1.4	.6	.5	.5	.6	.8	NA

Seen in this context, privatization has been responsible for a significant percentage of the DFI flowing into Egypt in recent years. It has not been sufficient to significantly increase the level of DFI as a percentage of GDP (thus stimulating broader economic growth) or of increasing Egypt's share of DFI going to developing economies. However, this must be attributed to the limited scope of the privatization program (e.g. only the Law 203 Public Enterprises) and Egypt's comparative/competitive position in attracting DFI.

Out of the 29 anchor investor privatizations listed by the MPE, 11 have involved sales to foreign strategic investors. These transactions are shown in Figure 13 below.

Figure 13:

Majority Privatized Companies to Foreign Anchor/Strategic Investors

Privatized Company	Foreign Strategic or Anchor Investor	Date of Privatiz ation	Country Origin of Foreign Investor	Value of Sale (LE M)
Al Nasr Bothing Coca	Coca Cola International	Apr 94	USA	286
Egyptian Botling Pepsi	Pepsi International	Apr 94	USA	131
El Nasr Boilers	Babcock&Wilcox	Sep 94	USA	16
Al Ahram Beverages	Luxor Group	Nov 96	USA	298
Al Wadi Export of Agri. Products	Egyptian Saudi Co.	Nov 98	Saudi Arabia	122
Nobarieya for seed Production	Egyptian Saudi Co.	Feb 99	Saudi Arabia	103
Delta Sand Bricks	Belina LTD	Jul 99	Greece	62
Beni Suef Cement	Lafarge/ Titan	Jul 99	France	527
Assiut Cement	Cemex International	Nov 99	Mexico	1,197
Alex Portland Cement	Blue Circle	Nov 99	United Kingdom	670
Ameriyah	Cimpor	Mar 02	Portugal	527
Total Sales value of FDI in privatization				LE 3,939
% Total as a share of Anchor investor total				57%
% Total as a share of total proceeds				35%

Source: S.Nasr World Bank Report, p.45/PEO

The 11 anchor/strategic investor transactions involving foreign investors accounted for almost LE 4 billion out of a total of almost LE 7 billion in sales proceeds for all of the 29 anchor privatizations. Anchor investor sales to foreign companies account for 57% of the total proceeds coming from anchor sales and 35% of total proceeds of the entire privatization program. Most of these cases has seen significant enhancements in technology.

4. Broadening of Ownership

The Privatization program has been quite successful in broadening ownership of the 101 majority privatized Law 203 companies as well as in 16 minority IPOs. The rationale for this Government objective is that broader citizen participation in ownership gives more people a “stake” in the market based economy. The ownership structure that has been emerging from the privatization program is characterized by the following:

- A higher concentration of ownership in most anchor investor privatizations, as would be expected since these involve selling a majority package of shares to one investor.
- A wide degree of ownership diversification in many of the IPOs to the point where the Holding Companies and/or public sector financial institutions have often remained the major single equity holder.
- Other public sector (mostly financial) institutions have acquired substantial ownership stakes in many of the IPO privatizations, limiting the extent of real privatization

- Over time, secondary trading of shares has led to a higher level of ownership concentration in several of the IPOs.
- Several major Egyptian private investor groups have acquired substantial equity in a number of privatized companies
- Foreign investment involves both direct foreign investment (especially in anchor privatizations) and portfolio investment (especially in IPO's) but the involvement of the latter is relatively modest
- 34 companies have been transferred to the ownership of their employees

Majority privatizations through IPOs have succeeded in broadening the ownership base of 38 former Law 203 public enterprises. In a typical privatization through a public offering, the equity holdings of public enterprises have bought by:

1. Investment and mutual funds,
2. Private individuals,
3. Foreign portfolio investment (which could include offshore Egyptian capital)
4. Non-MPE government institutions (mostly public sector financial entities)
5. Employees
6. Holding Companies

A number of these sample transactions are illustrated below:

1. Nasr City Housing

The Holding Company for BC	25%
A consortium of 40 foreign banks	11%
Mutual funds	10%
The Employees Stock Association	10%
Egyptian bank	11%
Egyptian insurance company	11%
Moroccan Investor	11%
Saudi Investor	5%
Egyptian individual	5%

Source: Nasr City Housing

2. EFIC

The Holding Company for Mining and Refractories	25%
The Employees Stock Association	10%
The National Bank of Egypt	9%
The Commercial International Bank and affiliates	8%
The Sayyad Group	7%
Free floating equity	33%

Source: Prime Securities S.A.E Research Report on EFIC

3. Kafr Zayat Pesticides and Chemicals

The Holding Company (2 Board Members, including the Chairman)	25%
Public Sector Investment Funds (2 Board Members)	22%

The Employees Stock Association (1 Board Members)	05%
Albert Dabaa, a pesticides trader from the private sector (1 Board member)	04%
The Sayyad Group (1 Board Member)	5-10%

Source: Kafr Zayat

4. Electro Cables Egypt

The National Bank of Egypt*	10%
The Sayyad Group	10%
The Misr Insurance Company*	10%
The Alem Group	05%
The Commercial International Investment Company (CIIC)	05%
The Employees Stock Association	10%
The Nile Development Fund	1.5%
The Public (free floating equity)	48.5%

Source: Electro Cables Egypt

- Denotes public sector entity

5. Middle & West Delta Flour Mills

The HCRFM (public sector)	39%
Misr Bank (public sector)	10%
Ahly Bank (public sector)	10%
Misr Insurance (public sector)	10%
The Employees Stock Association	10%
Free floating equity*	21%

HC for Food Industries

6. Nasr Dehydration Agricultural Products

Thoulathia Group	54.3%
Falcon Group	32%
ESA	10%
Individuals	3.7%

Source: Carana

7. Giza Contracting

HC	20%
ESA	10%
Mutual Funds	9%
National Bank of Egypt	5%
Bank of Alexandria	4.2%
Private Investors	51.8%

Source: Carana

8. Telemisr

Sorour and Magowi	55%
The Employees Stock Association	10%
The Public	35%

Source: Telemisr

It is impossible to quantify the amount of foreign investment in the IPO privatizations since there is no published data that details the ownership structure of the 38 Law 203 companies majority privatized through the capital markets. However, some evidence does exist of foreign investor participation in Egypt's

IPOs, particularly during the stock market boom of 1996. The government's first majority offering of a Law 203 company on the stock exchange, Nasr City Housing, caught the attention of numerous foreign investment funds, as well as a number of private Arab investors.

Of the 37 other majority and 16 minority privatizations conducted through the Stock Exchange, it is quite safe to assume that the bulk of investment into these companies was sourced from Egyptian capital.[21] Out of these privatized companies, the ownership structure of just two – Simo for Paper and Misr Free Shops Company, lists the participation of foreign investment as a result of the IPO:

SIMO's Ownership Structure after the Privatization

The Diyya Group	48%
The Khorafi Group	22%
The HCCI	15%
The Employees Stock Association	10%

Source: Holding Company for Chemical Industries

Misr Free Shops Ownership Structure after the Privatization

Al-Zidi Group	35%
Public enterprises and public sector banks	13.5%
Private sector investment funds and banks	13%
Foreign banks/investment funds/individuals	12.6%
The Employees Stock Association	10%
The public (free floating equity)	16%

Source: Egypt Free Shops Company: Information Memorandum

Anchor transactions have tended to lead to the creation of a concentrated ownership structure in the resulting privatized companies. As can be seen through the ownership structure of the four companies below, a solitary investor group has succeeded in taking control of more than 51% equity in each company. This has helped pave the way for the new majority shareholders to appoint new management teams and lead to substantial operational restructuring. Concentrated ownership has led to the total corporate transformation of several of Egypt's former public enterprises sold off to anchor/strategic investors, including Al Ahram Beverges, Assuit Cement, and to a lesser extend, Ideal.

1. Kahromica

Arab International Construction	51%
Abdel Rehim Hussein	10%
HC	29%
ESA	10%

Source: Carana

2. Al Ahram Beverages

[21] It is also possible to assume, however, that some of the investment funds participating in the privatisation program that are listed as Egyptian, may also be representing various non-Egyptian Arab investors.

The Luxor Group	12%
GDR Free Float	63%
ESA	10%
Misr Insurance	05%
The Bank of Alexandria	05%
Further Free Float	05%

Source: Al Ahram Beverages

3. Ideal

Olympic Group Financial Investments	53%
Ideal Commercial Company (owned by the Olympic Group)	24%
Al-Abd Family (Zanusi)	11%
The Employees Stock Association	10%

Source: Ideal

4. Assuit Cement

CEMEX	77%
HC for Metallurgical Industries	13%
ESA	10%

Source: Carana Q1 2001

In sum, while the privatization program has succeeded in its objective of allowing more Egyptians to participate in the ownership of companies, achieving this objective is not entirely positive, as will be noted in the Firm Level Impact analysis. Most importantly, fragmentation of the ownership may have an adverse effect on corporate governance and enterprise restructuring, if no single private investor group is able to exercise control and bring about the necessary changes in management and corporate strategy.

B. FIRM LEVEL IMPACT

In assessing impact at the enterprise level, the focus is on how they have performed under private ownership, and whether they have performed better or worse than they would have under continued state ownership and management. The assessment also considers whether performance varies by privatization approach (e.g. anchor investor, IPO and ESA). Impact is assessed in terms of:

- Corporate restructuring
- Financial performance
- Employment and productivity

Since most enterprises have been sold in the past few years, it is difficult to draw definitive conclusions, especially regarding financial performance, especially if the enterprises need deep restructuring, a process which can take several years before showing positive financial results. In this assessment, particular emphasis is given to the extent of corporate restructuring taking place as an indicator of short term firm level impact. The assumption is that new and active management is required for the privatized enterprises to perform better under private ownership than they would have under state ownership.

The analysis presented below demonstrates that:

- Only some of the privatized companies have undergone significant restructuring, and these have mostly involved anchor and/or foreign strategic investors. In cases where the state has remained a significant player (through its residual shares or close relationship with ESA's that have not finished paying for their shares), restructuring has been limited.
- Privatization has generally had a positive result on financial performance, while having very little impact on employment. However, capital expenditures have been limited.
- The corporatization and commercialization brought about by Law 203 has had a positive impact on the performance of state enterprises. With the assistance of an early retirement fund, these have managed to reduce overall employment by half, while managing financial results almost as good as the privatized firms.

1. Corporate Restructuring

It is generally assumed that privatization will lead to corporate restructuring and improved governance under private management. The theory is that new ownership will hold management accountable for improved performance (or change management), resulting in changes in product line, quality, markets, technology, and ultimately financial performance. In cases where ownership is fragmented (e.g. publicly traded companies), corporate performance take in consideration the interests of all shareholders, and not just the interests of selected blocks of shareholders and managers. Corporate governance is a crucial determining factor in whether restructuring takes place[22].

In the case of many of the Law 203 companies privatized through IPOs, residual state shares held by the HCs or state-owned financial institutions mean that the public sector maintains the largest single block of shares. This has often led to little change in corporate governance at the firm after privatization, since the HC and other government entities have tended to retain the same management structure. In an evaluation of the post privatization performance if 15 former Law 203 companies, all of the IPOs performed poorly with regards to their progress in developing a new management and corporate governance culture.[23] This is demonstrated in Figure 14 below, which shows that only the anchor/strategic investor privatizations were "noticeably reformed" after their privatization. IPOs tended either to be transitional reformers, or were rated as slow to reform.

[22] Corporate governance, as a commonly applied business concept in advanced market economies, is only beginning to gain currency in Egypt. In October 2001, a conference on corporate conference was held in Cairo. In its Development Program for 2002, the Ministry of Foreign Trade made provisions for the inclusion of corporate governance and gave it an Arabic language definition, dubbing it *Howkima Al-Sharikat*. The government is trying to give the concept a legal status and a new draft law on capital markets, which includes a provision for corporate governance, is likely to be put before the Parliament in late 2002.

[23] Carana study on the post privatisation performance of 15 former Law 203 companies.

Figure 14: Ratings for the Development of Post Privatization Corporate Governance and Management in 15 Former Law 203 Public Enterprises

Privatized Company	Date & Method of Privatization	Amount of Government Equity Sold	Stage of Post-Privatization Development
Al-Ahram Beverages Company	December 1996 Strategic Investor Sale	100%	Noticeably reformed
The Egyptian Bottling Company for Coca Cola	April 1994 Strategic Investor Sale	100%	Noticeably reformed
Al-Nasr Bottling Company for Pepsi Cola	April 1994 Strategic Investor Sale	100%	Noticeably reformed
Ideal	November 1997 Strategic Investor Sale & Public Offering	100%	Transitional
The Arab Company for Transistors and Electronics	September 1996 (73%) & October 1999 (27%) Two Public Offerings	100%	Transitional
Electro Cables Egypt	December 1997 Public Offering	100%	Transitional
The Egyptian Financial Industrial Company	May 1996 Public Offering	75%	Transitional
Kafr Zayat Pesticides and Chemicals	August 1996 Public Offering	75%	Transitional
Nasr City Housing	May 1996 Public Offering	75%	Transitional
Simo for Paper	June 1997 Public Offering	85%	Slow to reform
Middle and West Delta Flour Mills	August 1996 Public Offering	61%	Slow to reform
East Delta Flour Mills	August 1996 Public Offering	61%	Slow to reform
Upper Egypt Flour Mills	August 1996 Public Offering	61%	Slow to reform
Misr Free Shops Company	January 1997 (77%) & December 1997 (23%) Two Public Offerings	100%	Slow to reform
Al-Nasr Casting	December 1997 Debt-Equity Swap	100%	Slow to reform

Source: Carana Corporation

The foreign investors that have taken over former Law 203 companies have generally tried to improve corporate governance standards at the enterprises and bring them in line with international standards. For example, soon after Alexandria Cement Company was taken over by Blue Circle of Great Britain, the management stated its commitment to the protection of minority shareholders. Salem Sousou, the new financial manager of Alexandria Cement, stated in an article regarding minority rights in Alexandria Cement, that "the board of directors (of Alexandria Cement) was committed to increasing shareholder value for all shareholders in the company". The objective behind establishing a new company between Blue Circle and Alexandria Cement is in order to benefit all shareholders under the investment incentives and guarantees law number 8 of 1997."[24]

2. Financial Performance

Analysis of financial performance as a result of privatization is made very difficult by the lack of data from privatized companies, as well as from the short time period since privatization. The analyses and conclusions presented here are drawn from several sources including two recent papers on the impact of privatization[25], enterprise specific case studies developed by CARANA and others in recent years[26], and analysts reports and available data on publicly available firms[27].

The following principal conclusions can be drawn from the available sources:

- The financial performance of privatized companies has improved since privatization, especially in terms of net income, return on sales and return on assets. Improved financial results can mostly be attributed to improvements in efficiency, since output has increased only modestly (while lowering inventory levels).

- Companies remaining under the Law 203 Holding Companies have also improved their financial performance, although not as much as the privatized companies. The Omran study, which statistically compares 54 privatized companies to 54 comparable state owned companies, finds that the state companies experienced particular improvement in return on assets, no particular improvement in return on sales and net income, while return on equity went down. The Attia study also indicates that the HC performance has been improving by almost as much as the privatized companies, although he argues that through 1999, on average smaller and less profitable companies were offered for sale. Our own analysis of available data shows that financial performance of remaining companies has been mixed: revenues have been declining as has return on assets, whereas return on investment appears to have improved (probably because capital expenditures have been minimal).

- Neither privatized or remaining state companies have made significant capital expenditures, with the exception of a limited number of companies bought by anchor and especially foreign investors. The implication is that performance in privatized companies has improved mostly as a result of improved capital utilization. In the case of state companies, high inventory and

[24] Al Alam El Youm, April 4, 2001, Page 9
[25] Mohamed Omram, "Performance of State-Owned Enterprises and Newly privatised Firms: Empirical Evidency from Egypt", and Joseph Shawki Attia, "Financial and Economic Performance of Privatized Firms", PhD Dissertation
[26] Compiled as a Special Study by PCSU/CARANA Corporation
[27] As summarized in PCSU Quarterly Reports

accounts receivables, suggest that financial performance may turn out to be worse than reported.

- As will be further documented in the next section on labor and productivity, remaining state companies have reduced employment significantly, while there is little change in privatized companies.

Figure 15 Illustrates the Stock Exchange Performance of publicly traded privatized companies. Almost all these firms (34 of 37) have seen their share prices decline from the offering price, reflecting the overall decline of share prices since the boom years. However, 22 of the companies have had a positive yield, usually well over 10%, by paying dividends.

Figure 15:

	Stock Market Performance of Privatized Companies									
	Company Name	Code	Performance Indicators			Market Data for QI 2002			Initial Offering	
			Over Qtr	Since Offer	Yield	Closing	P/E Ratio	Last Div.	Price	Date
			1	2	3	4	5	6	7	8
1	Abu Kir Fertilizers	ABUK.CA	30.8%	-1.0%	10.4%	32.69	4.73	3.40	34.60	1-May-96
2	*Al Ahram Beverages*	PYBR.CA	14.7%	-9.2%	15.1%	39.78	7.04	6.00	67.00	13-Nov-96
3	*Alexandria Cement*	ALEX.CA	62.2%	-3.1%	0.0%	29.73	50.54	4.90	32.00	30-Nov-99
4	*Alexandria Flour Mills*	AFMC.CA	-9.0%	-41.5%	15.5%	6.46	3.28	1.00	82.50	29-Jun-97
5	*Alexandria Pharmaceuticals*	AXPH.CA	0.0%	3.1%	0.0%	81.46	4.74	10.81	66.15	1-Jun-95
6	Alexandria Spinning & Weaving	SPIN.CA	5.1%	-23.8%	0.0%	5.76	3.18	1.33	37.00	1-Jun-95
7	*Ameriyah Cement*	AMRI.CA	14.1%	-12.0%	20.3%	32.00	3.99	6.50	86.97	1-Jun-94
8	*Arab Cotton Ginning*	ACGC.CA	-0.7%	-9.7%	0.0%	33.99	12.91	4.00	60.00	1-Sep-96
9	Arab Pharmaceuticals	ADCI.CA	12.0%	4.5%	0.0%	51.00	4.43	8.50	40.00	1-Sep-96
10	*Bisco Misr*	BISM.CA	-9.6%	0.0%	12.1%	14.00	n/a	1.70	14.00	26-May-96
11	*Cairo Oil & Soap*	COSG.CA	2.2%	-36.6%	12.9%	14.00	n/a	1.80	31.00	01-Jul-00
12	*Cairo Pharmaceuticals*	CPCI.CA	5.9%	-3.5%	0.0%	38.00	4.10	7.17	46.00	01-Nov-96
13	Delta Industries (IDEAL)	IDEA.CA	-1.3%	-13.9%	8.7%	17.27	3.28	1.50	33.08	01-Dec-97
14	*Development & Engineering Consultants*	DAPH.CA	63.3%	-19.0%	0.0%	9.21	27.46	1.00	26.36	01-Apr-97
15	*East Delta Flour Mills*	EDFM.CA	11.7%	-11.1%	24.3%	16.45	3.63	4.00	31.00	18-Nov-96
16	*Eastern Tobacco*	EAST.CA	-8.2%	-12.7%	15.7%	38.17	3.43	6.00	96.00	22-Jun-95
17	*Egyptian Contracting (Mokhtar Ibrahim)*	ECMI.CA	-5.9%	-38.4%	22.6%	8.85	3.44	2.00	55.00	24-Jun-98
18	*Egyptian Electrical Cables*	ELEC.CA	-11.0%	-31.1%	0.0%	1.87	0.00	4.80	23.33	17-Jun-95
19	*Egyptian Financial & Industrial Company*	EFIC.CA	10.9%	-2.4%	11.5%	26.08	4.22	3.00	30.00	26-May-96
20	*Egyptian Starch & Glucose*	ESGI.CA	5.2%	-18.3%	0.0%	10.90	3.23	2.30	35.00	18-Jun-96
21	*El Giza Contracting*	GGCC.CA	0.7%	-30.4%	22.0%	9.11	3.03	2.00	47.25	15-Sep-97
22	***El Kahera Housing***	ELKA.CA	72.1%	-29.0%	1.7%	2.96	7.78	0.05	16.48	24-Mar-97
23	El Nasr Civil Works	NCCW.CA	13.5%	-24.3%	28.6%	11.35	2.16	3.25	33.25	24-May-98
24	*El Nasr Clothes & Textiles KABO*	KABO.CA	-9.7%	-32.5%	0.0%	15.44	n/a	2.00	102.00	11-Jun-97
25	*El Nasr for Dehydrating Agricultural Products*	NDAP.CA	-4.1%	-23.5%	0.0%	10.96	n/a	0.86	38.00	11-Aug-97
26	*El Shams Housing*	ELSH.CA	-9.4%	-38.3%	21.6%	2.78	5.73	0.60	15.00	01-Oct-98
27	*El Wadi for Exporting Agricultural Products*	WACE.CA	-7.4%	-27.6%	22.5%	10.45	n/a	2.35	31.00	17-Nov-98
28	*Extracted Oils*	ZEOT.CA	3.2%	-25.3%	0.0%	5.84	2.05	1.60	45.00	30-Mar-95
29	*General Silos & Storage*	GSSC.CA	-2.7%	-28.3%	31.2%	6.41	2.62	2.00	39.00	28-Oct-96
30	*Heliopolis Housing*	HELI.CA	-6.5%	-16.8%	13.0%	46.00	4.18	6.00	155.00	15-Aug-95
31	***Helwan Portland Cement***	HELW.CA	12.0%	-8.0%	0.0%	34.12	5.03	5.00	58.00	09-Nov-95
32	*Industrial & Engineering Projects*	IEEC.CA	-20.8%	-33.3%	15.8%	9.47	8.63	1.50	56.70	29-Oct-97
33	*Kafr El Ziat Insecticides*	KZPC.CA	16.2%	-3.2%	15.5%	19.40	4.83	3.00	23.20	01-Sep-96
34	*Mahmoudia Contracting*	MGCC.CA	-26.0%	-47.5%	0.0%	2.33	0.00	3.25	35.00	17-Jan-98
35	*Medinet Nasr Housing*	MNHD.CA	-3.2%	-7.1%	9.5%	21.02	6.39	2.00	32.50	13-May-96
36	*Memphis Pharmaceuticals*	MPCI.CA	-1.0%	-0.5%	0.0%	48.50	4.29	8.76	50.00	1-Sep-96
37	*Middle & West Delta Flour Mills*	WCDF.CA	2.1%	-11.7%	25.6%	19.50	3.37	5.00	40.00	30-Jun-96

3. Employment and Labor Productivity

At the start of the privatization program in 1991, Egypt's total official labor force was estimated to be around 15,250,000. The government was by far the largest employer in the country, accounting for 37.4% of aggregate employment, around 5,500,000 million employees,[28] including:

- All public sector companies,
- Local and national government,
- The military industrial complex (but not the armed forces)
- Other state institutions.

For its part, the 314 public enterprises of the Law 203 portfolio employed around 1 million workers (*mixed estimates ranging from 1,083,000 PEO and 932,000)*. Therefore, from the outset of the privatization program, only around 6% of Egypt's total labor force was potentially subject to the direct impact of the privatization of Law 203 companies. The sector-by-sector break down of the labor force of the Law 203 portfolio in 1991, together with average annual salaries per worker, and total salaries by the sector, are shown in Figure 16 below:

Figure 16: Labor Force in Law 203 Public Enterprises in 1991

Holding Company	Numbers of Workers	Average salary per Worker	Total Salaries (LE M)
Spinning and weaving	96,524	5,532	534
Textile manufacturing and trade	96,762	5,085	492
Cotton and foreign trade	49,156	5,900	290
Engineering industries	62,178	7,688	478
Metallurgical industries	72,827	9,337	680
Mining and refractory	61,826	9,042	559
Chemical industries	47,400	7,785	369
Pharmaceutical industries	29,145	7,583	221
Food industries	94,616	4,365	413
Mills and silos	56,505	3,858	218
Agricultural development	40,082	3,044	122
National construction	57,061	6,817	389
Electrical construction	90,741	5,466	496
Housing, tourism and cinema	19,918	6,326	126
Maritime transport	24,187	9,468	229
Transport	33,476	6,900	231
Total	**932,404**	**6,271**	**5,847**

Source: The Ministry of Public Enterprises

The size of the overall public sector labor force as a percentage of Egypt's total work force (which has grown numerically during the 1990s and is presently estimated to be around 20-22 million) has more or less remained constant, around 37%. However, the size of the labor force of the Law 203 portfolio has decreased by more than half during the decade of Egypt's economic reform. In 2001 the number had decreased some 453,000 employees. Figure 17 below, shows the total numbers for the remaining Law 203 labor force in 2001, broken down by the HC:[29]

[28] The World Bank, Arab Republic of Egypt: Public Sector Investment Review, p.56.

Figure 17: Labor Force and Salary Remaining Law 203 Portfolio in 2001

Holding Company	Total Labor	Average Salary/employee	Total Salaries in 2001
Spinning & Weaving	134934	7183.512	969.3
Trade	22866	6586.198	150.6
Engineering	25243	15243.83	384.8
Metallurgical	50312	15789.47	794.4
Chemical	42843	12256.38	525.1
Pharmaceutical	22207	11338.77	251.8
Food Industries	82173	8124.323	667.6
Construction	34891	10988.51	383.4
Housing, Tourism & Cinema	7771	14399.69	111.9
Maritime & Inland Transport	30216	9451.946	285.6
Totals	**453, 456**	**9,977.815**	**4,524.5**

Source: PEO

The reduction in the Law 203 labor force was largely due to three factors, two of which were directly related to the privatization program:

- Pre-privatization labor restructuring through the early retirement program (some 167,000 employees),
- The transfer of Law 203 companies to Law 159 through their divestiture to the private sector (some 222,000 employees).
- Departure from the workforce due normal retirement and other forms of natural attrition (some 148,000 employees)[30]

Figure 18 below presents a detailed account of the decline in the composition of the Law 203 workforce during the years of the privatization program:

Figure 18:

Changes in the Workforce of Public Enterprise Sector Companies: 30.06.93 to 31.12.2000

Description	Workforce	Percent
Law 203 workforce at 30/6/93	1,032,564	100.0%
Workforce in privatized companies	219,985	21.0%
Workforce which left under the Early retirement Scheme	167,442	16.0%
Normal attrition	148,933	14.0%
Remaining workforce at 31/12/2000	496,204	49.0%

Source: Office of Public Enterprises

Therefore, it is possible to conclude that Egypt's privatization program has had a direct impact on some 387,000 employees, or approximately 2-2.5% of the current total workforce. This is also equivalent to 6-7% of the current total public

[29] The number of HCs has gradually been rationalized during the privatization process and reduced to 10 HCs responsible for the remaining Law 203 portfolio in 2001

[30] Source: Carana study on early retirement

sector work force (Law 203 and non-Law 203 public enterprises and all levels of the state bureaucracy).

Given the high level of political concern with employment and social stability, while recognizing the level of overstaffing in state enterprises, the government gave strong priority to these factors when preparing to implement privatization. It went about creating a social safety net in order to minimize negative impacts of privatization:

- The establishment of an early retirement financial benefits program for employees voluntarily willing to terminate their employment ahead of the natural retirement age;

- Providing labor assistance programs such as job retraining, job placement and entrepreneurship schemes;

- The establishment of the Social Fund for Development[31]

Introducing stability in employment as a condition in the sale of companies.

A fund was created in 1997 to assist the HCs implement early retirement programs, primarily on the basis of proceeds generated from privatization. Under the government's early retirement program, and with capital provided by the fund, the HCs were able to offer the employees of their Law 203 affiliates packages ranging from LE 15,000 to LE 35,000 in compensation for taking their retirement early. Such measures would assist the government in reducing the volume of overstaffing in public enterprises slated for privatization. Some 167,000 Law 203 company workers have already benefited from the early retirement programs, as has been shown in Figure 18. Private sector funded early retirement programs were also applied in privatized companies, mostly in the case of anchor investor transactions. State funded and private sector early retirement programs were to be conducted on voluntary principles; under the original guidelines issued by the government that privatization would not be inimical to Egyptian labor. Figure 19 below shows the details of the labor retrenchment through early retirement program.

[31] World Bank, Privatization in Egypt: Achievements and Challenges, June 11 2000, p.24.

Figure 19:

Early Retirement Data by Gender from Beginning of ERS Program until 30 June 2001 (*Values in Million Egyptian Pounds*)													
Data of Labor who left on ERS from Beginning of Program until 30 June 2001													
	Male					Female					Totals		
Holding Company	Over 50 Years Old	Under 50 Years Old	Total	Cost	Annual Saving in Wages	Over 45	Under 45	Total	Cost	Annual Saving in Wages	Number	Cost	Annual Saving in Wages
Textile	17861	2931	20792	439	126	2071	495	2566	55	18	23358	494	144
Trade	12914	17917	30831	545	86	5214	9908	15122	256	40	45953	801	126
Engineering Industries	7651	6672	14323	421	144	1796	922	2718	78	26	17041	499	171
Metallurgical Industries	10126	13788	23914	806	256	1768	2375	4143	104	25	28057	910	281
Chemical Industries	6646	5063	11709	321	69	1449	1436	2885	79	17	14594	400	87
Pharmaceutical Industries	715	651	1366	28	15	1995	1919	3914	88	43	5280	116	58
Food Industries	9768	5820	15588	293	93	2343	2407	4750	88	29	20338	382	122
Construction	4517	2430	6947	162	55	1017	283	1300	34	13	8247	196	68
Housing, Tourism, & Cinema	3838	5087	8925	304	86	848	919	1767	60	18	10692	364	104
Maritime & Inland Transportation	5063	2679	7742	203	68	922	252	1174	32	10	8916	235	78
Totals	79099	63040	142137	3522.	998	19423	20916	40339	875	240	182476	4397	1238

There is no data available for the collective number of employees that were made redundant as a result of privatization of the 133 Law 203 public enterprises. However, research conducted into the post-privatization performance of the 67 non-liquidated privatized firms sold to investors and the 34 companies sold to their ESA gives a general indication on the impact of privatization on Egyptian labor. Figure 20 on the following page provides a summary of the amount of retrenchment that has taken place at a sample of 19 out of the 67 non-liquidated privatized companies, providing (estimated) employment figures at the time of privatization, and within a period of 3-5 years after.

Figure 20: Retrenchment Following Privatization
(a sample of 19 companies sold through IPOs, anchor/strategic investor transactions or debt equity swaps)

Privatized Company	Date & Method of Privatization	Total Labor Force at the Time of Privatization	Total Labor Force Post Privatization
El Nasr Boilers	September 1994 Anchor Investor Sale	1150	960
Al-Ahram Beverages Company	December 1996 Anchor Investor Sale	3,200	3900
The Egyptian Bottling Company for Coca Cola	April 1994 Strategic Investor Sale	6,000	Expanded
Al-Nasr Bottling Company for Pepsi Cola	April 1994 Strategic Investor Sale	4,000	6,800
Assuit Cement Cemex Egypt	November 1999 (87%)& June 2000 (13%) Strategic Investor Sale	3,700	1,200
Kahromica	August 1997 Anchor Investor Sale	1,200	1,000
Ideal	November 1997 Strategic Investor Sale	7,700	2,700
Totals for Anchor/Strategic Investors	**7 privatized companies**	**27,450**	**24,000** **(estimate)**
The Arab Company for Transistors and Electronics (Telemisr)	September 1996 (73%) & October 1999 (27%) Two Public Offerings	2,800	2,000
Electro Cables Egypt (Kabelat)	December 1997 Public Offering	3,400	2,100
The Egyptian Financial Industrial Company	May 1996 Public Offering	3,000	2995
Kafr Zayat Pesticides and Chemicals	August 1996 Public Offering	740	650
Nasr City Housing	May 1996 Public Offering	650	600
Simo for Paper	June 1997 Public Offering	1,100	850
Middle and West Delta Flour Mills	August 1996 Public Offering	6,400	6,200
East Delta Flour Mills	August 1996 Public Offering	5,000 (estimate)	4,900
Upper Egypt Flour Mills	August 1996 Public Offering	6,500 (estimate)	6,450
Nasr Dehydrated Agricultural Products	August 1997 Public Offering	1150	650
Misr Free Shops Company	January 1997 (77%) & December 1997 (23%) Two Public Offerings	1,400	1,000
Giza Contracting	September 1997 Public Offering	1,250	1,100
Totals for IPOs	**12 Privatized Companies**	**32,390**	**29,495**
Al-Nasr Casting	December 1997 Debt-Equity Swap	4,000	3,500
Total Decrease in Labor Force	**19 privatized Companies**	**63,840**	**56,995**

Source: Meetings with companies/case studies from PCSU quarterly reports/Terterov PhD/Kompass
* Reduced to 800 by June 2002. Much of the reduction in the workforce can be associated with the sale of one of the company's main loss making factories in Ismailiya to another private investor.

In the above sample companies, fewer than 7,000 out of nearly 64,000 employees have become redundant since privatization, equivalent to around 9% of the workforce within a period of 3-5 years following divestiture. There are some differences by type of privatization:

- In the eleven IPOs, there has generally been little noticeable reduction in labor, with the only two exceptions being the first two companies in the sample. In one of these, Telemisr, much of the worker reduction took place as a result of the sale of one of the company's significant loss making assets, a lamp factory in the city of Ismailiya. The lamp factory was employing around 400 workers at the time of the privatization, around 13% of the company's total workforce. In a number of the other IPO privatizations in the sample there has been very little change in the labor force. In these companies HC and other state institutions have remained significant equity holders, and very little labor or management restructuring has taken place. This is especially evident in the case of the flour milling companies. In these three companies the original total workforce of just fewer than 18,000 employees has only been reduced by less than 500 in the several years since their privatization.

- The experience of the anchor investor sales demonstrates mixed results with regards to the impact of privatization on labor. In the case of the beverages companies, employment has generally tended to increase due to substantial corporate transformation and restructuring of Al Ahram Beverages Company and the two cola bottling companies. This has led to the original public sector firm being absorbed into a new corporate entity altogether. Substantial new investment injected into the companies by the new owners has led to expanded productive assets that have not only productively utilized existing labor, but also created abundant new employment positions. Substantial re-allocation of the existing labor force has also taken place within these firms, as many new technical, administrative and managerial positions have been created.

- Privatization has generally had minimal impact on the labor force of the 34 Law 203 companies sold to their ESAs. There has been very little private sector driven worker redundancy in these companies. In the case of first – largely experimental - ESA transactions, the 10 public works companies sold to their employees in 1994-95, total employment has actually increased slightly, from around 21,000 at the time of privatization, to about 22,000 some five years later.

The increase in employment in the 10 ESA companies is attributable to the following factors.

  - One is the over-all expansion of the 10 companies business and the positive growth in worker productivity, which has almost doubled since the privatization

  - ESA ownership of the company, since it would generally be difficult for management to persuade the ESA to encourage workers to retire voluntarily. There are no voluntary retirement programs in place at the 10 companies.[32]

- When employees leave the company, all shares must be bought back by the ESA from the retiring employees at full value, discouraging retrenchment.

The attitudes of the typical Egyptian worker to the concept of privatization seems to be at best ambivalent, though more often it remains skeptical or negative. Although the government points to its publicity campaigns to placate labor anxiety about the impact of privatization, most workers still tend to associate privatization with retrenchment and loss of workplace benefits. Several privatized companies have made press headlines, which have pointed to high levels of retrenchment and problematic industrial relations since privatization. These include Kahromica, Coca Cola and Electro Cables Egypt.

In summary, the experience of the Egyptian privatization program generally shows that most of the reduction in employment is taking place prior to privatization. Pre-privatization employment levels have been maintained at many privatized firms, and in a number of cases new job opportunities have been created. The total number of Law 203 jobs lost due to privatization can be estimated at 365,000 (assuming 10% of the privatized labor force, and 167,000 early retirees), or about 36% of the total Law 203 labor force at the outset of the program. However, at the same time, the Egyptian economy was creating 436,000 jobs each year between 1991-99. Furthermore, as will be discussed in the next section on Sector Level Impact, liberalization of sector policies has led to new entrants and investment in the sectors involved in privatization. Since, as estimated by the World Bank, manufacturing has the highest labor elasticity of 1.2 (relative to investment), the overall impact of privatization and liberalization must be considered positive.

C. SUB-SECTOR LEVEL IMPACT

Prior to the privatization program, the Egyptian economy was characterized by many sub-sectors in which economic activity was monopolized by public sector enterprises. Since a market economy is based on the principle that competition is the "invisible hand" that promotes efficiency and innovation, neither public sector nor private monopolies can be viewed as positive. Thus, an important test of the impact of privatization is to assess the extent to which both transactions and government policies have contributed to increasing competition, facilitating entry to new companies, and enhancing overall sub-sector dynamism.

As will be documented in this section of the report, sector level impacts are among the most positive and lasting impacts of the privatization program in Egypt. In most sub-sectors, there have been new entrants, improved technology, expanded product range and availability, and in most instances, improved quality, distribution and service. This means that all Egyptian consumers and end-users of the goods and services involved benefit from privatization. Also, in many sub-sectors, there has

[32] Carana ESA study, p.22.

been enhanced competition. The review found that the impact on prices were mixed. However, most price increases were attributed to improved product, service and availability than to liberalization. Below are the results of data analysis and interviews in a sample of sectors encompassed by the program.

1. Rice Milling

There have been substantial changes in the Egyptian market for rice milling during the 1990s as a result of sector liberalization and privatization of public sector mills. During the early 1990s, rice became one of the first agricultural commodities to be liberalized in Egypt. The government's 8 public sector rice milling enterprises comprised a virtual state monopoly with 88.2% of the milling capacity. Liberalization of the rice-milling sector resulted in substantial market entry by private sector firms. Economic returns of growing rice increased relative to other crops, attracting substantial private sector activity. By 1997 private mills overtook public mills in milling capacity. Public sector milling companies rapidly lost market share to the private sector, and were operating well below full capacity amidst the intense private sector competition. By 1998/99, the private sector firms constituted 78.6% of the total milling capacity of the sector.

Competition in the Egyptian rice-milling sector was therefore already thriving when the HCRFM privatized 7 out of its 8 rice mills to their ESAs in 1998. The final Law 203 rice milling company was also sold to its ESA in 2001. The Egyptian rice-milling sector is now highly dynamic and competitive, although this is more directly the result of market liberalization policies as opposed to privatization of state mills specifically. The new private sector projects in the market have been the prime contributors to a vast increase in Egypt's rice production and new levels of product quality that are now available to the consumer.

The HC continues to be heavily involved in the management of the rice mills, who are in effect competing in the sector with tacit HC as well as implicit and explicit subsidies. The privatized mills are presently providing the sector with redundant, un-needed milling capacity, although they are also providing employment for over 9,000 workers.[33] Rice milling is an example of how privatization and liberalization can be successful from the perspective of the overall economy, even though the performance and value of the former state enterprise might be suffering.

2. Flour

Partial liberalization of the Egyptian flour market during the mid 1990s has created fierce competition and over-capacity in the sub-sector for the 72% white bread. However, despite privatization of 3 of the government's 7 Law 203 flour milling companies in 1996, the market for the 82% dark bread

[33] ABT Associates Inc, op. cit, p.10.

remains largely unchanged. It is still heavily subsidized and regulated by the state.

Bread is the single largest component of the Egyptian diet accounting for roughly 26% of an individual's food intake. Both consumption and production of bread has been increasing noticeably in Egypt (mostly due to an increase in population growth) during the last decade, and the country is striving towards self-sufficiency in production. However, Egypt continues to import around 50% of its wheat needs at international prices, forcing the government to pursue the need to subsidize wheat production despite a commitment to price liberalization and privatization of public enterprises in the sector.

Egypt's flour (wheat) milling industry is divided into two segments according to the different type of flour produced:

1. The dark 82% extraction flour, which is the lower quality product subsidized by the government and accounts for the bulk of production and consumption. This segment of the milling industry has traditionally been dominated by public enterprises, which act as regional monopolies. Since 1991, the government has fixed prices in the sector, leaving profit margins very low, making the 82% product the domain of public enterprises. The primary objective of the public sector milling companies has been to meet the annual production targets set by the government.

2. The 72% white extraction flour, which is of a greater purity and is used for finer forms of bread, pastries, cakes, biscuits and other baked products. This segment has been more of a free market in terms of price and competition and, due to the relatively higher profit margins, has traditionally been dominated by the private sector. Since the mid 1990s, Law 203 milling companies have also become active in milling 72% bread, and the market has since become characterized by structural over-capacity, fierce competition and plummeting profit margins.

The market for the 72% flour market continues to be characterized by intense competition and in 1999 the number of private mills producing this type of bread reached 22.[34] The public sector is also active in milling the 72% flour, and production volumes are split evenly with the private sector. A diversity of high quality white bread products is widely available in Egypt due the competitive and innovative character of the market for this sub-sector. However, the current market capacity for 72% flour is double that of market demand, and price wars are likely to continue. It can be expected that the consumer will be the biggest winner of the price competition in the 72% flour market in the short term, although consolidation is likely. There is also a serous policy question of whether the state needs to be in the milling business, especially 72% of flour.

[34] Kompass, p.50.

4. Beverages

Despite the highly acclaimed privatization of Al Ahram Beverages, Egypt's monopoly brewer in 1997, the beer industry in Egypt remains a monopoly, albeit private. High barriers to entry have traditionally protected the beer industry. The privatized Al Ahram Beverages company controls over 90% of sales in the market for beer, with imports and other producers constituting an insignificant market position. However, while the private sector has replaced the government's former monopoly, the quality and availability of beer in Egypt has generally improved. Al Ahram has introduced several new brands of beer into the market since the privatization and has invested heavily into ensuring that adequate quality controls are adopted. Product availability has generally improved, due to major investment in new production facilities and an expansion in the distribution network in parts of the country characterized by heavy market demand. The diversity of products under the private sector's existing monopoly and low import penetration has also resulted in a minor price rise for original brand name products. The new brands of beer introduced have tended to carry a higher price tag than the original brands, although these are still price competitive compared to imported products.

The market for carbonated soft drinks was transformed as a result of the privatization of the state owned bottling plants producing Coca Cola and Pepsi Cola in April 1994. Up until privatization, government enterprises dominated the sector, though private firms were also present in the market. Since the privatization of the Colas in 1994, as well as Al Ahram Beverages in 1997, the private sector controls the market, with the major players being:

1. Coca Cola (45% market share)
2. Pepsi Cola (40% market share)
3. Al Ahram (8% market share)
4. Schweppes (4% market share)[35]

The price for the mainstream bottled products has increased marginally since privatization, though the quality is said to have improved and has been standardized, since all the main players in the market have invested heavily in quality control and improved production methods. Distribution channels have been enhanced by the private sector, expanding accessibility of products to the consumer. New products have been introduced by the private sector entities, and there has been a general shift to canned products, which are more expensive than bottled soft drinks.

5. Cement Sector

The Egyptian cement industry has witnessed a number of very high profile privatizations in recent years, yielding significant revenues for the government and bringing substantial competitive trends into the sector. Up to 1999, the cement industry was dominated by Law 203 public enterprises,

[35] Al Ahram Beverages Company, "The Beverages and Brewing Sector", in Marat Terterov (eds), Doing Business in Egypt, Kogan Page, London, p.232.

with the only significant private player being Suez Cement, which was established in 1977 under the framework of Investment Law 43 (1974). A more recent, major private sector market entrant into the cement market has been the Egyptian Cement Company, founded by Suez Cement and several private shareholders in 1994. There have also been a further 8 newly established private sector companies entering into the market during the late 1990s, when the demand for cement in Egypt was expanding significantly. However, these enterprises were established prior to the mainstream privatization activity that began to take place in the sector in 1999. They are more attributable to liberalization of the market as encouraged by the government under Law 203, as part of Egypt's commitment to economic reform.

With the sale of Beni Suef Cement Company to Lafarge of France in July 1999, the door was opened for other strategic foreign investors to acquire Law 203 cement companies. The main privatization transactions that followed the sale of Beni Suef were as follows:

1. Assuit Cement to Cemex of Mexico (November 1999)
2. Alexandria Cement to Blue Circle of the UK (November 1999)
3. Ameriyah to Cimpor of Portugal (March 2000)

Furthermore, Suez Cement (originally private sector Egyptian) made a successful bid to buy out another public sector cement producer, Tourah Cement, in early 2000. Helwan Cement, already a minority IPO from 1995, saw its remaining government equity bought out by a private Egyptian investor, AESIC, which took control of the company in September 2001.[36]

The Egyptian cement market has become far more dynamic and price competitive due to sector liberalization under Law 203 and the privatization of the bulk of the Law 203 cement producers. This has led to a significant increase in cement production, fostering both a decline in unmet demand and market price for cement in Egypt. This has also led to the closure of some of the smaller, newly established private sector cement producers, who have not been able to compete in the market.

The Egyptian cement market is now dominated by foreign and domestic private sector producers, as is demonstrated in the following table:

[36] AESIC is an Egyptian company registered in Switzerland, governed by Mr Omar Gemei. It is a consulting company that has operated for some time in the Egyptian cement industry and its Board of Directors is comprised of other Egyptian public and private cement company executives.

Figure 21:

The Egyptian Cement Market in 2000-2001

Law 43/159	Egyptian	Suez Cement/Tourah*	30% market share
Law 159	Foreign	Assuit Cement/Cemex Egypt	15% market share
Law 159	Foreign	Beni Suef/Lafarge Titan	06% market share
Law 159	Foreign	Ameriyah/Cimpor	09% market share
Law 159	Foreign	Alexandria/Blue Circle**	03% market share
Law 159	Egyptian	Egyptian Cement Company***	12% market share
Law 203	Egyptian	Helwan Cement	13% market share
Law 203	Public	National Cement	12% market share

Total public sector market share 12%

Total private sector market share 88%

Source: Kompass/EFG-Hermes
* Established as private/JV company in 1977 under Law 43 of 1974
** now owned by Lafarge
*** Greenfield Egyptian and foreign investor private sector from early 1990s

6. Textiles and Garments

The spinning and weaving (textiles) industry is both at present and historically one of the most important sectors in the Egyptian economy. According to the Egyptian Textile Manufacturers Federation (ETMF), there are about 42 public enterprises and 2,356 private enterprises engaged in the Egyptian textiles industry. It is estimated that there are also thousands of small textiles workshops and factories around the country that are not members of the ETMF. The ETMF states that the textiles industry employs an estimated one million workers – around 30% of Egypt’s industrial workforce. In this context, the remaining state-owned companies employ about 135,000 or 13% of the total. In 1997, the aggregate value of Egypt’s domestic textiles production was valued at around LE 8 billion, LE 3 billion of which was exported (accounting for some 25% of Egypt’s total exports).

Figure 22: Private Sector Share in the Textile and Clothing Industry

	Private Sector Share (1992/93)	Private Sector Share (1999-2000)
Ginning	0	37
Spinning	8	58
Weaving	NA	40%
Knitwear	NA	60%
Clothing	NA	70%

Source: Abt Associates and ETMF

Until the last few years, the public sector had a monopoly on all the "upstream" stages in the supply chain for cotton textiles, by far the most important in Egypt: internal trade and supply of cotton, cotton ginning, spinning of yarn and weaving and dyeing of fabric. With no option to import inputs, this meant that private garment producers were dependent on these public sector suppliers in terms of price, quality and availability. Numerous studies have demonstrated that these policies negatively impacted the competitiveness and dynamism of a sector that could have been a much larger exporter and source of jobs.

In the past few years, as shown in Figure 22 above, the combination of privatizations and policy liberalization have allowed increasing private sector participation. For example, in cotton ginning, there are 7 major gins: two state owned, two privatized and two new private. The result is a greater degree of choice of suppliers for downstream producers.

However, the poor financial performance of the remaining Law 203 companies, and the difficulties that the HC has had in privatizing these, indicate the depth of structural and competitive difficulties that developed in this highly globalized and competitive industry. It may be that dynamism and growth can best be restored by promoting more new entrants and investment in the sub-sector.

7. Electronics and Home Appliances

Egypt's economic reform and privatization policies of the 1990s broke the monopoly of the two state owned companies involved in assembling **televisions** (El Nasr Television and Telemisr). Growth in the industry accelerated in the early to mid-1990s and the private sector soon established itself as the dominant force in the television sub-sector. Competition amongst Egyptian firms, who vied to produce/assemble and import televisions under license from the major multinational television producers, spread rapidly during the 1990s. At present the market is dynamic and the selection of products available to the consumer is diverse in both brand name and quality. There are presently 10 private sector firms in the industry, one privatized, and several that are either still state owned under Law 203 or joint venture companies. The composition of the market for televisions is shown in Figure 23 on the following page:

Figure 23: Egypt's Leading TV brands and their Producers

TV Brand	Origin	Produced	Producer/Agency	Ownership
Goldstar (1)	Korea	Locally	Int'l Electronics Co./El Nasr Co.	Private/State-Owned
NEC	Japan	Locally	Telemisr Com	Privatized
Toshiba	Japan	Locally	Int'l Electronics Co./El Nasr Co	Private
Goldi	Egypt	Locally	Int'l Electronics Co./El Nasr Co	Private
Grundig	Germany	Locally	Int'l Electronics Co./El Nasr Co	Private
Philips (2)	Netherlands	Locally	Int'l Electronics Co./El Nasr Co	Private
Daewoo	Korea	Locally	Banha Electronics Industies Co.	State-Owned
Samsung	Korea	Locally	Arab organization Industries (AOI)	State-Owned
Samsung	Korea	Locally	El Tholathia Co.	Private
Prince	Egypt	Locally	Int'l Electronics Co./El Nasr Co	Private
New Star (3)	Egypt	Locally	Int'l Electronics Co./El Nasr Co	Private
LG (Goldstar)	Korea	Locally	Telemisr Co./IGI Co.	State-owned/Private
Sony	Japan	Imported	NA	Private
Panasonic (5)	Japan	Imported	Baghdad Co.	Private
Sharp	Japan	Imported	Egyico	Private

Source: Kompass/HC Brokerage

The privatization of Telemisr was done in two separate transactions, during 1996 and 1999. The company has performed poorly since its privatization and has run up substantial losses since it experienced a complete ownership and senior management over-haul in 1999-2000. The company's board of directors was suspended in June 2001 and the present management is struggling to cope with internal liquidity shortages and having difficulty in maintaining production (source: meeting with the company, June 2002). Given the new vibrancy that emerged in the television sector during the 1990s, the disappointing performance resulting from the privatization of Telemisr has little impact on the quality and availability of goods and services available to the consumer.

In **White Goods** (washing machines and refrigerators), The industry has become highly competitive as a result of sector liberalization policies of the 1990s. Prior to early 1990s, the state held a 100% monopoly in the production of white goods, through one major public enterprise, Ideal. There was no private sector competition either from imports or from domestic producers. With the advent of sector liberalization policies, Ideal's market share began to decline for both washing machines and refrigerators. The market itself started to become more vibrant however, as new private sector competitors started introducing the Egyptian consumer to some new products and services. Major industry multinationals such as Zanussi of Italy, and Turkey's Arcelik started operating under license in the Egyptian white goods market.

Ideal was privatized and bought out by the Olympic Group Financial Investment Company in late 1997, further transforming the white goods sub-sector. The Olympic Group has absorbed Ideal into its own corporate strategies, downsized the operation of some of Ideal's less productive assets and opened new production facilities. The market for both washing machines and refrigerators is now highly competitive and Ideal has been recovering the market share that it lost prior to privatization. Largely due to the Olympic Group's major investment in a new washing machine factory, Ideal's production of washing machines has increased from 130,000 annual units at the time of privatization, to 210,000 at present (*source: interview with OG's VP, June 2002*).

In the refrigerator market, Ideal remains the dominant player in the market for low cost refrigerators (85% market share), and a leading player in the market for refrigerators as a whole (40% market share). However, both Ideal's fridges and washing machines have been re-launched since the privatization, and are now barely recognizable from what they were under the public sector. This is especially the case for the company's low cost refrigerators. Ideal now also provides a whole range of new, after sales services to the customer and its products are marketed as packages of delivery, technical support, insurance and refunds, as is common with producers in market economies. While the price of a washing machine or a new refrigerator has increased in Egypt since the time when Ideal operated under the public sector, the market has been transformed since that time and the consumer now benefits from an entirely different product.

8. Fertilizers and Pesticides

The Egyptian market for fertilizers and pesticides was liberalized during the early 1990s, in line with the government's commitment to liberalize prices and trade in the markets for a number of basic commodities. These policies led to an influx of imported fertilizers and pesticides entering the Egyptian market and significant price competition. A wide range of new products, particularly in pesticides, began to characterize the market on the supply side.

In the fertilizers market, there have been three privatization transactions to note, as shown below:

Egyptian Financial Industrial company (EFIC)	IPO	May 1996
Abou Kir Fertilizers	IPO	May 1996
Abou Zaabal Fertlizers	3 year lease	currently under-way

Two of the companies, EFIC and Abou Zaabal, are Egypt's primary producers of phosphate fertilizer, one of three types of fertilizers generally used in Egypt. The two companies have traditionally constituted a public sector monopoly in the Egyptian phosphate fertilizer market and given their privatization, it is now evident that the private sector dominates the sector. However, the HC has retained a significant (25%) equity stake in the privatized EFIC and the HC's negotiations to lease Abou Zaabal Fertilizers to an anchor investor were still in progress at the time of writing. Therefore, despite privatization activity in this segment of the fertilizer industry, there have been no fundamental changes to market structures since the liberalization of the mid 1990s. Although the Egyptian fertilizer companies are now once again listed as private companies, their production and management strategies have remained the same and there have been no new entrants into the market. The main competition to the Egyptian producers comes from imported fertilizer, despite the government's continued protection of the domestic market with 30% tariffs against imports of phosphate fertilizer.

In the nitrogen fertilizer segment, the dominant market players are the privatized firm, Abou Kir Fertilizers, and the Law 203 companies El Nasr Fertilizers, Misr Chemical Industries (Kima) and Delta Fertilizers. However, although Abou Kir is listed by the PEO as having been majority privatized in an IPO in May 1996, less than 51% of the company is in private hands (Carana, Q1 2002, p.27). The company was sold by the HC to other government entities and more than 51% of the enterprise is presently held by non-Ministry of Public Enterprises government entities (Ibid). Therefore, despite the HC's divestiture of Abou Kir, privatization has not been able to spur competitive forces or any new market entry into this segment of the Egyptian fertilizer market.

However, there has been much more competition in the distribution of nitrogenous fertilizers. Whereas there was no private sector participation in distribution in 1990/91, by the end of the decade, the private sector controlled 77% of distribution, and coops an additional 13%. This has contributed to a doubling of domestic production.

The monopoly that Egyptian public enterprises held in the production of household and agricultural pesticides declined rapidly when the sector was liberalized during the early to mid 1990s. Cheap imports flooded the market and by 1995 had captured around 65% of sales in the pesticides market. The main Law 203 pesticides producer, Kafr Zayat Pesticides and Chemicals, saw its market share decline from a near monopoly, to 25%. Kafr Zayat was privatized in 1996, there-by giving imported pesticides and private sector produced products an even greater market share over state enterprises. The onset of fierce competition in the market has forced Kafr Zayat to become innovative as it seeks to maintain its market share. This has resulted in the introduction of a diversity of new domestically produced and imported pesticides products entering the Egyptian market, with enhanced distribution capacities and substantial price competition. Public sector firms still operate in the sector and are primarily represented by El Nasr Intermediate Chemical Company.

9. Maritime and Inland Transport

The maritime and inland transport sector was, and still is, one of the most troubled and inefficient sectors in Egypt adding considerably to the logistics costs. It is reported that since liberalization and privatization, the sector becoming much more competitive, slightly efficient but much more consumer friendly since the privatization program began.

10. Power Cables

The monopoly previously held over the industry by the public sector firm Electro Cables Egypt was broken in the mid 1990s, leading to several private Egyptian companies entering the market. The leading private sector company to enter the market was that of El Sewedy, the private electrical consortium who developed a complete vertical integration enterprise. Elecro Cables was, however, privatized in 1997 and there is no longer any public sector market share for the production of power cable in Egypt. Electro Cables is still the market leader despite the decline of its previous market monopoly, holding a market share of 40% in 2002. Privatization has not essentially changed the character of the power cables market in Egypt since the private sector had become active in the sector and competition was established while Electro Cables was still a Law 203 company. All of the firms (both privatized and private greenfield) continue to sell to public sector authorities. Electro Cables has had several management changes since the privatization and has generally been struggling financially during the last 2 to 3 years.

Recommendations and the Road Ahead

Egypt is at risk of loosing the fiscal and economic gains of the 1990s from the privatization program. The risk is associated with the increasing fiscal burden of the remaining Law 203 portfolio, and opportunity cost of divesting of non-productive assets and/or putting them in the hands of the more efficient private sector. Therefore, the road ahead is clearly the need and urgent task of divestiture of the remaining portfolio. As stated before, all the aspects of the issues and obstacles in the way of divestiture of the remaining portfolio have been studied by CARANA/PCSU, on behalf of USAID. In Appendix 4 bellow, the recommendations of the studies most relevant and helpful to the task are presented.

IMPACT	RATING			
	Very Positive	Positive	Some Positive Impact	No Impact
Macro Economic	Increased Domestic Savings Rate, Productivity, Foreign and Domestic Investment			
Fiscal	Reduced Public Financing, Increased Revenues from Sales Proceeds and Tax Payments	Commercialization Introduced Financial Discipline in PEs Leveled the Playing Field for Private Sector	PE's Debts to Government and JV Banks	
PE Debts		Reduced Public Risk		
PE Losses		Reduced Public Risk		
Accumulated PE Losses		Reduced Public Risk		
Public Investment		Reduced		
Sector		Liberalization, New Entrants, Reduced Unmet Demand	Improved Product Range, Technology, Product Availability, Quality and Service	
Consumer, Producers and Suppliers	Cement, Electronics, Home Appliances, Rice-Milling	Fertilizers, Pesticides, Beverages	Flour-Milling, Power Cables, Maritime and Inland Transport	Textiles and Others
Labor	Reduced Government Wage Bill		Labor in General, in Anchor Investments and some ESAs	Labor in IPOs, most ESA
Capital Markets		Stimulated Markets in 1990s		

Widening of Ownership			Partially Achieved	
Governance			Companies Sold to Anchor Investors	Other Privatized Firms

Appendix 1: Laws and Decrees Relevant to and Supporting Privatization

Law	**No.**	**Issuing Date**
Establishing the Egyptian Electricity Authority	12/1976	February 12, 1976
Stamp Duty Law	111/1980	January 1996
Amending some provisions of law no. 12 of 1976 authorizing the establishment of the Egyptian electricity authority	36/1984	March 27, 1984
Investment Law.	230/1989.	July 20,1989.
Explanatory Instructions No. (1) To Articles 29 & 118 Of Law No. 187/1981 As Amended By Law No. 187/1993 & Law No. 5/1998.		
Public Business Sector Law	203/ 1991	June 19,1991.
Developments in the capital market law	95/1992	
The executive regulations of the tax law as amended up to Sep. 1993		September, 1993
Authorizing The Establishment Of The Cotton Spot Exchange (Mina Al Basal Exchange).	141/1994	May 31,1994.
Concerning The Promulgating Of The Inland Cotton Trade Law.	210/1994.	June 17,1994.
Amending the company law no. 159 of the year 1981	212/1994	June 17, 1994
Amending Some Provisions Of The Law On The Capital Market Issued As Per Law No. 95 For 1992.	10/1995	March 23,1995.
Concerning Specialized Ports (Bulletin)	1/1996.	January 24,1996.
Amending certain provisions of law no. 12/76 concerning the establishment of the Egyptian electricity authority	100/1996	June 30, 1996
Amending certain provisions of law no. 84 of the year 1968 concerning public roads	229/1996	July 14, 1996
Awarding the public utility concession for the establishment, management, &exploitation of airports & landing grounds	3/1997	February 8, 1997
Investment Guarantees & incentives	8/1997	May 11, 1997
Amending Certain Provisions Of Law No. 12/1964 Concerning The Establishments Of The Egyptian General Organization For Maritime Transport.	1/1998.	January 8,1998.
Amending Certain Provisions Of The Law On Joint Stock Companies, Partnerships Limited By Shares ,And Limited Liability Companies As Promulgated By Law No. 159/1981.	3/1998.	January 18,1998.
Amending law no. 30/1975 for the policy of the Suez Canal	4/1998	January 19, 1998
Amending certain provisions of the law on income taxes as promulgated by law no. 157/1981	5/1998	January 22, 1998
Concerning Some Provisions Related To The Distribution Of Electricity Companies, The Generating Stations And The Transmission Networks , And Amending Some Of The Provisions Of Law No. 12/1976 Establishing The Electricity Authority Of Egypt .	18/1998.	March 26,1998
Transferring The National Telecommunications Authority Into An Egyptian Joint Stock Company.	19/1998	March 26,1998
Adding a new article to law no. 1/1996 concerning specialized harbors	22/1998	April 25, 1998
Tenders Law.	89/1998	May 8,1998
The reorganization of private sector contributions to capitals of public sector banks	155/1998	June 11, 1998
Amending certain provisions of central audit agency law as promulgated by law no. 144/1988	157/1998	June 11, 1998
Concerning the Protection Of National Economy From The Effects Of Harmful Practices In Int'l Trade With Its Executive Statutes D.No. 549/1998.	161/1998	June 11,1998.
Companies Law		March 1999.
The Executive regulations of the law concerning insurance supervision & control in Egypt		January, 1999
The executive regulations of the capital market law		September, 1999
Models of contracts of joint stock companies & limited liability companies under the companies law no. 159/1981		November, 1999
Law no. 10 of 1981 promulgating the law on the supervision & control on insurance in Egypt, as amended by laws no.s 307/1989, 91/1995, & 156/1998		January, 2000
Law no. 95 of the year 1992 promulgating the law on the capital market		January, 2000
Promulgating the law on Securities central lodging & listing	93/2000	May, 18, 2000

Prime Minister Decrees

Decree	No.	Issuing Date
Amending Certain Provisions Of The Executive Statutes Of The Law On Investment Guarantees And Incentives.	1585/1998	May 29,1998.
Concerning The Executive Statutes Of Law No. On Investment Guarantees & Incentives.	2108/1997	August 9,1997.

Ministerial Decrees

Decree	Issued By	No.	Issuing Date
The executive regulations of the company law	Minister of Investment affairs & int'l cooperation	96/1982	June 26, 1982
The executive regulations of the law on capital market	Minister of economy & foreign trade	135/1993	April 8, 1993
The Admissibility Of Exercising Maritime Transport Works By Egyptian Private Sector Companies And Egyptian Individuals (Bulletin).	Minister Of Transport And Communications.	21/1996	July 2, 1996.
Permitting The Exercise Of Maritime Transport Work By Egyptian Private Sector Companies And Egyptian Individuals.	Minister Of Transport And Communications	21/1996	December 15,1996
Implementing Certain Provisions Of Law No. 3/1998 Concerning The Amendment Of Certain Provisions Of The Law On Joint Stock Companies, Partnerships Limited By Shares And Limited Liability Companies As Promulgated By Law No. 159/1981.	Minister Of Economy	25/1998.	February 1,1998.
In Connection with Conditions & Controls For Granting Licenses To Practice Maritime Transport Works & Their Relevant Works	Minister Of Transport And Communications	30/1998	May 13, 1998
Maritime transport concerning licenses granted for exercise of maritime transport activities	Minister Of Transport And Communications	31/1998	May 14,1998
Enforcing Certain Provisions Of Law No. 3/1998 Concerning The Amendment Of Certain Provisions Of The Law On Joint Stock, Partnerships Limited By Shares And Limited Liability Companies.	Minister Of Economy	75/1998.	March 10, 1998.
Amending The Executive Statutes Of Import & Export Law In Connection With Cars Importation & 2 Articles Published In Al Ahram Newspaper On 7/11/1998: - Boosting Local Factories Through Prohibiting The Importation Of Old Cars - Confining The Importation Of Cars For The Current Year On The 1999 Production.	Minister Of Trade & Supply	580/1998.	November 7,1998.
Amendments on import & export law	Minister of Trade & Supply	619/1998	November 21, 1998
Amending the executive statutes of the insurance supervision & control law in Egypt	Minister of Economy	45/1999	February 15, 1999
Amending some of the provisions of the executive statutes of the insurance supervision & control law in Egypt	Minister of Economy	158/1999	May 29,1999
Amending certain provisions of the executive statutes of capital market law	Minister of Economy	43/2000	January 26, 2000
Amending certain provisions of the executive statutes of capital market law	Minister of Economy	44/2000	January 26, 2000
Amending certain provisions of the executive statutes of capital market law	Minister of Economy	92/2000	February 12, 2000

Presidential Decrees

In Addition To the Previous Laws & Decrees:
1) The Commercial Code Modified Till 1977.
2) Promulgating the Agriculture Law, Law 53/1966.
3) Import & Export Regulations Dated January 1998.
4) Import & Export Regulations Up To July 1998.
5) Promulgating the Trade Law, Law 17/1999.
6) The Egyptian accountancy standards
7) Customs Tariff (Harmonized) modified up to April 2000.

Government Institutions and Entities Directly Involved with privatization Program

- **The Ministry of Public Enterprises (MPEs)** established in October 1993 (?) is responsible for all reform aspects of public enterprises including privatization, restructuring, labor and legal issues. *The Public Enterprise Office (PEO)* is an independent body created to assist the Minister of Public Enterprises. Its main responsibilities are to act as a coordinator for the privatization and restructuring programs, and to initiate and monitor plans for the privatization program. Although, the PEO has no executive authority, it is a central driving force and a link between the government and the Holding Companies. In its capacity as the technical secretariat to the Minister, the PEO has a staff of about 30 people funded almost equally by the Government of Egypt, the United Nations Development Program (UNDP) and the United States Agency for International Development (USAID). The USAID is reassessing its role and involvement in the program after June 30, 2002.

In 1993, the PEO published an action plan entitled "General Procedures and Guidelines for the Government Program of Privatization, Restructuring and Reward System" which can be considered the only formal document that reflects the government's objectives and commitment.

- **The Quattro Committee (QC)** is comprised of the PEO, Capital Markets Authority, the Central Auditing Committee and the Cairo Stock Exchange. The QC's responsibilities concerning initial public offerings (IPOs) include suggesting and approving privatization strategies, reviewing technical valuations, evaluating market values of companies, and suggesting fair prices for IPOs.

- **The Holding Companies (HCs)** were created in 1991. The ownership and management of 314 PEs were transferred from the various Ministries to 17 HCs. The portfolio of these HCs were designed to eliminate sector monopolies, introduce competition, and ensure that each HC had an array of enterprises with differing profitability and sales potential. HCs are primarily responsible for organizing the sale of their constituent PEs (known as affiliated companies).

- **The Capital Market Authority (CMA)** established in 1979 is a government organization, which reports to the Minister of Economy. Pursuant to the Capital Markets Law No. 95 of 1992, the CMA was given sole control over supervising, reforming, and modernizing the Cairo Stock Exchange. The CMA is charged with market development, supervision of trading, broker licensing and general market surveillance.

- **The Share Pricing Committee (SPC)** is comprised of the CMA and the Cairo Stock Exchange. It is the sole authority to review and approve the share price offered in the IPO process.

- **The Central Auditing Authority (CAA)** is an independent government body reporting directly to the People's Assembly, which audits the performance and evaluation of companies that are at least 25% publicly held. Furthermore, it reviews valuation studies undertaken by HCs and QC's.

Currently, neither the HCs nor the PEO office are directly empowered to approve the sale of an affiliated company, nor can they insist upon adherence to standardized sale procedures. This dispersion and diffusion of responsibilities and accountabilities among the various government organizations has sometimes creates confusion and hindrances to the privatization process. Prospective investors find difficulty in getting reliable and current information of companies to be privatized.

Also, other Ministries are responsible for undertaking their reform programs. For instance, the Ministries of Transport, Telecommunications, Power, etc. are directly responsible in undertaking their own respective privatization programs. The public enterprises under the ownership and control of these Ministries are outside the legal framework and process of the Ministry of Public Enterprises.

Appendix 2: Ministerial Privatization Committee Decisions on Non-operating Land Issues

Date	Decision	Situation Now	Reasons
June 5, 1996	The committee has decided to exclude land and buildings listed amongst company assets to be sold in full or to offer shares on the stock market, and this applies for companies which land and buildings are located within City zones.	The decision was later amended at a following meeting	Difficulty in selling off the majority of companies without land
June 5, 1996 (remainder)	The committee has decided that the holding company has the right to include amongst the sale value of the affiliated company compensation for use of land or buildings which were not included in the sale value for the period which it deems suitable	This was implemented in the case of the Ahram Beverages Company	Difficulty in the sale of the majority of companies without land
	The committee decided that the holding company and affiliated company should take the legal and accounting procedures necessary for transfer of ownership of land and buildings mentioned from the affiliated company to the holding company	Underway in unutilized assets	
	The committee decided that the company has the right to implement the above guidelines on all or some of the land and buildings owned by the affiliated company which is located within the city zones	Underway in unutilized assets	
	The committee has decided that there should be disclosure to the buyer that the value determined as a minimum share price for the share does not include ownership of the land and buildings, but only includes the right to utilize these lands within the determined period.	This was implemented in Al Ahram Beverages	Difficulty in the sale of the majority of companies without land
August 4, 1997	The committee decided to design the contractual relationship between the ports authority and maritime companies, as for industrial companies which own wide areas of land, a decision has been made to transfer land to the holding company along with possibility of granting utilization rights to affiliated companies for their utilization.	Has not taken place yet	
August 12, 1997	The committee has stressed the previous decision in its session of 4/8/1997 which calls for the treatment of the matter of land through the granting of utilization rights for a fee in cases where the large size of land and its value stand in the way of executing sales transactions, whereby the utilization rights period extends for thirty years.	There has not been a case reviewed to date which is subject to this decision	

Appendix 3: Details of Privatization Transactions for Each Category

Privatization Achievements: Sales to Anchor Investors

	Name of Company	Date of Contract	Private Sector	ESA	Remaining HC Share	Total Sale Value (LE millions)	Approval to Law 159
1	Pepsi Cola	11-04-94	90.00%	10.00%	0.00%	131	16-12-94
2	CocaCola	20-04-94	90.00%	10.00%	0.00%	286	16-12-94
3	El Nasr Boilers	27-09-94	100.00%	0.00%	0.00%	16	6-12-94
4	El Nasr Transformers (Elmaco)	25-02-96	90.00%	0.00%	10.00%	115	13-07-96
5	Al Nasr Utilities	10-11-96	90.00%	0.00%	0.00%	40	30-06-97
		(4-08-99)	10.00%				
6	Al Ahram Beverages	13-11-96	90.00%	10.00%	0.00%	298	18-02-97
7	Misr Mechanical and Electrical Projects (Kahromica)	19-06-97	61.00%	10.00%	29.00%	103	18-09-97
		(26-08-97)					
8	Modern Textiles (Bolivara)	30-06-97	N/A	N/A	N/A	33	N/A
9	Delta Industries (Ideal)	Dec-97	90.00%	10.00%	0.00%	311	5-01-98
10	Kaha for Preserved foods	Aug-98	90.00%	10.00%	0.00%	154	Feb-01
11	El Wadi for Exporting Agricultural Products	17-11-98	68.00%	27.00%	5.00%	122	18-12-98
12	Nobarieya for Seeds Production - Nobaseed	24-02-99	100.00%	0.00%	0.00%	103	20-04-99
13	Gianaclis	4-03-99	N/A	N/A	0.00%	32	Underway
14	Beni Suef Cement	5-07-99	76.00%	5.00%	*19.00%*	527	29-08-99
		(2-02-00)	19.00%				
15	Delta Sand Bricks	5-07-99	90.00%	10.00%	0.00%	62	25-09-99
16	Arabia Foreign Trade	Aug-99	90.00%	10.00%	-	15	27-04-00
17	Assiut Cement	Nov-99	77.00%	10.00%	*13.00%*	1,197	1-11-99
		(Jun-00)	13.00%			183	
18	Alexandria Cement	30-11-99	90.00%	10.00%	0.00%	670	1-02-00
19	Industrial Gases	22-12-99	90.00%	10.00%	0.00%	60	Feb-00
20	Telephone Equipment	Dec-99	80.00%	10.00%	10.00%	100	12-02-00
		14-02-02	**10.00%**	**10.00%**		**11.4**	
21	Torah Portland Cement	(9-12-94) (5-05-95)	76.40%	5.00%	18.60%	1,226	Mar-00
		26-01-00					
22	Plastic & Electricity Industry	3-02-00	90.00%	0.00%	10.00%	94	Feb-00
*	Ameriyah Cement	Mar-00	29.00%	0.00%	0.00%	527	1-10-98
23	Ramsis Agriculture	30-01-00	100%	-	-	161	Underway
24	Egyptian Engineering & Equipment (MICAR)	Jun-00	90.00%	10.00%	0.00%	25	15-07-00
25	Alexandria Confectionary	Aug-00	90.00%	0.00%	10.00%	28	Underway
26	Egyptian Gypsum	8-02-01	90.00%	0.00%	10.00%	83	Underway
27	Arab for Carpets	5-07-01	100%	-	-	50.1	Underway
28	*Alex for Cooling***	*30-07-01*	*90%*	*0.00%*	*10.00%*	*33*	*Underway*
29	*Abou Zaabal Fertilizer***	*23-11-01*	See Notes			*182.8*	*Underway*
	Total					**6,978**	

Source: Public Enterprise Office

*The 29% sale of **Ameriyah Cement** is recorded in sale value total for anchor sales, however it is not counted as an anchor sale. The sale is recorded as a majority IPO.

**Reported as sales by MPE, but awaiting final approvals

Notes on Anchor Investor Sales: The buyer of **Abu Zaabal for Fertilizers**, Cement Misr, will lease the company for a period of three years before buying. Cement Misr is committed to paying LE 182.8 million for the company under an installment plan against collateral over a three-year period. The PEO therefore records this transaction as an anchor sale with a value of LE182.8 million. The MPE considers this to be a pioneering transaction and has offered to conclude other transactions with investors on this basis. However, the transaction has yet to generate any proceeds for the government since payments are to be made on an installment basis.

El Nasr Transformers (Elmaco) is listed as an anchor privatization sold by the government in February 1996 for LE 115 million. Elmaco was sold to the Egyptian American Company for Transformers (EGMAC) and the company was transferred to Law 159 in July 1996. However, while EGMAC is listed as a Law 159 company, it has more than 51% public ownership and a number of Egypt's donors (especially the IMF) refused to acknowledge the sale of Elmaco as a bona fide privatization.

Ramsis Agriculture was sold to a religious fund and liquidated. The PEO records this as an anchor sale. Likewise, a production line of **Arab Carpets** was sold to a religious fund after the general assembly had elected to liquidate the company. The PEO records this as an anchor sale. **Modern Textiles (Bolivara)** was taken over by United Arab for Spinning and Weaving (UNIRAB), as an asset sale for LE 33 million in June 1997.[37]

[37] Bolivara was an asset sale only, meaning that the investor acquired the company's assets (including labor), without its debts, which were later settled by the HC.

Privatization Achievements: Majority Public Offering						
Name of Company	**Date of Sales**	**Private Sector**	**ESA**	**Remaining HC Share**	**Total Sale Value (LE Millions)**	**Approval to Law 159**
United Arab for Spinning & Weaving	(1994) 1998	60.40%	6.9%	32.70%	226	5-05-97
Ameriyah Cement	(1994) 1998	61.00%	10.00%	0.00%	768	1-10-98
Alex. For Spinning & Weaving	(1995) 1998	94.60%	5.40%	0.00%	82	5-03-98
Egyptian Electrical Cables	(1995) 1997	95.00%	5.00%	0.00%	321	8-12-97
Extracted Oils	30-03-95	42.53%	8.54%	48.93%	85	26-04-98
Paints & Chemicals (Pachin)	(1995) 1997	53.75%	8.00%	38.25%	836	3-10-97
Helwan Portland Cement	(6-09-01) (9-11-95) 3-12-96	95.00%	5.00%	0.00%	1202	4-01-97
United Housing (& Construction)	12-02-96	3.11%	7.00%	0.00%	5	21-05-96
Abou Kir Fertilizers	May-96	2.80%	0.00%	0.00%	20	Completed
Medinet Nasr Housing / Construction	13-05-96	64.94%	10.00%	25.06%	190	30-06-96
Egyptian Financial & Industrial Co	26-05-96	64.70%	10.00%	25.30%	70	30-06-96
Egyptian Starch & Glucose	18-06-96	51.03%	10.00%	38.97%	68	10-09-96
Middle & West Delta Mills	30-06-96	51.00%	10.00%	39.00%	177	30-10-96
Nile Matches (and Prefabricated Houses)	Sep-96	55.67%	8.90%	35.43%	34	28-09-96
Kafr El Zayat for Insecticides	(Feb-01)(Sep-96)	85.00%	5.00%	10.00%	60	28-09-96
Misr Oil & Soap	7-08-96	50.92%	10.00%	39.08%	73	17-09-96
Arabia Cotton Ginning	Sep-96	90.00%	10.00%		87	21-12-96
Telemisr	09-1996 (03-1999)	90.00%	10.00%	0.00%	59	25-11-96
Upper Egypt Flour Mills	4-11-96	51.00%	10.00%	39.00%	165	04-11-96
East Delta Mills	18-11-96	51.00%	10.00%	39.00%	110	18-11-96
Nile Cotton Ginning	Jan-97	90.00%	10.00%		295	27-07-97
Misr for Free Shops	2-02-97	87.40%	10.00%	2.60%	133	21-05-97
Cairo Housing (& Construction)	24-03-97	69.38%	10.00%	0.00%	118	29-04-97
Development & EngineeringConsulting	30-04-97	88.00%	10.00%	0.00%	104	21-05-97
Nobareya Agricultural Engineering	14-05-97	79.38%	20.00%	0.62%	27	21-06-97
KABO	11-06-97	63.00%	0.00%	7.00%	197	18-05-96
Middle East Co. for Paper SIMO	22-06-97	75.00%	0.00%	25.00%	55	19-08-97
Upper Egypt Contracting	5-06-97 (4-07-98)	75.00%	10.00%	0.00%	15	29-06-97
Nasr Dehydrated Agricultural Products	11-08-97	90.00%	10.00%	0.00%	24	14-12-96
El Giza Contracting	15-09-97	70.00%	10.00%	20.00%	33	16-11-97
Industrial & Engineering Projects	29-10-97	80.00%	10.00%	10.00%	299	30-12-97
El Nasr Casting	Dec-97	0.00%	32.50%	0.00%	48	24-11-97
Mahmoudia Contracting	17-01-98	69.75%	10.00%	20.25%	54	15-02-98
El Shams Housing	Oct-98	50.46%	5.00%	44.54%	31	13-10-98

El Nasr Civil Works	24-05-98	70.67%	10.00%	19.33%	105	30-06-98
Arabia & United Stevedoring	16-05-9808-11-98	29.50%	21.95%	49.00%	17	11-01-99
Bisco Misr (Second Trench for ESA)	(Jun-00)26-05-98	45.69%	9.3% 8%	45.01% 37.01%	89	Oct-98
Cairo Co. for Oil & Soap	Jul-00	61%	0.00%	39.00%	33	Underway
Total					**6,315**	

Source: Public Enterprise Office

Majority Public Offerings provides details on the sale of companies through the stock market. The table gives the name of the company, date(s) of sale, and the amounts sold to the private sector, the company's ESA and the remaining HC share.

Notes on IPOs: A company whose initial sale was for minority interest is reported as a minority IPO and is then moved to Majority IPO for subsequent sales over 50% in the year of initial sale. **Ameriya Cement** is an example of this reporting method and is why it is not counted as an anchor transaction as reported by PEO in March 2000.

United for Housing and Construction, **Abou Kir Fertilizers**, and **El Nasr Casting** are reported as majority IPOs, however less than 51% is in private sector hands. 51% or more of the company is held by non-MPE government entities. Essentially these companies were 'sold' to other government entities by their holding companies. **Arabia United Stevedoring**, and **Bisco Misr** are also reported as Majority IPOs however less than 51% of the company is in private sector hands.

Privatization Achievements: Majority Sales to ESAs

	Name of Company	Date of Contract	Private Sector	ESA	Remaining HC Share	Total Sale Value (LE Millions)	Approval to Law 159
1	Consulting Office for Irrigation	25-06-94	4.00%	95%	1.00%	1	27-04-94
2	Kom Ombo Valley	15-09-94	4.73%	95%	0.27%	70	27-04-94
3	General for Land Reclamation	10-11-94	4.86%	95%	0.14%	60	27-04-94
4	Egyptian Real Estate	16-11-94	4.70%	95%	0.30%	46	27-04-94
5	General Mechanical Excavation	16-11-94	4.76%	95%	0.24%	23	27-04-94
6	Egyptian Dredging	6-12-94	4.17%	95%	0.83%	19	27-04-94
7	Upper Egypt Dredging	7-12-94	4.80%	95%	0.20%	8	27-04-94
8	Regwa	3-01-95	4.77%	95%	0.23%	28	27-04-94
9	Arabia for Land Reclamation	7-01-95	4.77%	95%	0.23%	61	27-04-94
10	El Beheira Company	16-02-95	3.20%	95%	1.80%	49	27-04-94
11	El Nile for Heavy Transport	15-11-97	-	95%	5.00%	27	18-10-98
12	El Nile for Goods Transport	15-11-97	-	95%	5.00%	24	24-10-98
13	El Nile for Inland Transport	15-11-97	-	95%	5.00%	27	18-10-98
14	Damietta & Bilkas Mills	1-01-98	0.10%	90%	9.90%	49	27-06-99
15	Sharkeya Mills	1-07-98	0.10%	90%	9.90%	39	4-03-99
16	Kafr El Sheikh Mills	27-07-98	0.10%	90%	9.90%	13	19-09-99
17	Rasheed Mills	26-09-98	0.10%	90%	9.90%	12	30-10-99
18	El Beheira Mills	26-09-98	0.10%	90%	9.90%	22	8-08-99
19	Dakahleya Mills	3-10-98	0.10%	90%	9.90%	37	27-06-99

20	Alexandria Mills	10-10-98	0.10%	90%	9.90%	27	10-07-99
21	Marine Supplies & Contracting	19-10-98	-	51%	49.00%	16	5-11-98
22	Amoun Shipping Agencies	4-11-98	44.00%	44%	5.00%	26	11-03-99
		30-01-99					
23	Abu Simbel Shipping Agencies	4-11-98	44.00%	44%	5.00%	26	11-03-99
		(30-01-99)					
24	Memphis Shipping Agencies	4-11-98	44.00%	44%	5.00%	43	11-03-99
		30-01-99					
25	Martrans	10-11-98	44.00%	51%	5.00%	43	11-03-99
26	San El Hagar Agricultural	1-03-99	0.00%	95%	5.00%	18	14-03-99
27	Egyptian for Irrigation	Jan-99	60.00%	30%	10.00%	5	14-03-99
28	Transport Works	1-07-99	0.13%	95.00%	4.87%	12	25-12-99
29	Direct Transport	1-07-99	0.08%	95.00%	4.92%	18	25-12-99
30	Suez Shipment & Auto. Stevedoring	24-10-99	0.1875%	61.88%	6.69%	22	1-02-00
31	Gharbeya Mills	Jul-01	00.0%	90%	10%	51	Underway
32	Misr for Import Export	30-07-01	00.0%	100%	00.0%	17	Underway
33	United for Trade	19-02-02	00.0%	98%	2%	4.9	Underway
34	Arab Textiles	19-02-02	00.0%	98%	2%	5.8	Underway
Total						**950**	

Source: Public Enterprise Office

Majority sales to Employee Shareholding Associations lists the companies in which over 51% of the shares were sold to the company's ESA. (See note 6 on page 18) The table gives the date, value and percentage of sale. The ESA usually has between 5 and 10 years to pay the HC for the company and accumulate board directorships as they pay.

Notes on Privatizations to ESAs: Amoun Shipping Agencies**,** Abou Simbel Shipping Agencies**,** Memphis Shipping Agencies **a**nd Egyptian Irrigation are reported as privatized through ESAs. However, less than 50% is held by the ESA and over 51% is held by both the ESA and the private sector.

Liquidations

	Name of Company	Date	Liquidator
1	Upper Egypt Agricultural*	17-04-90	Ahmed Serrafy
2	West Nobareya Agricultural*	10-11-91	Ahmed Abu Hadab
3	Middle Delta Agricultural*	10-11-91	Farouk Omar
4	Al Nahda Agricultural*	26-11-91	Mahfouz Boutros
5	El Nile for Corps Import*	7-01-92	Youssef Al Hayatmi
6	Cairo for Building & Prefab Houses	15-06-93	Mohamed Shoukri
7	South Tahrir Agricultural*	28-02-94	Mahfouz Boutros
8	Faraskor for Wood	7-05-94	Mohamed Mounir - Abdel Aziz Hareedi
9	General for Foundations	23-02-95	Abdel Halim Abdel Fattah
10	General for Contracting & Sanitary Works	23-02-95	Abdel Moneim Akl
11	High Dam for Civil Works*	18-03-96	Moustafa Nour
12	Canaltex	26-08-97	Badr El Dakar
13	Pre-Fabricated Houses	5-11-97	Saad Salem

14	General for Batteries	1997	Mohamed Rashid
15	Cairo for Silk Textiles	1-07-98	Wageeh Rady
16	Industrial Fittings & Services	13-07-98	Yousry Yousry
17	Graphite & Stationary Co.	15-09-98	Ali Waly
18	General for Metallurgical Wealth	28-09-98	Mohamed Shalakany
19	Maryout Agriculture	17-10-98	Abdel Bary Abdel Bary
20	Egyptian for Leather Tanning	25-11-98	Hosny Mowafy
21	Sand Bricks	6-02-99	Fekry Fashara
22	Egyptian General Agriculture Co.	11-09-99	Hamed Abu Ghaleb
23	General Co. for Production & Agricultural Services	11-09-99	Essam Zerd
24	Egyptian Co. for Meat Production and Dairy	23-09-99	Fardous Badran
25	North Tahrir Agricultural Co.	25-09-99	Mohamed Borhan
26	Egyptian Gypsum Quarry & Marble - Gemco	14-10-99	Sarwat Abdullah
27	Sornaga Rerfractories	29-12-99	Mr. Ali El Din Mohamed Badra
28	General Co. for Engineering Works	8-05-00	Samir Kenaway
29	Egyptian Refractories	13-02-00	Osama Mahmoud
30	United Poultry Production	24-06-00	Hamed Abu Ghaleb
31	Egyptian Electrical Equipment (Shaher)	Jan-01	Eng. Nagwa Fakher
32	Egyptian Company for Metal Trade (Segal)	Jan-01	Mr. Maher Abdullah

Source: Public Enterprise Office
* Liquidation complete

Privatization Achievements: Multiyear Leases

	Name of Leased Assets	Company Name	Date of Contract	Annual Lease LE/$	Duration	Total LE/$Million	Management Company
1	Aga Factory	**El-Dakahlia for Spinning & Weaving**	08-05-97	1, 560,000	5	7.8	N/A
2	New Weaving Factory Mostorod-Kaluobia	**Industrial Shops for Silk & Cotton (Esco)**	15-10-97	$750,000 +3% net FOB for raw material	10		N/A
3	**First Group**: Miami(Cairo)-Al Chark (Cairo)-Radio(Alex)-El Horeya(Alex)-Misr(Port-Said)	**Misr Company for Dist. & Show Rooms**	20-03-99	2,200,000	20	44	N/A
4	**Second Group**: Segal (Cairo)-Roxy (Cairo)-Winter Rio (Alex)-Summer Rio (Alex)-Opera (Sohag)		20-03-99	2,600,000	20	52	N/A
5	**Third Group**: Diana (Cairo)-Winter Normandy (Cairo)-Ferial (Alex)- Rashid (Rashid)		20-03-99	2,500,000	20	50	N/A
6	Menia El Kamh Factory	**El Sharkeya for Spinning & Weaving**	01-07-99	9,000,000	5	45	Islamic Company for Plastic & Weaving**
7	String Dye Factory	**Cairo Dying & Preparation**	Sep-99	336,000	5	1.68	Mr. Said Ramzy Hanna**
8	Fibers Factory		Oct-99	1,600,000	5	8	Mr. Sabry Ishak Missiha and Mr. Emad Sabry Ishak**
9	Galal Studios	**Misr Studios and Cinema production**	02-01-00	379,000	20	7.58	Studio 13 Company for Artistic Production & Distribution**
10	El Ahram Studios		Feb-00	2,100,000	20	42	Egyptian Company for Media Production City**
11	Misr Studios		Feb-00	2,250,000	20	45	El-Exeer for Technical Services**
12	Cinema City Studios		Feb-00	5,400,000	20	108	Egyptian Company for Media Production City**
13 to 14	2 Floating Hotels Anni & Hotob	**Egyptian For Tourism & Hotels**	9-03-00	$1.200.000	5	$6M	N/A
15 to 16	2 Floating Hotels Isis & Osiris		19-04-00	$672.000	5	$3.3M	N/A
17 to 18	2 Floating Hotels Tut & Aton*		3-05-99	$1,000,000	5	$5M	N/A
19	Darphala Factory	**Misr Aluminum**	19-02-01	$14,400,000	25	$360M	N/A
20	Gypsum Factory—Sadat	**GYMCO**	19-02-01	2,000,000	4	$8M	N/A

Source: PEO
* Reported in 2000
** HC reported data

Note: This is an increasingly popular mechanism used by the GOE to transfer management of difficult/troubled companies or assets to the private sector. The table provides the duration, annual amount, total value (when given) and the management company (when available).

Privatization Achievements: Production Assets Sold

	Sold Assets Statement	Owner	Date of Selling/ Contracting	Value/LE millions
1	Cairo Sheraton	N/A	14-11-96	350
2	Al Borg Hotel	Egyptian Hotels	6-11-97	6
3	San Stepheno Hotel: Lands and Premises	Egyptian Hotels	Aug-98	271
4	Siklam Factory	N/A	27-08-98	20
5	Distillation Factory	Egyptian Koroum	8-10-98	26
6	Plastic Factory in Kabari	National Plastics	22-06-99	3
7	Kowar Grinding Balls Factory	Delta for Steel	Aug-99	28
8	Production Line for Yoghurt & Ice Cream	N/A	24-11-99	.6
9	Basatin Factory	Sabi Company	30-11-99	14
10	Tinning Factory in Ghamara	Cairo Metal Products	22-01-00	.6
11	Nile Hotel	N/A	Feb-00	49
12	Agriculture Dehydration factory	Gianaclis	Jun-00	4
13	Oil and Olive Production	Gianaclis	Jun-00	.5
14	Barrel Factory	Alex Metal Products	Jul-00	11
15	Apparatus Factory	Niaza Company	Dec-00	19
16	Nozha Factory	Alex Metal Products	Jan-01	25
17	Minya Factory for Iron Sheets	Alex Metal Products	Jan-01	3
18	Nadler Factory	Alex Confectionary	30-01-01	11
19	Syringe Factory	El Nasr Glass and Crystal	2002	20
			Total	**862**

Source: Public Enterprise Office

Further Notes to Privatization Activity Tables

1. During the fourth quarter 2001, the PEO updated their review of transactions through December 31. These tables are constructed from this PEO data. Companies whose shares were sold in trenches are reported in the year of the largest or most significant sale. The year in which the sale is recorded is given and trench sales are shown with parentheses.
2. The date given in the approval column identifies when a company's general assembly approved the change to Law 159.
3. When percentages do not add to 100%, the information has not been provided.
4. Values are rounded to the nearest million.

Appendix 4: Selected Summary Recommendations from Privatization Studies

1. The Labor Study

Findings and Recommendations

The recommendations of this study take full account and incorporate the relevant findings of the recently completed field survey titled: Effects of Early Retirement on Individual and Households (EERIH), carried out by CARANA/PCSU, on behalf of USAID. The main findings of EERIH relevant to this study are as follow:

1. The Majority of early retirees (ERs), about 82% were over 50 years of age and had between 20-30 years of service.
2. About 75% of ERs were not seeking employment.
3. About 40% of the ERs had quickly spent their cash compensation and were left with only the pension
4. 96% of ERs considered their pension not sufficient to meet their household expenses
5. About 37% of the ERs considered lack of family medical coverage as a major disadvantage in taking early retirement
6. About 37% of ER's would have started a business, but the cash compensation was not sufficient and had no access to credit
7. The majority of younger ERs considered early retirement jeopardized their economic and social goals and status

From the above findings, it can be deduced that a number of modifications are urgently needed for the labor adjustment program to meet its stated social and economic objectives. Most of the required can be made with nominal or no additional costs to the Government. In addition, the government is at risk of loosing the fiscal gains from the earlier successes of the privatization program if the burden of remaining Law 203 portfolio on the government's resources continues. Therefore, the completion of the labor adjustment program, with needed modifications is essential.

Recommended modifications to the program, based on the findings of this and the EERIH studies, are as follow:

- There does not appear to be any need to change the financial value of the compensation package.

- The medical coverage to be extended for the ERs over 50 years of age with qualified members of the families should be extended till normal retirement age, for others during the transition to new employment or say, for a maximum of two years. A study to determine the details of the medical extension and its additional cost should be conducted immediately.

- Develop and implement a coherent, a Pre-ER clear and transparent information dissemination program to increase awareness of all important features of the program, including:

  - Selection criteria
  - Method of lump sum calculation
  - Method of pension calculation

- When the lump sum payment will be made
- Assurance that the program is strictly voluntary
- What happens to employees who do not elect to participate
- Any other benefits workers may be entitled to if they participate

- Develop options to the lump sum withdrawal of cash compensation and individual counseling service. This service should also provide information and assistance in job search, training and starting a new business.

- "Distressed" companies selected for sale, or liquidation, should be given priority for restructuring
- Consider new option for financing of the labor adjustment program and recommended modification. A possible option is to prepare a labor adjustment program to be financed by the donor community (USAID, the World Bank, EU and others). The program's initial investment is estimated as $ 400-500 million equivalent. The framework for the scenario is outlined below:
    - Establish a Labor Adjustment Fund (LAF) in a reputable local private bank, e.g. HSBC, Egyptian American Bank that would manage the fund. LAF would cover the cash compensation package.
    - Establish a Technical Assistance (TA) unit and an Early Retirement Individual Counseling (ERIC) unit. Both units could be funded by the donor community, and if necessary, augmented by the government, HCs or the LAF income.
    - Local and international experts in business development, finance and accounting, and technicians would staff the TA unit. The TA unit would be the preparation and evaluation arm of the LAF. The unit will provide advice on options to and managing the lump sum cash compensation withdrawal, provide advice and assistance on starting up businesses and perform due diligence for the LAF financing.
    - The ERIC unit could be managed by NGO (s), volunteers and professionals, and would provide individual counseling on pre and post early retirement, advice on job search, available training programs referral to the TA unit. The unit could also assist HCs and ACs with development and dissemination Pre-ER information program.
    - Request USAID financing for preparation of LAF and establishment of TA and ERIC units.
- Transitional funding will be required may be to provide adequate flexibility for timely labor force restructuring until the LAF is operational or the Privatization Restructuring Fund is restored to comfortable levels from privatization proceeds. The most viable ways of transitional financing are:
    - Inter-company lending or transfer of excess cash;
    - Asset sales (land, buildings, machinery and equipment, inventories);
    - Leasing, rentals and subletting;
    - Sale/factoring of accounts receivable;
    - Divestiture of passive investments and certain investments requiring active management not tied to core activities;

- Priority privatization of companies that already have in place appropriate debt levels and labor force size for privatization.

The early retirement program should be managed in a uniform and consistent manner monitored by a central authority.

2. Debt Study

Excess Debt. To further examine the debt situation among the Law 203 companies, and the degree to which the debt carried is sustainable, this Study applies the concept of *excess* debt. Excess debt is based on the interest coverage ratio. Excess debt is defined as any debt resulting in interest coverage (defined as the ratio of cash flow to interest expense) greater than a standard, figure 1 bellow.

Figure 1

	Total Debt	*Percent of Total Debt*	**Excess Debt**	*Percent of Total Excess*	*Excess as % of Total Debt*
Chemical	2,811.5	10.7%	1,748.1	13.6%	62.2%
Construction	1,824.3	6.9%	312.0	2.4%	17.1%
Engineering	1,885.7	7.2%	1,617.7	12.6%	85.8%
Food Industries	2,098.6	8.0%	124.7	1.0%	5.9%
Housing, Tourism and Cinema	149.2	0.6%	.0	0.0%	0.0%
Maritime and Inland Transport	127.3	0.5%	123.2	1.0%	96.8%
Metallurgical	6,587.7	25.1%	2,146.5	16.7%	32.6%
Pharmaceuticals	459.0	1.7%	90.1	0.7%	19.6%
Textiles	9,142.9	34.8%	5,808.0	45.2%	63.5%
Trade	1,210.3	4.6%	891.4	6.9%	73.6%
Total	26,296.5	100.0%	12,861.7	100.0%	48.9%

Source: Law 203 database (PEO). See footnote for Table 1. Excess debt calculated per description in text.

Total excess debt of the Law 203 portfolio, using latest available data and the various assumptions presented in the study, is LE 12.9 billion, just under 49% of total debt. Most debt in the four troubled heavy industry holding companies is excess, ranging from 62.2% of the total in chemicals, 85.8% in Engineering, to 63.5% in Textiles.

Debt Groups. There are approximately 190 Law 203 companies still remaining in the Law 203 company portfolio. For the purposes of further analyzing the level of debt and excess debt, the portfolio has been separated into three classes based on their level of excess debt.

- *Group 1:* Those profitable companies which are able to easily service their debt, that is, their cash flow is more than 2.0 times interest payable on debt during the most recent annual period. By definition, they have zero excess debt.

- *Group 3:* Those companies that have negative cash flow before interest payments. No amount of debt restructuring alone will bring them to a position of being able to service their debt, because their operating losses before debt service are already too large. By definition, all debt is excess, since loss-making companies cannot service any of their debt.

- *Group 2:* Those companies that have positive but insufficient cash flow to comfortably cover interest payments, i.e., companies with cash flow coverage less than two times interest payments.

Of the 173 companies for which data was available, 53 companies with over 59 % of the total Law 203 company debt fall into Group 2, those for which debt restructuring might make a difference. Because they have negative cash flow, Group 3 companies are assumed to have no ability to repay debt in the future. The 25 Law 203 companies with the largest excess debt account for LE 9.4 billion, or almost 73% of the total.

Debt Restructuring to Date. It is not perhaps widely known that the Law 203 Holding Companies have already undertaken a large amount of debt and labor restructuring, over a period of many years. In fact, our survey of six HCs showed that LE 10.2 billion in bank debt has been restructured through negotiations with creditor banks, over the past

several years. The credits that were restructured were dramatically (over 60%) reduced, through a combination of payments, debt forgiveness, and changes in loan terms and conditions.

A Recommended debt restructuring policy. In this period of declining resources, the question becomes not only HOW to maximize the amount of debt restructuring, but WHERE to focus resources. The remainder of this study explores the goal of *focusing all debt restructuring resources on Group 2 companies*. In general, Group 2 companies are those for which a reduction in debt should make a difference in how easily they could be sold for more attractive prices. Group 1 companies should be able to be sold as they are, or perhaps with limited labor or unbundling restructuring. The corollary to this observation is that *no debt restructuring should be carried out on Group 3 companies.* The banks have no choice but to accept this situation, since they are not willing to step in and take the assets.

The study addresses a number of objections to this proposal, including the responsibility olf the Holding Companies to the Banks.

The Privatization Restructuring Fund as a Source of Funds for Debt and Labor Restructuring. Privatization proceeds are the traditional source of much of the debt and labor restructuring of Law 203 companies. Through the end of 2000 over LE 13.1 billion have been generated by privatization sales, LE 5.8 billion in proceeds have been transferred to the Ministry of Finance, or 44% of proceeds. To put this figure into perspective, total government revenues for 1998/99 were over LE 73 billion.

Before 1999, decisions about the utilization of privatization proceeds were made more at the holding company level. Each HC kept 1/3 of its own proceeds, with the remainder passing to the Ministry of Finance. In the 4th quarter of 1999, to standardize the procedures for using proceeds in debt and labor restructuring, a Restructuring Fund was created. The Prime Minister approved legislation at the same time to allow the Ministry of Public Enterprises to keep 50% of sales proceeds of its privatized affiliates, as opposed to 1/3 previously. Since its creation, over LE 1.3 billion has been paid to the Holding Companies, for restructuring purposes. Over 50% of the Fund's payments were spent on Debt Settlement, and 32 percent on Early Retirement. LE 293.1 (17% of the total) has also been used for "technical and management restructuring", in spite of the spirit of its original design.

Unfortunately, the Fund now finds itself in the position of having relatively little new inflow, while demands on the Fund, particularly for the restructuring of "loss-making companies", are reported to be far in excess of cash available. The Restructuring Fund also creates some unproductive incentives for the Holding Companies. HCs keep none of the proceeds of any sale of shares – the proceeds flow directly to the Restructuring Fund and the Ministry of Finance. There is thus little incentive to privatize AC shares, since the funds generated cannot be used by the HC and are lost. There is reportedly an "agreement" that gives HCs the right to use privatization proceeds to retire debt assumed by the HC during a privatization transaction.

HCs are thus much more likely to pursue the sale of assets owned by the affiliated companies directly, where all proceeds stay in the AC for later use within the AC or the HC. This partially explains the recent increase in asset sales by indebted HCs.

Simulations of future Restructuring Fund Policy. To review and quantify the impact of our recommended strategy, and to review the impact of a number of different assumptions, the PCSU has created a Debt Restructuring Simulation Model of the Law 203 Holding Companies and the Restructuring Fund. The details of the model, its construction, and the assumptions behind it are presented in the appendix and in Appendix III. The model should not be used to *forecast* the privatization proceeds or debt or labor restructuring needs of a particular company. The model's value lies in understanding the implications of certain assumptions for the entire portfolio.

Based on a variety of assumptions, the model projects that the total amount of required debt and labor restructuring to privatize the companies is over LE 8.4 billion. Total privatization proceeds are projected to equal LE 10.6 billion, yielding LE 5.3 billion for the restructuring fund. The model assumes that 139 companies are privatized over the next four years. (Any proceeds from Group 3 liquidations and non-privatizations are not included.) In order to achieve that level of privatization, the HCs had to assume all of the excess debt and labor of the Group 1 and 2 companies. (By definition, excess debt is that debt which must be retired in order to successfully privatize.)

The LE 3.4 billion shortfall in the Restructuring Fund sources for companies in Groups 1 and 2 highlights the problems faced by the Fund, even before beginning to address the substantial Group 3 debt and labor restructuring. It confirms the discussion of the first section: the appropriate policy for debt restructuring is to withhold all debt restructuring from Group 3 companies. Funds are simply not available.

Review of additional opportunities for restructuring the debt of Group 2 companies in order to make it easier to privatize them. As highlighted in the prior section, proceeds from sale of Group 1 and Group 2 companies will be insufficient to meet Group 2 demands, much less those of Group 3 companies. However, there are other possibilities beyond the Restructuring Fund for generating additional funds for affiliate companies to use to reduce excess debt (or for labor restructuring), instead of using limited Restructuring Fund resources.

Holding companies and affiliate companies (Groups 1,2 & 3) as a whole can provide substantial cash from internally generated sources such as:

- Use of excess cash
- Sale of non-core and/or un- or under-utilized assets
- Collection of past due and current receivables
- Leasing of unused or under-performing assets
- Liquidation of highly troubled companies
- Factoring or sale of receivables

The model generated projects that the level of excess assets approaches LE 4.3 billion. It indicates that there is untapped cash potential within the Law 203 companies. *The result is that using cash from excess assets to "pre-restructure" certain ACs could result in the* *application of LE 1.4 billion of cash from internal restructuring to debt and labor restructuring, resulting in a reduction of the deficit at the Restructuring Fund, to LE 1.7 billion.*

An Action Plan. The actions which the GOE should take in order to increase the sale of Law 203 companies and to better manage privatization proceeds are:

- Prioritize restructuring efforts on Group 2 companies.
- Promote Restructuring Fund policies that will maximize incentives for Holding Companies to privatize and maximize restructuring.
- Set up a high-level commission to aggressively manage the generation of internal resources. As an added incentive to holding companies and affiliate companies, it might even be worthwhile for the Restructuring Fund to require that before any consideration is given to using Restructuring Fund resources for an affiliate, that the company demonstrate that it has exhausted all internal resource options.
- Actively use and enhance the Debt Restructuring Simulation Model.
- Use realistic, market-based valuations in setting the sales price of Law 203 companies.

It is clear that there are significant opportunities to generate additional cash for debt and labor restructuring, leading to a noticeably higher potential for selling Group 2 companies. In addition, use of the Restructuring Fund model can provide its managers with a tool to better predict and prioritize needs and what can be done to address them.

All of this comes to naught, however, if the model is not actively used, and if there is not an extremely serious, continuing and tightly managed effort to generate internal cash from the affiliate companies. Ideas are only as good as their implementation, and implementation only as good as the implementers and those to whom they report. It is critical to the success of this proposed program that the Minister of Public Enterprises, the Ministerial Privatization Commission, and the Prime Minister take responsibility for ensuring its successful implementation. Without that commitment, it is likely to fail.

3. Alternative Privatization Methods Study

<u>Summary Recommendations</u>

<u>Law 203 Company Privatization</u>

- *Institutionalize market-based valuation techniques*
- *Treat small Law 203 companies differently, and allow pre-approvals of sales for smaller companies*
- *Develop standardized procedures for the tender and pipeline processes*
- *Reduce and mandate negotiation periods for all sales*
- *Facilitate payment by installment*
- *Develop rapid batch tendering strategy to accelerate privatization of smaller companies, and develop RBT procedures and a centralized tender office for RBT transactions*
- *Create a centralized auction office for Law 203 assets and shares, and develop auction mechanisms and procedures*
- *Develop packaging "Tool-Kit" of best packaging practices*
- *Provide training in packaging and deal structuring as required.*
- *Work to show long-term benefits of privatization*

<u>Intermediate Privatization Vehicles</u>

If the purpose of an IPV program is to transfer shares of state-owned institutions to an IPV in the hopes that the IPV will be more objective and less politically influenced in its privatization decisions than the current holders of the shares, then the establishment of an IPV program is not in the best interests of privatization. If the political will exists in Egyptian society to transfer shares in JVs held by state-owned institutions, then the privatization of the JVs could take place without the expenses of an IPV. More importantly, privatization of the JVs could be done without the disadvantages and shocks to the financial system that would occur with the removal of the shares from the state-owned banks' and insurance companies' portfolios.

An IPV should only be used in Egypt if the intention of the government is to private a broad ownership base for privatized companies in the Egyptian society in the course of a mass privatization program. The main advantage of an IPV is to provide the general public with a diversified participation in a mass privatization program. In order to be successful, the management of the IPV would need to be independent and capable of making decisions regarding the company on economic rather than political grounds. The IPV should be partially financed by the investing public who would pay for the shares in the IPV, thus partially compensating the state-owned banks and insurance companies for their assets. The proceeds from the sale of shares in the fund should be split between the fund and the state-owned institutions that transferred the shares. Finally, the IPV would need to have a sunset provision so that it would terminate as a privatization fund and convert into a mutual fund after a determined period of time.

4. Strategies for Privatization of Distressed

Within the overall reform program, this report focuses on 49 distressed companies. These companies are owned and managed by ten separate holding companies: (i) Spinning and Weaving; (ii) Engineering Industries; (iii) Metallurgical and Mining Industries; (iv) Chemical Industries; (v) Construction Industries; (vi) Food Industries; (vii) Maritime and Inland Transport; (viii) Trade; (ix) Pharmaceutical Industries, and (x) Tourism, Housing and Cinema. Two of the ten holding companies -- Spinning and Weaving and Engineering Industries -- have the largest exposure in terms of employees (more than 70% of the total distressed companies), assets (more than 85% of the total assets and liabilities), and operating financial losses (also a significant share).

1. Forty-three textile companies are listed under Law 203, of which only 14 are slated for privatization. The remaining 30 companies have limited potential for privatization due to their relatively poor and unattractive current financial conditions. However, these remaining companies represent more than 50% of the labor force and more than 70% of the assets of the total textile sector companies under Law 203. This segmented or partial approach yet again delays the necessary sector reforms that are necessary to accompany the privatization of distressed companies in the textile sector.

2. Within the 14 distressed textile companies slated for privatization, revenues have declined by more than 50% in the past three years, while cost reductions have not kept corresponding pace. These companies are facing rapid deterioration in earnings and labor productivity. Ownership change, if possible, may not solve the sector's long-term viability and sustainability.

3. To further expedite the privatization process for distressed companies, the government requested assistance on two specific areas: (i) Valuation techniques and the "total bid package"; and (ii) Debt/equity swaps.

Valuation Techniques:

The determination of valuation is a matter of judgment, irrespective of the technique used in the valuation process; it will have to be defended to taxpayers, the other stakeholders who invest and the managers who will have to assume responsibility and custody over the assets. There is no single technique that is considered acceptable or correct. Based on the use of these techniques, valuation results can vary significantly. However, given the subjective nature of valuation, ultimately it is the market that will determine the price of the asset. In the case of trade sales, this will involve negotiations with the government about the fair price. Many governments have tried to increase the level of transparency by eliminating and/or reducing the subjective interventions.[ii]

However, there are many qualitative factors that are not captured in the rigid quantitative methods. The significance placed on qualitative characteristics cannot be discounted and must not be overlooked. Some examples are:

- World political and economic factors (flow of direct foreign investment, current industry trends, availability of capital in the international markets, etc.);

- Country political and macroeconomic factors, state of government, perceived risks, economic stability, corporate governance, etc.;

- Company profile (market share, company size and critical mass, labor relations, strength of competition, technological capabilities and expertise, strength of customer-vendor relations, competence and ability of management), and

- Extraneous factors, availability of financing, interest by "credible" foreign companies, market positioning, timing of sale, opportunity cost-benefit from the sale of assets, sector competitiveness, cost of transaction, payback, etc.)

At best, the valuation of assets is an art. It is influenced by institutional, macroeconomic and personal factors. In Egypt, the only valuation method recognized by the Central Auditing Authority (CAA) is "replacement value", making it difficult for shareholders to propose prices based on market-oriented principles, creating potential dilemmas for the government and the CAA. Furthermore, this reliance on a single dominant methodology/technique has unnecessarily delayed the overall privatization process and introduced an element of uncertainty regarding the pricing and sales decisions. One of the strategies the government implemented was to float a small number of shares in the stock market (IPOs) to let the market determine the price. This technique is acceptable, and should be encouraged; however, it is generally limited to profitable companies, which have established a proven track record of financial performance. In the case of distressed companies, this approach may not be viable and sustainable.

Some Suggestions on Valuation Techniques

The issue of selling distressed companies is not one of valuation techniques or a lack of qualified staff to undertake complex financial analysis, but rather an assessment of objectives and priorities. If the overall privatization objectives were to achieve economic growth and employment and encourage higher levels of private investments, then appropriate valuation strategies and processes would be in place. At the moment, the objective is to reduce the size of the fiscal deficit, which necessitates higher valuation techniques.

Distressed companies have some unique and common financial characteristics. They are loss-making entities, operating in "old" industries, functioning primarily to protect labor and *not* markets, technologically obsolete and not responsive to customer needs. Under these conditions, traditional financial valuation techniques can only provide a reference point or a negotiating position and not a key decision in the process for sale. Therefore, in the case of distressed companies, the traditional financial valuation techniques should be replaced by a much broader set of parameters that include the following changes in strategy, structure, process and techniques:

- The current privatization objectives for distressed companies should focus more on growth, competition and employment creation rather than an inward fiscal orientation. This change in the government's objectives would send a favorable signal and induce changes in process and methodologies.

- The major responsibility of CAA should be to review methodologies employed by private investors and comment on their accuracy and consistency. Currently, the CAA has the statutory responsibility for technical valuation of all government assets. This authority places overdue restrictions on the negotiation process between the government's team and the private investors.

- The decision on awarding a winner in the sale of distressed companies should be based not solely on price, but rather an integrated business strategy and plan. The traditional approach in awarding contracts has been the assignment of assets to the highest bidder based on price. This procedure has merits as it eliminates any subjective intervention in the process. However, in the case of distressed companies, this may not be the most useful methodology as there are other important factors. The following factors have been used actively in other countries in awarding contracts to the winning bidder:

PROPOSED SELECTION CRITERIA AND WEIGHTS

Factors	Max. Points	For
Bidder's Experience, Personnel and Business Plan	25	Presentation
Basic Investment Plan (Amount and Quality)	35	Highest
Additional Investment Proposal	5	Largest
Former Employees to be retained	15	Highest
Community and Environmental Linkages	10	Presentation
Improving Competitiveness and Exports	5	Largest
Financing Offer	5	Best Offer
TOTAL	**100 POINTS**	

The proposed total bid package is not without its shortcomings. The selection based on a combination of investment, price and employment criteria is subjective as to the relative weights for each factor. However, it is a proxy to ensure that the government's interests are being taken into consideration by the potential bidders.

- The government, with the assistance of its advisors (Promoters) should encourage, where possible, multiple bids for the sale of distressed companies. If there is one potential bidder, it is difficult for the government's negotiating team to optimize its results. Where possible, every effort should be made by the promoter to introduce more than one bidder for each transaction.

Debt/Equity Swaps:

The Government of Egypt has recently announced its intent in using debt/equity swaps as a mechanism in fostering its privatization program, especially for distressed companies. However, experience with the use of this instrument within Egypt is limited. This section focuses on the general description of the use of debt/equity swaps within an international framework, some preliminary suggestions on how it could be used within the Egyptian context, and a description of the regulatory framework and key features of this program in selected Latin American countries.

The debt/equity conversion scheme, while by no means a panacea for ending the debt crisis, is one of the many practical approaches that relieves the debt burden, stimulates new investment, and provides for some liquidity in the frozen credit situation. Furthermore, it is one of the means that has been actively used to achieve faster change of ownership by using external debt bonds.

The early debt/equity conversions completed in Chile, Mexico and the Philippines were market-driven mechanisms that have facilitated in the formation of international joint ventures. They are distinct in the sense that they are motivated largely by financial, rather than technological or market issues.

Suggestions on Debt/Equity Swaps

Debt/equity swaps have been actively used as market-based solutions to address the issues arising from the debt crisis. However, the success of the debt/equity swap program depends, to a large extent, on the host government's commitment to undertake practical short-to-medium term alternative solutions to promote foreign investment and privatization. This instrument may not be most readily applicable in the Egyptian context for the following reasons: (i) PE debt is significantly denominated in local currency; (ii) foreign investment in distressed companies has been, and could remain, limited given the current investment overhand; (iii) the legal, regulatory and financial institutions are not yet prepared in undertaking this program; and (iv) the return of flight capital does not seem to be a government priority, as was the case in Chile and many other countries. However, to implement a debt/equity conversion program successfully, the Government of Egypt may wish to consider the following policy, regulatory and institutional actions:

- ***Establish a transparent, simple framework with minimum administrative procedures.*** Such a policy framework could include the following elements:

    - ✓ Link the Rescheduling Agreements with the objectives and priorities of the government's program;

    - ✓ Clarify foreign ownership and management issues with regard to the repatriation of profits and dividends, etc.;

    - ✓ Define the role of the local investors and how they may participate in the program. In the case of Chile, the participation has had a favorable impact on return of foreign flight capital;

    - ✓ Ensure that the impact of the implementation of the program on pre-established money supply targets; and

    - ✓ Maintain consistency between this program and other foreign investment and know-how transfer promotion policies.

- ***Assign managers with strong financial and economic capabilities to execute the debt/equity conversion program.*** A "top notch" team should be established to include corporate financial restructuring skills that encompass an understanding of the international capital markets, the structure of discount and differential of exchange rates, etc.

- ***Support and deepen the local capital markets.*** Resources required by the private sector to implement the conversion program need to be available through supportive local capital markets. Fund-raising in the public sector should force business managers to focus more closely on corporate performance, investor rewards and greater efficiencies and strategies.

4. These two tools -- valuation and debt/equity swaps -- may not by themselves achieve the government's objectives in expediting the privatization of distressed companies. In order to achieve more timely and measurable results, the government should re-examine the current structure and process for the privatization of distressed companies. This re-examination is important in light of the following factors: (i) current political and investment climate in the region, which has increased political risk; (ii) private capital flows are declining, especially to old age industries; (iii) the institutional framework is relatively diffused and the process remains unclear and not transparent; and (iv) the current state of these companies are unattractive unviable.

5. Therefore, to assist the government with the privatization of distressed companies, the following suggestions are proposed:

Other Important Suggestions

- ***Introduce greater flexibility in the current legal framework.*** The current legal framework is not entirely conducive for the privatization of distressed companies. The current law makes specific reference to the maximization of valuations, the interests of minority shareholders are not well protected and accessing funds on a timely basis for restructuring prior to the sale of the distressed companies. These legal obstacles should be addressed specifically and laws amended in order to eliminate delays.

- ***Centralize the decision-making process for the restructuring and privatization of distressed companies.*** The decision-making process for distressed companies is highly diffused and fragmented among various government agencies. There is no central focal point in expediting the decision-making process, which is one of the essential prerequisites in privatizing distressed companies. Potential investors are generally looking for "bargain" opportunities and are extremely savvy in financial valuations. These investors generally need quick turnaround decisions and credible, timely and reliable information. Therefore, given the complexities involved in the privatization of the distressed companies and the requirements and profile of the potential investors, the government should centralize and streamline the decision making process for distressed companies.

- ***Establish a small multi-disciplinary team with vested authority for implementing key actions with an in-built exit strategy and incentive program.*** Although some 30 people are involved in coordinating the government's reform program in the PEO's office, most of the staff is not well versed in issues involving complex restructuring aspects. Due to the many and interwoven nature of distressed companies, the government should consider establishing a small multi-disciplinary team of very high caliber international professionals (preferably of Egyptian origin). The small team should consist of lawyers, financial analysts, economists, labor specialists, sector specialists, and communications and political relations specialists. This team should have a contract for no more than two years with a retainer salary structure and a highly attractive and lucrative bonus program. The head of this small technical team should have the political authority, trust and managerial authority to undertake and implement the program. It would streamline the decision-making authority within the government's program, as well as minimize the issues of timely reliable data and lack of transparency.

• ***Undertake a "sectoral" approach to the reform program versus an individual case-by-case transaction.*** The privatization process is currently undertaken on a case-by-case basis with limited adherence and attention to sector policies, competitiveness and strategy. In many cases, distressed firms cannot be sold because of their lack of competitiveness, on-going financial losses and relatively poor business environment. This overall framework provides for obstacles and limitations to the promotion of private sector participation. In the case of the affiliated firms in the spinning and weaving group, the entire "value-added business chain" of the sector seems to be highly distorted because of the poor and unreliable supply of raw materials, limited incentives in promoting sectoral growth and international competitiveness, and weak domestic and international distribution chains. The attractiveness and competitiveness of the spinning and weaving sector could greatly enhance its competitiveness if the government undertook an overall sectoral reform as opposed to an individual affiliated company approach. Without accompanying sectoral reforms, ownership changes by itself in the spinning and weaving sectoral may not achieve the desired reforms and objectives.

• ***Redefine the role, selection criteria and compensation structure of the promoters.*** There are too many promoter firms with limited experience who have been short-listed on the government's privatization program. According to most international standards, this would be considered a long, long list of "bankers". The government should draft specific terms of reference for all 14 affiliated companies slated for privatization within the Spinning and Weaving Holding Companies group. The role of the investment banker must be all encompassing and must be highly proactive and include active participation in the strategy formulation and marketing campaigns. The terms of reference should include, among other factors, assistance on: (i) the definition of Egypt's textile policy and competitive strategy; (ii) the restructuring and sale strategy for the 14 affiliated companies; (iii) an action plan and road-map for marketing these affiliated companies to a list of international and domestic firms; and (iv) negotiating the transfer of assets and drafting the shareholder agreement for eventual sale. Based on this broader scope, the existing short-listed firms should be invited to present their proposals. The top three investment banking firms with the highest technical qualifications, as per agreed selection criteria, would be invited to present their financial bids. The government would fairly compensate the winner based on a combination of a retainer fee structure and appropriate incentives for success fees.

• ***Emphasize elements of the total bid package in awards versus solely based on price maximization.*** The total bid package emphasized a much broader base than price in the selection of the winning bid. The bid package looks at a range of elements that are important in meeting the government's overall objectives of employment, investment, financing, etc. It has been used effectively in defining the criteria for the winning bidder.

6. In conclusion, there are no simple techniques and easy solutions in privatizing distressed companies. The over-arching success is to: (i) find creative solutions; (ii) develop aggressive marketing plans for luring potential investors; (iii) streamline decision-making procedures; and (iv) ensure that the patient recovers while in "intensive care", setting a time frame for "recovery". In addition, the government should explore options for restructuring (merger or consolidation of assets), liquidation or closure of the company, in order to reduce the ongoing adverse risks and continued financial drain.

5. Corporate Governance Study

1. The draft companies law should be harmonized with the new capital markets and depository laws after their enactment.
2. The draft companies law could include a list of specific responsibilities for the Board of directors. It could also recommend the mandatory creation of audit and other committees of the Board.
3. All parties (the Holding Companies, regulators, the securities industry, and issuers) should encourage rapid conversion of registries and depositing of shares into the MCSD.
4. Careful attention should be paid to companies with relatively large numbers of shareholders not maintained by the MCSD. A review of off-exchange transfer procedures may be worthwhile.
5. Egypt does not comply with one-share/one-vote. Although this is not an OECD requirement, international investors encourage it.
6. To the extent it is not covered in the new Capital Markets Law, insider trading should be made illegal, as part of the executive regulations, and steps should be taken at enforcement.
7. Per the OECD Principles, "Votes should be cast by custodians or nominees in a manner agreed upon with the beneficial owner of the shares."
8. The laws and procedures related to shareholder appeals to the CMA and shareholder arbitration should be reviewed, and lessons learned should be incorporated into the Executive Regulations of the new Capital markets Law. Contractually binding arbitration may be a good solution to the problem of a slow court process.
9. The restrictions on the use of proxies and the blocking of shares required at annual meetings represent an unnecessary burden on shareholders, and are out of line with international standards. A working group should be convened to study the entire question of voting rights, procedures, and proxies, with the final goal of drafting provisions for the new draft company law that will modernize voting procedures and the use of proxies.
10. The working group should also explore mandatory cumulative voting as a way of increasing minority representation on closely held Boards.
11. Imposing a duty of loyalty of another fiduciary duty on controlling shareholders and/or officers of the company is a direct approach to reducing the risk of expropriation of minority shareholders. It should be investigated if these obligations could be inserted into the draft Uniform Companies Law.
12. The laws regulating Board conflicts of interest should be reviewed in the draft law.
13. To the extent not addressed in the new draft Capital Markets Law, takeover regulation should be reviewed to ease the regulatory burden as much as possible.
14. The CMA should be the "relevant administrative authority", the official guarantor of corporate governance in Egypt, and should work hand-in-hand with the Companies department to regulate the activities of joint stock companies.
15. The Ministry of Economy and the CMA should develop a strategy for future development of accounting rules, application of the accounting standards, and improving the training of the accounting profession.
16. The CASE should be supported in a vigorous enforcement of its new listing rules, even if large number of delistings should eventually result. Delisting should only take place once all other alternatives and penalties have been exhausted.
17. The CASE should encourage compliance with all aspects of the new rules, including the crucial data on ownership structure, names of directors, bank relationships, voting rules, etc.
18. The revision to the company law (and any work towards a code of best practice) should include a review of holding company law and practice. This area is a potentially large problem for shareholder rights.
19. Egypt should begin the process of putting together a code of best practice. The Code should specifically address the Management Oversight / Board Structure issues. Shareholder rights and disclosure issues that are raised can be inserted into Law and Listing requirements. Some countries to look at as models are Korea, Brazil, and especially Mexico, whose economies were similar in structure to Egypt. Moving quickly is important because the some of the Best Practice Committee's recommendations could be incorporated in the final version of the new Uniform Companies Law and perhaps even the Capital Markets Law. Moving quickly would also show Egypt's eagerness to embrace foreign investors and the global capital market.