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PROGRAM INFORMATION DOCUMENT (PID)
APPRAISAL STAGE

November 13, 2016
Report No.: 111275

Operation Name	Second Fiscal Consolidation, Sustainable Energy, and Competitiveness Programmatic Development Policy Financing
Region	Middle East and North Africa
Country	Arab Republic of Egypt
Sector	General energy sector (50%); Macro-Fiscal Management (30%); Trade and Competitiveness (20%)
Operation ID	P161228
Lending Instrument	Development Policy Lending
Borrower(s)	Arab Republic of Egypt
Implementing Agency	Ministry of International Cooperation
Date PID Prepared	November 13, 2016
Estimated Date of Appraisal	November 30, 2016
Estimated Date of Board Approval	January 12, 2017
Corporate Review Decision	*November 23. 2016*

I. Country and Sector Background

Egypt, the largest country in the Middle East and North Africa region (MENA) with a population of 91 million, and the fourth largest economy, is at an inflexion point within a region combatting instability and conflict and, on the domestic front, with a recognition that vigorous reforms are needed to address some of the long-standing structural constraints to inclusive growth and macroeconomic stability. The 2011 Arab Spring—generated by the long-standing weaknesses in public service delivery, incapacity of growth to produce positive social outcomes, and weak competition and transparency—ushered in a new era. However, the economic dividends of post-2011 reforms have not fully materialized in Egypt. In fact, over the past five years, domestic barriers to inclusive growth, including poor governance, uncertainty linked to the post-2011 political transition, significant economic distortions such as an overvalue exchange rate and an inefficient foreign exchange allocation system, a business environment characterized by lack of competition, and an energy sector that held back rather than powered economic activity, were compounded by external shocks in the form of terrorism, regional instability and declining workers remittances from Gulf countries.

This DPF series is part of an international package and supports the Government of Egypt's economy-wide reform program, which aims to bring the economy back on track amidst macroeconomic and social vulnerabilities. It has been prepared in close coordination with the African Development Bank, which co-financed DPF1 and is expected to provide parallel financing of around US$500 million for DPF2, and is closely aligned with the IMF's three-year, US$12 billion Extended Fund Facility (EFF), which was approved on November 11, 2016.

II. Operation Objectives

The DPF series is built around three pillars, which are also the Program Development Objectives (PDOs) of this operation: (1) advance fiscal consolidation through higher revenue collection, greater moderation of the wage bill growth, and stronger debt management; (2) ensure sustainable energy supply through private sector engagement; and (3) enhance the business environment through investment laws, industrial license requirements as well as enhancing competition.

III. Rationale for Bank involvement

This is the second operation in a series of three DPFs, covering the period 2015-17. Although there are important risks, including from the macroeconomic and reform implementation perspectives, the proposed DPF series will play a key strategic role in deepening Bank support for Egypt's much needed structural reforms. The Bank's engagement will also provide global lessons and experience relevant for reform sequencing and implementation.

IV. Tentative financing

Source		(US$, millions)
Borrower		0
International Bank for Reconstruction and Development		1,000
	Total	**1,000**

V. Institutional and Implementation Arrangements

The Ministry of International Cooperation is the main coordinating agency for monitoring and evaluation among the five other participating ministries. The Prior Actions detailed in this operation are the prime responsibility of five ministries: Ministry of Finance; Ministry of Electricity and Renewable Energy; Ministry of Petroleum; Ministry of Planning and Ministry of Trade and Industry. The inter-ministerial working group created for the DPF remains functional. The Ministry of International Cooperation is the coordinator with other ministries on monitoring of the results indicators, which are based on routinely published sector indicators.

The program outcomes are being monitored through the measurement of the progress toward the achievement of results indicators included in the policy and results matrix. The Ministry of International Cooperation has the responsibility of presenting the information related to the reform implementation and progress made towards results on time and in a format satisfactory to the Bank.

VI. Risks and Risk Mitigation

The overall risk rating of this operation is high. The major risks that could have a substantial impact on the operation's ability to achieve its development objective include: (a) macroeconomic challenges associated with high fiscal deficit and low levels of foreign exchange reserves; (b) political and governance challenges; (c) challenges on sector strategies; and (d) ability to enhance social protection in time under weak institutional and implementation capacity. These risks, if materialized, could singularly or jointly impact the Government's willingness and ability to implement the reforms or make the outcome of the development agenda less successful.

However, the risk of not engaging outweighs the program risks: The region is experiencing an unprecedented turmoil with ongoing conflicts in Egypt's neighborhood. Managing regional stability, promoting sustainable growth, social inclusion and impact of displacement require the highest consideration of the global policy makers; where Egypt's political, economic and social stability is essential. Any risk for instability in Egypt has enormous implications for the region, Europe and the wider global community. Egypt has taken significant steps towards sustainable private sector led growth that is focused on job creation, and the World Bank Group has a unique opportunity to realign its relationship and facilitate the continued implementation of Egypt's reform program over the medium term, complimenting with IMF's proposed three-year program on Extended Financing Facility approved on November 11, 2016.

VII. Poverty and Social Impacts and Environment Aspects

The GoE is undertaking a number of deep and structural reforms, the benefits of which will take time to be realized and may have adverse distributional impacts in the short term. The overall direct impacts of the reform package due to electricity tariff increase, VAT and fuel price adjustment amount to a little over 2 percent of the household budget, which is not insignificant but still relatively small. These direct impacts are broadly neutral across the income distribution, geographic areas and gender of head of household. Fiscal transparency measures such as citizen budgets can educate the public about the government's activities and help build public support for difficult policy reforms provided there is a strong outreach to citizens to raise awareness about such measures. The GoE has committed to enhancing social protection through reallocation of EGP 21 billion of budget across schemes linked to enhanced food subsidies, increase targeted cash transfer program to additional 700,000 households from 1 million households reached already, increased social pensions, and specific schemes covering Upper Egypt including enhance coverage of children meals in schools, gas connections, and public works.

The policies supported by the proposed DPF are not likely to have negative impacts on the country's environment or its natural resource base. The World Bank assessed whether specific country policies supported by the DPF are likely to have significant effects on the country's environment, forests, and other natural resources. The assessment concluded that the proposed DPF operation is expected to result in overall positive effects on Egypt's environment and natural resources. Pillar 2 of this proposed operation, which pertains to enhancing sustainable energy supply, comprises a number of policy interventions that are expected to bring about significant changes in the country's energy profile, in particular an increase in fuel switching to natural gas in electricity generation and by the production sectors of Egypt. Other planned changes include the shift toward more renewables in the electricity generation mix. Furthermore, it is anticipated that the planned gradual increase in electricity tariffs will lead to lower consumption through rationalization and higher efficiency of use. These interventions will clearly result in environmental benefits that are to be realized through the decrease in greenhouse gas (GHG) emissions, which contributes to Egypt's climate change agenda; decrease in lower emissions of air pollutants; and thus contribute to a reduction of health risks and improvement of air quality.

VIII. Contact point

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