

PROJECT INFORMATION DOCUMENT (PID) CONCEPT STAGE

Report No.: PIDC18609

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| Project Name | Equal Access and Simplified Environment for Investment (EASE) in Egypt (P153487) |
| Region | MIDDLE EAST AND NORTH AFRICA |
| Country | Egypt, Arab Republic of |
| Sector(s) | Public administration- Industry and trade (100%) |
| Theme(s) | Regulation and competition policy (40%), Micro, Small and Medium Enterprise support (40%), Managing for development results (20%) |
| Lending Instrument | Investment Project Financing |
| Project ID | P153487 |
| Borrower(s) | Government of Egypt |
| Implementing Agency | Ministry of Investment, Ministry of Industry, Trade, and Small Industries |
| Environmental Category | C-Not Required |
| Date PID Prepared/ Updated | 10-Dec-2014 |
| Date PID Approved/ Disclosed | 29-Jan-2015 |
| Estimated Date of Appraisal Completion | 16-Mar-2015 |
| Estimated Date of Board Approval | 08-Jun-2015 |
| Concept Review Decision | Track II - The review did authorize the preparation to continue |

I. Introduction and Context

Country Context

The revolutions that started in Egypt in January 2011 led to a tumultuous period marked by instability, stagnating growth and per capita incomes, rising unemployment and poverty, and setback in population growth rates. Egypt went through two regime changes and presidential elections in the space of just three years, with periods of unrest, uncertainty, insecurity, and violence that have left the population eager for stability and direction. With a new constitution adopted in January 2014 and parliamentary elections expected in January 2015, the political landscape has evolved quickly while the economy is only just beginning to show signs of recovery.

The Egyptian economy had achieved high growth rates during 2004-2008, however, the global financial crisis of 2008, followed by the unrest and uncertainty associated with the 2011 revolution, led to a slowdown in economic activity. Overall social conditions have been deteriorating, in

tandem with the economic downturn since 2011. The unemployment rate reached 13.3% during the last quarter of FY14 (April-June 2014), marginally lower than the rates recorded since the beginning of FY14. Out of the 3.7 million currently unemployed, some 70% are between 15 and 29 years old, making youth unemployment a key challenge for economic inclusion and stability. The latest poverty data indicate that 26.3% of the population has been living below the national poverty line in FY13, with poverty rates reaching 50% in rural Upper Egypt. The loss of formal employment has been a key reason for households falling into poverty. This increases the vulnerability of women, youth and rural Egyptians, since they are the most likely to be unemployed.

Throughout its fluctuating economic performance, the structure of the Egyptian economy remained broadly the same over the past decade. Formal business entry and growth is muted, and investments have been skewed towards large, capital-intensive firms that do not create jobs. This lack of dynamism, particularly in the manufacturing sector, is reflected in the very low rates of business entry in Egypt, the severely skewed size-distribution of firms, where a small number of large firms coexist with a vast majority of micro firms – with limited development of a small or medium scale business sector. Even periods of GDP growth have not led to growth in formal private sector jobs.

Moreover, energy subsidies coupled with an unfriendly business environment that favors large investors who can influence bureaucratic outcomes and who have privileged access to (often subsidized) inputs like land, capital or energy, have led investments to be skewed towards large, capital-intensive businesses that created few jobs. This project aims specifically at addressing these regulatory, institutional and governance issues that have plagued private sector dynamism in Egypt for years. The current context and the strong will of the government authorities to address these longstanding regulatory reforms offer a unique opportunity for making progress in these areas.

Sectoral and Institutional Context

The business environment in Egypt suffers from multi-layer administrative compliance burdens, which represent a serious obstacle doing businesses in Egypt. This is particularly the case when it comes to small businesses. In Ease of Doing Business 2015, Egypt ranks 112 out of 189 countries (as a comparison, Morocco ranks 71 and Tunisia 60). In the WEF Competitiveness Index 2014 Egypt ranks 118 of 148. Stimulating inclusive growth throughout the economy will require a fundamental change in administrative culture- , establishing a priority focus on achieving public-policy objectives in the least burdensome way for business.

The complexity and uncertainty in acquiring an industrial license exemplifies the problems faced by investors. An assessment of the industrial licensing system in Egypt found that based on evidence from interviews with both business owners and regulators, the procedures for obtaining an operating license and a certificate of industrial registration require a minimum of several months but may take several years. The Industrial Register, initially intended as a means of data collection on industrial activity in Egypt, has morphed into an instrument of control, which involved detailed technical evaluations and inspections of factories by IDA technical staff, and became another administrative barrier to investment and business activity. A strategic assessment of business licensing and other administrative procedures found that as a result, “Egypt has one of the most complex, unwieldy, and time-consuming licensing systems in the world.” Similar levels of complexity, arbitrariness and uncertainty prevail in most areas of government-business interaction: access to land, construction permits, licensing, inspections, customs and tax compliance, and sector-specific regulations. Evidence also suggests that disadvantaged governorates are more vulnerable to administrative challenges. According to the Investment Climate Rapid Survey conducted in 2011, business

licensing and operating permits in Sharkiya, Lower Egypt, were identified as a major constraint for 27 percent of business respondents, compared to only 8 percent in Cairo.

The government is striving to respond. The Ministry of Investment is engaged in a major reform of the Investment Law, possibly to be passed by Presidential decree even within the next few months. The Cabinet has launched a Higher Council for Regulatory Reform which is undertaking to reform a slew of business and investment regulations. Among the many areas that the government is targeting to reform, industrial licensing, access to land and permitting (Construction Permitting) are some of the more immediate constraints to business growth. The current government's agenda aims at sending a strong signal to investors by engaging on an ambitious plan to overhaul the business environment—what will determine the private sector's response to it will largely be driven by how credible, deep and sustained is this new window of reform opportunity. The General Authority for Investment and Free Zones (GAFI) aims to become the national platform for investment entry and business licensing at the sub-national level through its One-Stop-Shops (OSSs) and Information Portal.

The revival of the Egyptian Regulatory Reform and Development Activity (ERRADA) regulatory simplification program is a good sign that a systemic approach to this agenda is envisaged. ERRADA's mandate is to support the Government's efforts in building a regulatory management system, based on a dialogue between public and private institutions, aiming at increasing efficiency, competitiveness and creating more job opportunities. Initiated in 2008 but then suspended in the wake of the 2011 uprisings, the Government authorities revived ERRADA with Prime Ministerial Decree No. 1038 of 2014 and assigned the Minister of Industry, Trade & Small Industries the supervisory role over the program.

The focus on industrial licenses, access to land and construction permits is also a sign that the government aims to address the toughest issues and priority constraints to investment. These topics have little quick fixes to offer. They require a "simplification shock" to send a credible signal to investors, results on the ground and sustained public governance reforms in the relevant agencies and institutions, at the national and local levels, to address the deep-rooted problems of unequal treatment of businesses. The agencies with the mandates for these regulations are all actively engaged on the reform agenda. The Industrial Development Authority (IDA) is the principal authority mandated to regulating the industrial sector and allocates land for industrial projects, while the General Authority for Investment & Free Zones (GAFI) is the principal governmental authority concerned with facilitating investment through its OSSs, which aims at easing and decentralizing business entry, licensing and operations. ERRADA is mandated to catalyze and support reform implementation.

Relationship to CAS

The WBG is preparing a Country Partnership Framework (CPF) jointly with IFC and MIGA, for FY15-19 with Board presentation early next year. The strategy process was launched on March 5, 2014 with the government and, starting on June 15, 2014 consultations were held. The aim of the first phase of the CPF consultations was to listen to the priorities of the Egyptian people and to inform the CPF. In the first round of consultations, Education, Health, Social Safety Nets, and Improvement of the Business Environment, came on top of the priorities. Accordingly, the CPF focuses on key drivers of increasing shared prosperity and reducing extreme poverty; among which are: (i) supporting economic stability and improved governance; (ii) creating opportunities for sustained income generation by promoting private sector policies to level the playing field.

The findings of the current Strategic Country Diagnostic (SCD) for Egypt indicate that reforms such as phasing-out of energy subsidies and large-scale public investments in infrastructure will produce inclusive growth and jobs only if the complexity, discretion, and uncertainty that businesses face in complying with regulations and accessing services and factors of production are significantly reduced. This is consistent with the findings of recent WBG analytical work including “Jobs or Privileges” and “More Jobs, Better Jobs: A Priority for Egypt ”which conclude that the main constraint to private sector growth is a business environment characterized by complexity, uncertainty, and unequal treatment which have led investments to be skewed towards large, capital-intensive businesses that created few jobs. What fundamentally constrains the growth of a smaller-scale business sector is the complexity of the regulatory environment, the unequal access to regulatory services and (subsidized) inputs and factors, and the uncertainty this imposes on businesses. Recent evidence has shown how political connections or connections in the bureaucracy offer a competitive edge for privileged investors. The myriad of regulatory barriers facing businesses provide an advantage to those with unproductive skills or assets like political or bureaucratic connections to get around those barriers. It also offers protection from arbitrary and discretionary enforcement of regulations. This uncertainty and unpredictability in the interaction with government agencies and the unequal and arbitrary treatment to which businesses are subject, extends to areas like access to land, inputs and even credit. These issues trickle down at the local level and in all areas of government-business interaction, and are not limited to favors to connected large investors which enjoy anti-competitive positions. Yet, they are particularly harmful to small businesses that do not have connections and resources to shield them from this uncertainty and help them get around complex regulatory requirements. The disparity also has a spatial component, with access to services and facilitation evident between metropolitan and non-metropolitan areas which persist despite some attempts to decentralize government functions and authority.

This project aims at addressing the issues identified in the SCD and Jobs reports starting with regulatory areas that are most constraining to businesses (land allocation and licensing) by revamping the institutional set-up for the delivery of licensing through GAFI and improving the process of regulatory reform for more inclusivity and consultations via ERRADA. If not addressed, the same issues of uncertainty and discretion in the business environment that have muted or distorted the private sector response to previous waves of reforms may again limit the impact of current reforms and large public investment projects. The 2004-2006 wave of macroeconomic and microeconomic reforms, including in the tariff and tax areas, have been successful at increasing private investment rates, FDI and growth. But these investments mostly happened in large, capital intensive industries and were limited in the small scale manufacturing or services sectors. Few jobs were created and informality grew. For the same reasons, the ongoing reforms and investments may have the same disappointing impact in terms of formal job creation and SME growth if the core issues of uncertainty and arbitrariness in regulatory compliance and state-business interaction continue to prevail and to benefit a few. These same issues will also continue to limit the impact on job creation and business growth of other policies and interventions, including in the infrastructure, skills and financing areas.

To reap the jobs benefits of the ongoing reforms and public investment projects, the priority for the Government of Egypt should be to profoundly and credibly reduce the complexity and uncertainty in business-government interaction, which is the focus of this project.

II. Proposed Development Objective(s)

Proposed Development Objective(s) (From PCN)

To improve the efficiency, accessibility, and transparency of key investment services by reforming industrial licensing and land allocation processes, and enhancing the capabilities of one-stop shops through which investor services are provided while supporting the Government's efforts in building a regulatory management system.

The higher level objective to which this project contributes is to increase private investment rates and job creation, particularly among SMEs, and improve productivity growth through increased competition and a leveled playing field.

Key Results (From PCN)

Progress towards achieving the project's development objectives will be measured by a series of quantitative and qualitative indicators at the component level. The key results of the project would be the enactment of the transformational reforms for private sector licensing and land allocation framework.

This will be measured by:

- Industrial Sector gains:
 - o Compliance Cost Savings for the industrial sector
 - o Reduction of licensing requirements and duration

- Industrial Sector Growth / Development:
 - o Increased land area allocated for industrial investments:
 - # of land plots/area allocated for MSMEs and % to total
 - # of land plots/area allocated through Zone Development Agreements and % to total
 - # of land plots/area allocated for expansion (existing investors) and % to total
 - # of land plots/area allocated for new/expansion FDI investment and % to total
 - o Increased Industrial Sector market entry:
 - # of projects receiving project approval
 - # of projects receiving Operating License
 - # of projects receiving Industrial Register

- Transparency and Accessibility to service and information:
 - o Published regulatory requirements and clarity of process
 - o Facilitated on-line application, requirements and instructions
 - o Developed on-line industrial land cataloguing
 - o Activated Appealing system
 - o Activated Public Private Dialogue and QA function

III. Preliminary Description

Concept Description

The project seeks to transform industrial licensing and land allocation processes from two of the greatest impediments to investment in Egypt into streamlined and transparent processes. The project aims to provide technical assistance and systems to transform IDA licensing and land allocation processes and support the deployment of those reforms in GAFI OSSs by providing technical assistance, systems and capacity building. The project will also provide technical assistance and

capacity building to the ERRADA program to reinforce ERRADA as the mechanism for catalyzing these and future reforms.

Component 1: Capacity building for managing regulatory reform (ERRADA)

The Project aims for building the capacity of the GoE regulatory reform program (ERRADA) by providing the necessary support to enable the performance of its mandate to manage business environment regulatory reform. The project will focus on supporting ERRADA around a set of horizontal (cross-cutting) reforms in the sense that they target constraints affecting firms in all sectors of the economy such as the transparency and predictability of the regulatory environment as well as vertical targeted priority areas of reform of industrial licensing and land allocation.

Within the horizontal reforms, the project will support ERRADA in:

- completing a comprehensive inventory of business related formalities/administrative procedures;
- process mapping and re-engineering of the most relevant/frequent formalities/administrative procedures with the objective of streamlining and simplifying them;
- establishing an informational portal of business related administrative procedures rendering all information related to the requirements of these procedures accessible to the general public in a simple and comprehensive manner;
- putting in place a public consultation and review mechanism to secure that all business related legislative proposals are properly reviewed and consulted with the stakeholders, including the private sector.

Component 2: Supporting Industrial Sector transformational reforms (IDA)

The Project aims to support IDA focus on its strategic roles of regulation and development and transform its approach to implement risk based regulation principles. The project seeks to implement the recommendations of IDA's Strategic Assessment Paper of 2008 , specifically:

1. Eliminate technical evaluations and inspections as a precondition for industrial registration and perform inspections/evaluations on risk-assessment basis utilizing professional, accredited private practitioners,
2. Return the policy objective of industrial registration from a licensing function to its original purpose as a data collection function, and hence delink import/export and other permits from the industrial register,
3. Adopt primarily a wholesale industrial land allocation rather than the focus on the "retail" land allocation by setting and administering policies and procedures for industrial land allocation and introducing best practice contracting instruments with private developers,
4. Support IDA's technical capacity building at the governorates' level to enable decentralization of regulatory decision making to be deployed through existing OSSs

Component 3: Facilitating accessible and transparent regulatory services (GAFI)

The Project aims to support GAFI become the national platform for business entry, licensing, and access to investor information at the sub-national level through its One Stop Shops and GAFI

Information Portal. This will be done by:

1. To streamline the business entry and licensing process for investors:
 - a. Developing systems to enable hosting of licensing services both at the central agency and in the One-Stop-Shops.
 - b. Decentralizing IDA licensing services through GAFI OSSs. This would entail addressing GAFI's processes and interfaces with all the involved regulators including primarily IDA, but also other line ministries and local authorities involved in licensing.
 - c. Capacity building and technical assistance to enable and support GAFI in this enhanced client-facing role.
2. To enhance access to quality information, transparency and connectivity:
 - a. Consolidating information on access to land through showcasing all land available for investment under the jurisdiction of the Industrial Development Authority (IDA), on GAFI's website. Information would include areas available, terms and location.
 - b. Further e-integration of the OSS network, including e-archiving and electronic connectivity between OSS branches and agencies such as IDA to enhance quality of service provided by OSS.
 - c. Developing GAFI's capabilities for the tracking, collection, analysis, and publication of quality private sector data and information to better inform policy makers, the private sector, and potential investors (both foreign and domestic).

IV. Safeguard Policies that might apply

| Safeguard Policies Triggered by the Project | Yes | No | TBD |
|--|-----|----|-----|
| Environmental Assessment OP/BP 4.01 | | x | |
| Natural Habitats OP/BP 4.04 | | x | |
| Forests OP/BP 4.36 | | x | |
| Pest Management OP 4.09 | | x | |
| Physical Cultural Resources OP/BP 4.11 | | x | |
| Indigenous Peoples OP/BP 4.10 | | x | |
| Involuntary Resettlement OP/BP 4.12 | | x | |
| Safety of Dams OP/BP 4.37 | | x | |
| Projects on International Waterways OP/BP 7.50 | | x | |
| Projects in Disputed Areas OP/BP 7.60 | | x | |

V. Financing (in USD Million)

| | | | |
|--|------|-----------------------|---------------|
| Total Project Cost: | 6.00 | Total Bank Financing: | 0.00 |
| Financing Gap: | 0.00 | | |
| Financing Source | | | Amount |
| Borrower | | | 0.00 |
| MENA Transition Fund - IBRD as Implementing Agency | | | 6.00 |
| Total | | | 6.00 |

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