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The Role of Postal Networks in Expanding Access to Financial Services

Country Case: Egypt's Postal Finance Services

The World Bank Group
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Author's Note

This paper discusses the role of the postal network in expanding access to financial services in Egypt. It reviews the public postal operator within the postal sector and within the broader context of the communications sector. The roles of the postal network and state and privately-owned banks are also reviewed from the perspective of the financial sector development, with particular focus on payments systems development and microfinance.

This paper was prepared with desk research in 2004. Field visits were not scheduled.

While this country case on Egypt can stand alone, it is an integral part of this large study of the potential of postal networks to coordinate with financial service providers in 7 countries (*Egypt, Kazahkstan, Namibia, Romania, Sri Lanka, Uganda, and Vietnam*) and 5 regions (*Africa, Asia, Eastern Europe and Central Asia, Latin America and the Caribbean, and the Middle East and Northern Africa*).

Glossary of Abbreviations and Acronyms

ATM	automated teller machine
BdC	Banque du Caire
CIDA	Canadian International Development Agency
EFT POS	electronic fund transfer at point of sale
EGP	Egyptian pound
ENPO	Egypt national post office
FFI	formal financial institution
GDP	gross domestic product
HR	human resources
ICT	information and communications technology
IMF	International Monetary Fund
KfW	Kreditanstalt für Wiederaufbau
LAN	local area network
MCIT	Ministry of Communications and Information Technology
NBD	National Bank for Development
NGOs	non-governmental organizations
NPL	non-performing loan
PBDAC	Principal Bank for Development and Agricultural Credit
piaster	EGP 0.01
POS	point of sale
ROSCAs	rotating savings and credit associations
SME	small and medium enterprise
SWOT	strengths-weaknesses-opportunities-threats matrix
UNDP	United Nations Development Programme
UNICEF	United Nations International Children's E Fund
UPU	Universal Postal Union
USAID	United States Agency for International Development
USD	United States dollar

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Summary

SWOT Analysis of Egypt Postal Financial Services

Strengths	Opportunities
• Has historical operator of postal savings and payment services. • Provides broad-based, low-threshold access through more than 9,000 post offices compared to approximately 2,000 bank branches; particularly well-represented in rural and poor sub urban areas; about 60 percent of the post offices run as agencies by private or public sector entities. • Mobilizes small deposits with low minimum deposit requirements and has more than 12 million savers (30 percent of adult population)—more than the number of individuals served by the entire banking sector. • Processes considerable volume of payment transfers per year (money orders, pensions, and electricity bills)—40 million semi-cashless transactions as compared to 12 million check payments transactions by the banks. Operates an efficient nation-wide postal giro circuit for some 10,000 public entities. • Is piloting new services (debit cards, pensions, and payroll accounts) with new technologies (ATM and EFT POS) in Greater Cairo. • Initiates co-operation with the banking sector to develop cost-efficient, sector-wide, small-value payment instruments and services. • Is perceived as a non-bank by the population, which also has a high level of personal trust in postmasters/post offices in rural areas. • Is showing record profits; has no NPL portfolio and has never defaulted in payments to depositors. • Recently has invited involvement of private sector management and taken first steps towards private sector partnerships.	• Postal banking offers potential to broaden and deepen access to financial services by increasing propensity to save, increasing savings, improving payments efficiency, and offering small credit, pension, and life insurance products. • The postal network's existing infrastructure and customer streams can be the nation's channel for small-value, standardized financial services. • In the short term, the postal network could capture much more of the international remittances market if modern marketing, ICT, and alliances are applied; this could also be the basis for new savings and payments products. • Synergies are possible when the postal network modernizes with implementation of ICT, Internet access, and a platform for e-government and e-commerce (fulfillment). • The post office could become Egypt's first chain of convenience stores, providing basic financial services, communications, and retail trade. • Egypt has several modern private sector banks that might be poised to expand their position in the growing retail market, through an alliance with Egypt National Post Office (ENPO).
Weaknesses	**Threats**
• Non-transparent performance measurement; management information system measuring postal financial services and mail revenues non existent • Non-transparent regulatory and managerial structure • No qualified banking management, basic marketing skills only • No role in international remittances, leaving informal channels a significant role to play • Incomplete product package; demand for small credit, life insurance, pensions and other payments and savings products not met; cannot expand due to legal framework • Not connected to any clearing house • Slow progress toward modern ICT in post offices due to investment in information technology and human	• Postal reform strategy has not been determined and role of the government in day-to-day management of ENPO is significant. • In financial sector development, broad-based access to financial sector does not feature as a priority; state banks continue to dominate the sector. • Postal mail service in a further liberalized sector may limit pace of development in postal financial services.

resource training; limited access to funding • Limited by legal framework for commercial flexibility and asset management • Problems with overstaffing and low productivity	

1--Postal Sector Development

The history of state postal services in Egypt can be traced back to Pharaonic times, more than 2,500 years ago. In 1866, when part of the Ottoman Empire, the foundations were laid for the current national postal system, when the Egyptian Viceroy acquired the private postal administration "Posta Europea" and renamed it "Postes Egyptiennes," which the public used with confidence. French experts helped set up postal service standards as practiced by the French postal state service at that time. The network of services expanded and a few years later included postal money orders.

The postal law underwent major revision and modernization (in some respects) in 1980, and postal services were entrusted to the Egyptian National Postal Organization (ENPO). To date, there are no annual reports published by the ENPO. Most of the data here relies on what ENPO reported to the Universal Postal Union (UPU), plus privileged access to internal annual accounts and budgets of two different years, 1996–97 and 2000–01.[1]

Performance Indicators of the Egyptian National Postal Organization

Egypt's postal services comprise the same traditional core services provided by postal systems in most countries: delivery services (addressed letters and parcels), a number of financial services (such as postal service and current accounts, issuance and delivery of money orders), and agency services where the postal system performs some activities on behalf of the government (for instance, selling duty stamps, disbursing pension payments, and issuing vehicle licenses).

Egypt's combined per capita flow of domestic and outgoing international letters is low (3.3 pieces per capita in 1997, 2.87 in 2002), even when compared to other African (7 pieces per capita) and Arab countries (7.6 pieces per capita). Per capita flow of parcels in Egypt is also low compared to other regions.[2] For both parcel and letter traffic, domestic post is quite limited. The number of packages internationally mailed in Egypt, however, is closer to the amount posted in other regions. Egypt's postal system issues fewer money orders per capita per year than most countries, but has an impressive number of postal savings accounts. Each post office serves an average of 8,948 individuals, compared to the larger numbers served by a single post office in Qatar (23,600), Saudi Arabia (13,400), and Syria (22,000).

In terms of operational efficiency, the Egyptian National Postal Organization employs close to 41,000 workers, with an average number of 5.25 workers per permanent postal establishment. This is not significantly different for postal establishments in other parts of the world.

Output per worker, however, is much lower, in Egypt. The average number of domestic letters delivered in Egypt in 1997 was 3,385 per letter carrier, and 3,002 per worker in 2002, compared to around 40,000 pieces per worker in Africa and Latin America. Mail productivity has declined 3–5 percent per year since 1997, but this indicator may be misleading because a large part of the postal workers are engaged in postal savings and payments services.

[1] The fiscal year in Egypt runs 1 July–30 June.
[2] Per capital flow of parcels in Egypt is 0.03 and 0.003 per every 1000 inhabitants, compared to flows close to 150 pieces per 1000 inhabitants in Latin America and Eastern Europe and the Commonwealth of Independent States (CIS).

Despite low demand and poor operational performance indicators, ENPO incurred a small deficit of around 1 percent in 1997, which turned into a slight surplus in 1999 when current expenditures accounted for 98 percent of total revenues. This “break-even” situation is not atypical of postal systems in different parts of the world. Went from slight deficit to profitable Since 2000, the net results of ENPO have moved upward considerably from USD 2.5 million in 2000 to approximately USD 5 million in 2002, representing 2.1 percent of total revenues. About two-thirds of revenues stem from postal financial services and less than 30 percent from postal (mail) services.

As a result of demand, productivity, financial results, and investment patterns, ENPO appears to exhibit patterns of the vicious cycle faced by many developing countries’ postal authorities: low demand volumes result in poor financial performance, which translates into low investment levels causing reductions in quality of service that leads to further cycles of depressed demand. In addition, competition from other sectors and services exert more pressure on postal services. ENPO is trying to improve itself to generate funding for the modernization needed to improve services and attract more customers and business.

Competition from Telecommunications and Information Technology

Egypt has witnessed significant developments in both basic telecommunication services and access to the Internet (or e-mail service) in the past decade. These trends are expected to reduce demand for traditional postal services, especially with limited developments in e-commerce in the country. Therefore, it appears that the ‘substitution impact’ of developments in IT and telecommunications outweigh the ‘complementary impact’ that requires expansion in e-commerce activities. The latter is delayed because of the need to establish the right financial instruments not yet adopted by Egyptian consumers and businesses.

Examining Egypt’s indicators for telecommunications and IT, current indicators still show limited service in Egypt compared to other regions. For example, there were only 8.64 fixed lines per 100 inhabitants in 2000, a figure that is only higher than Africa and is just over half the world average of 16.17 lines per 100 inhabitants. Similarly, cellular phone subscriptions per 100 individuals are still low compared to other regions in the world: Egypt has 2.14 subscribers per 100 inhabitants, compared to a world average of 12 subscribers per 100 inhabitants. In these areas, developments take place rapidly, and Egypt’s ratios are expected to improve substantially before 2010.

As indicators of competition replacing traditional mail services, IT and Internet use exhibit a similar picture, as rates in 1998 compare poorly to other regions of the world. Internet users in Egypt numbered 16.3 per 100,000 inhabitants in 1999, which was lower than the average for African countries (22.0), while the world average was 270 per 100,000 inhabitants. Estimated use of personal computers and Internet hosts per 10,000 inhabitants gives more or less the same position for Egypt.

Telecommunications and IT development in Egypt in the past 3–4 years, however, has accelerated rapidly. For instance, between October 1999 and February 2002, fixed-line subscribers increased by some 40 percent and the Ministry of Communications and Information Technology (MCIT) projected it to reach 50 percent 2004. The number of mobile phone subscribers in February 2002 was 5.4 times the subscriptions in October 1999. The Internet user population has also multiplied and in December 2003 was 2.7 million, nearly 3 times the rate in October 1999.

The growth of mobile phone subscriptions by 183 percent annually over the period 1995–2000 (being the highest in the world) has added to the growth momentum in these markets, either in terms of substituting phone calls or freeing up fixed phone lines for Internet access.

Estimates for Egypt do not exist on how actual or projected developments in IT and telecommunication services will impact demand for traditional postal services. Electronic services, such as e-mail, teleconferencing, and faxing are already cutting into first-class mail business, which generates a relatively large part of the mail volume and mail revenues in Egypt. It is also somewhat unlikely that banks, utilities, credit card companies, and other businesses will develop bulk mail services, since they have not already and since alternative electronic communications are increasingly available.

On the other hand, Egypt's e-commerce lags and there are still barriers to any short-term potential for its growth. This also applies to direct mail (e.g., catalogue shopping), which is not popular in Egypt. The combination of high urban concentrations with access to nearby bazaars and shops, and rural communities with poor and often illiterate inhabitants, limits short-term market opportunities for direct mail and marketing. Egypt may not ever develop a direct mail industry but move directly into e-commerce, if and when the legal and technical infrastructure sufficiently matures, the logistic providers can handle physical fulfillment, and banks manage the payment fulfillment.

While Egypt's current IT and telecommunication conditions are not as threatening to postal services as they are in more developed countries, progress in these areas is sufficient to increase competitive pressures on postal services and to limit development of the postal business. At the same time, slow development of e-commerce and mail-order delivery imparts a net negative impact on telecommunications development in Egypt, which is basically the substitution of letter and document traffic from regular mail to telecommunications and electronic means.

Other countries' experiences suggest that this environment, where the threat of competition is perceived as severing important value-added postal markets, triggers postal sector reform. In addition, postal reform in many countries has been part of a comprehensive strategy for improving government services. These two conditions exist in Egypt, for example, in the Ministry of Finance's program to link expenditures in various government bodies to performance indicators and tangible outcomes. Thus, with the environment indicating that postal reform is needed and feasible, the need to analyze postal reform options becomes urgent.

Postal Sector Reform

The two main areas covered in this section are the degree of corporation and commercialization of ENPO and how that guarantees the autonomy and accountability necessary for independent management, and the market framework in which ENPO operates and how that enhances competition from private operators in areas that are not reserved for the public operator.

Corporation: Laws and Decrees

Two laws govern the operation of ENPO: Law 16/1970, the Postal Services Law; and Law 19/1982, giving ENPO economic authority. These two laws grant ENPO many features given to postal authorities under the corporate model. ENPO also has independence, which is not granted to many public entities in Egypt or even to postal authorities in other countries. For example, the Postal Services Law (16/1970) grants ENPO an exclusive area for delivery and mailing of all postal materials, including parcels. Law 19/1982 gives ENPO the exclusive right to provide postal financial services, such as money orders, postal savings, and checking accounts. ENPO is free to "enter into agreements with other ministries or public agencies, subject only to approval by ENPO's Board of Directors."

Furthermore, Law 19/1982 allows ENPO to subcontract the provision of such services as the sale of post stamps and the delivery of mail items to private entities (i.e., postal agents). Ministerial Decree 31/1985 added international and domestic express mail to the list of services that ENPO provides. Additionally, the regulations allow the Board of the Authority to delegate any other services that it deems feasible to the private sector. The Board of Authority, in this respect, relies on a standard contract with either the urban or rural "postal agency" that stipulates standard physical requirements for private providers of these services. Law 16/1970 states that the postal authority is the sole entity entitled to transport and deliver letters and parcels, as well as provide postal financial services and management of postal savings accounts. The Executive Regulations, issued in 1972 to expand and clarify Law 16/1970, define these services plus weight and dimension limits for packages and materials being posted through ENPO.

In 1985, the Postal Law was amended to allow private courier services to offer express mail services. The only condition the Law mandated is that the private courier services acquire a license to practice for an annual fee payable to ENPO. The amendment opens the exclusive area granted to ENPO for express mail service, making this the only service where ENPO faces competition.

Two weaknesses in Egypt's Postal Law are handicaps for ENPO. The first is the law itself, which defines no clear pricing formula, and neither the law nor its executive regulations links prices in any way to inflation indicators, competition, or market development. Instead, the executive regulations accompanying Law 16/1970 stipulate that a committee periodically determine the prices (which are changed by ministerial decrees). If the prices do not cover the cost of providing the services, the government reimburses ENPO for the difference. The last update occurred in 1998. The law and its amendment do not address the pricing of private sector services contracted by ENPO.

Similarly, prices that ENPO charges for agency services, such as payment of pensions and salaries, are negotiated between ENPO and the corresponding government agency. Requirements include features of the space to be utilized as well as "integrity" requirements for the person operating the postal agency (e.g., a minimum education level and a clean criminal record among other preconditions). The unrealistic pricing is underpinned by the fact that ENPO has very weak management information systems and is unable to determine actual cost per item or product profitability. (ENPO is further handicapped in these interagency negotiations. For example, regarding pension payments, ENPO is actually required to provide these payments without charges to the corresponding pension agency.)

The second weakness concerns public utilities, which in other countries rely on the postal system for distribution and collection of bills. Similarly, other large entities in Egypt are not (and have not been) obliged to use the postal system, depriving ENPO of "captive" major clients. While it is not suggested that regulations impose constraints on how utilities and banks conduct their businesses, this requirement underlies the economies of scale in standard letter delivery. As a result, one should not anticipate that postal reform will lead to strong growth in mail volume.

Commercialization and Pricing

According to the institutional environment set by the Postal Law and its amendments, ENPO commercialization is not constrained by any legal or institutional barriers. In practice, however, many of the conditions necessary for successful commercialization are not present.

An essential pre-condition for commercialization is **commercial management and availability of management information systems (MIS)** to help determine the priorities and course of commercialization. For a long time, ENPO's management was selected through internal promotion only. This produced technically very skilled and experienced postal management with relatively limited experience with competition and commercialization. Efforts to introduce MIS have been limited, and commercial MIS analysis (for product profitability, client profitability, post office or regional profitability, for example) remains underdeveloped.

Since 2002, ENPO has been lead by a Director General who has more than 15 years of private sector management experience and who has the ability to introduce private sector practices within ENPO. The Director General is supported by several private sector representatives appointed to ENPO's Board. Commercialization efforts have gained some momentum since these changes.

The absence of a pricing formula means that postal service pricing lags considerably behind inflation and market developments in general. The main beneficiary of this policy is domestic mail/parcel traffic. For example, while domestic prices increased 25-fold from 1970 to 1998, the price of sending a standard domestic letter in 1998 was only 10 times the price in 1970. Other domestic postal services exhibit more or less the same pattern, even for services that typically serve the business community, such as the delivery of parcels and periodicals. Because this policy serves an agreed-upon social goal, ENPO must be reimbursed for the difference if these prices are lower than the actual cost of providing the service. Based on conversations with officials at ENPO and public discussions, it appears that ENPO does not get reimbursed regularly for the difference between prices and actual cost of providing the service.

International services have outpaced domestic inflation, in some cases with prices that are 400 times those charged in 1970 for the same service. It is not clear—due to weak MIS—whether the universal service obligation is partially financed by increases in international service charges (while domestic prices continue to be subsidized) or whether these increased rates for international services result from the need to cover part of the cost of international service with foreign currencies that have significantly appreciated against the Egyptian pound.

Two issues have to be considered regarding commercialization. First, the bulk of the mail service, particularly parcel delivery, in developed and developing countries is generated by the business sector. Second, given that Egypt's postal service indicators are lowest in the domestic service segment, commercialization policies must focus on improving the quality of domestic services provided. These policies can help to break the vicious cycle in the postal mail sector. Therefore, price liberalization of services not representing core universal service obligations (as defined by the majority of countries) could serve two objectives: to improve the price/quality combination of value-added services, such as express mail and parcel delivery (which could be of more value to businesses than the subsidized-price/lower quality combination), and to make a positive impact on ENPO's revenue flows.

In addition, not requiring large utilities to use ENPO for their bill delivery and payment collection seriously reduces domestic demand for standard postal services in Egypt. This is a critical drawback given the fact that even in developed economies the largest 10 percent of all mail customers typically produce well over 80 percent of all the mail. These large mail users include banks, insurance companies, utilities, publishers, mail-order companies, and direct-mail houses, among others. As it would be difficult to justify regulatory intervention to force these potential bulk mailers to use the postal system, ENPO should consider developing a marketing approach to attract these large clients through account managers that can offer tailor-made services, including special rates. Within the current structure of ENPO, there is no identifiable marketing and sales function.

Even if major clients voluntarily switched to ENPO, there are limits to potential gains in delivery services from economies of scale, especially with the expected expansion of e-commerce and other IT-telecommunication means of payment. This same development, however, presents postal services with a **valuable opportunity in terms of economies of scope in financial postal services**.

ENPO Outlet Network: Strength in Rural and Low-Income Areas

	Post offices	Banks	Insurers	Stockbrokers
Greater Cairo	393	525	< 50	< 150
Alexandria	117	138	< 30	< 50
Port Said	29	31	< 20	< 10
Sinai	37	38	< 20	< 10
Rural and remote areas	2,440	541	< 20	< 20
TOTAL	**3,016**	**1,273**	**< 140**	**< 240**

Source: Egyptian Banking Company for Technological Development (2000).

This potential is pursued in many countries, but different sizes of the postal and the bank branch networks in Egypt suggest that ENPO has a golden opportunity to use its existing network to more advantage. Its extensive postal network had postal establishments in 5,152 public offices, in addition to 4,015[3] private offices in 1999–2000 (according to the Central Agency for Public Mobilization and Statistics, 1999–2000), a total of 9,167 post offices. Over 40 percent of the post offices are in rural areas—far more extensive coverage than the number of bank branches in rural and lower-income urban districts. While banks outnumber post offices in Greater Cairo, the number of banks in rural and remote areas is only slightly over 20 percent of the number of postal offices. Postal savings accounts represent only 3 percent of total national savings. Therefore, while it may not be economically rewarding for banks and other financial institutions to set up branches and networks for financial services outside the main cities, ENPO's commercialization efforts could focus on becoming a

[3] Data on the size of the postal network widely differ. In particular, the number of postal agents varies between approximately 2,000 and 6,000.

strong financial network backbone with or without collaborating with the banking system. These developments can balance competition facing postal services in business delivery.

ENPO has begun to explore this potential by proposing to electronically connect all postal offices supplying financial services. It is not clear, however, if ENPO is considering major increases of this electronic financial network in its short-term development plan. Additionally, ENPO has plans to use other sources to create a network of postal business centers that would supply such commercially-oriented services as photocopying, faxing, and Internet access. Again, the idea is to better utilize ENPO's presence in rural and low-income areas while keeping additional operating costs low.

ICT-Based Modernization

With more than 9,000 outlets throughout Egypt, a labor force of 41,000 individuals, 12 million Egyptians holding EGP 22.5 billion in postal savings accounts, and multiple delivery services for the Egyptian public, the postal sector holds special importance and enormous potential in the nascent information society. The owner of the ENPO, the Ministry of Communications and Information Technology (MCIT) has identified the postal system as a key component of the government's information infrastructure and a major tool in fostering e-business and propagating its benefits at the grassroots level.

MCIT is exploring ways by which ICT can be used to improve quality of services, efficiency, capabilities, and the organizational structure of Egypt's postal sector. Reforms propose to use modern technologies to improve the quality of services provided to customers, while creating a new stream of revenues for Egypt. To date, MCIT supported an ambitious sectoral modernization program under which more than 400 major post offices around the country have been equipped with computers, local area networks (LANs), and local servers, with more to follow in the coming years. MCIT is also setting up a postal information network, which will improve communication within the postal system by connecting individual post offices and improving the exchange of financial information and operational data. The network will connect computerized local post offices with the regional postal centers and the four main postal hubs in order to computerize all existing financial applications. This will allow easy access to all the necessary operational information and will ensure that postal customers will receive efficient service.

Extending e-business and e-commerce activities to the grass roots level, MCIT launched a major pilot project in 2002 to establish an electronic fund transfer (EFT) network using automatic teller machines (ATMs) and points of sale (POS) in 56 post offices in Greater Cairo. Using smart card technology, this project will help establish the necessary infrastructure for electronic payments for government services at postal outlets. It will also facilitate access to postal savings accounts as well as pensions and salaries for more than 10 million individuals, in addition to Internet banking capabilities.

Another key element of the postal reform process is the development of new services to increase postal revenues. Additional modernization efforts include the development of a hybrid mail project, a service aimed at corporate customers looking to implement an e-delivery system for business documents. Plans are also in place to introduce e-billing for postal customers, allowing individuals and companies to pay their bills over the Internet.

The Egyptian National Post Organization, responsible for distributing pensions in Egypt, has also launched a new system in co-operation with the Ministry of Social Affairs to end the long waiting times and huge crowds at the monthly distribution times. Features of the new system include increasing the number of days and hours it offers the services as well as introducing new means of distribution, such as transferring the pensions to clients' savings accounts and offering the use of ATMs.

In addition, in 2003, MCIT and ENPO agreed to the establishment of a joint venture company named Giro-Nil with two banks, Banque Misr (state-owned) and CIB Bank (privately-owned), to develop advanced cashless payment services. The joint venture is currently designing its strategy and business model.

The ultimate goal of postal reform is to create a system where modern technology and a free flow of information benefit the customer. A modern, efficient postal service that utilizes the latest information technology will not only increase Egypt's social and economic development, but will also contribute significantly to the creation of an Egyptian information society.

The initiatives taken by the MCIT and ENPO appear to be promising steps toward providing public access to modern information and communication technology. These projects could reposition the postal network as the vanguard of financial and information services by installing ATMs, EFT, POS, and Internet banking terminals in post offices. An encouraging sign is the growing co-operation between banks and the private sector to develop these services. While these steps are promising, they are small-scale in relation to the scale of needs in the country. Evaluation of the pilot projects and a subsequent cohesive planning and implementation of the nationwide rollout will determine the eventual success of these initiatives.

Regulatory and Market-Based Reforms

At the current stage of development of postal services in Egypt, most of the reform efforts have been directed at the corporation and commercialization of ENPO, not at reforming postal services as a comprehensive market. This section discusses the main principles that must underlie the next phase of postal service reform in Egypt, taking into account the whole postal services market, not just the incumbent national provider.

Separation of Sector Policymaker, Regulator, Owner, and ENPO Operator Roles

As the incumbent public operator responsible for meeting the country's universal obligation, ENPO should transfer its regulatory role to an independent agency. This regulator should take over the role of granting licenses to private courier operators. It must establish a fair pricing mechanism, particularly if services develop economies of scale. The regulator should delineate and enforce the exclusive (and diminishing) area for ENPO where private companies are not allowed to compete, while ensuring that private operators face a transparent and predictable environment governing their operations in the postal market. The regulator can also determine the performance goals of ENPO, specifying the financial and quality targets to be achieved. In addition, the role of the regulator may be expanded to introduce financial and performance targets that govern the relationship between ENPO and its network of private offices, again with the objective of enhancing service quality and competition for services in public (not ENPO exclusive) areas. In addition, as reform of the postal sector progresses, the roles of MCIT as policy maker, and ENPO as owner and operator of the sector must become transparent.

Enhancing Competition in Services Not Bound by a Universal Service Obligation

Private courier services were introduced in Egypt in a 1985 amendment to Law 16/1970 which had stipulated that postal services (vaguely defined) be supplied only by the public operator. Beginning in 1987, private courier companies were allowed to compete in express mail services, subject to an annual license fee of 10 percent of profits, with a minimum of EGP 250,000. Because no additional requirements were agreed upon, courier companies are free to determine all other aspects of their operation, including setting their prices, as long as they meet the license fee imposed by ENPO. They can also deliver (or ship) parcels heavier or larger than allowed in the state postal system because neither parcel size or much else is restricted or regulated by the license from the Egyptian postal authority.

Currently, seven private companies are licensed to operate in the courier market: six are branches of foreign companies and the one Egyptian company is Middle East Courier. In addition, an estimated 40–50 companies operate without a license. Their market share is officially estimated at not more than 10 percent of the courier services market. Unlicensed private couriers risk having their operations shut down, deliverables confiscated, and fines levied on them. It is not clear, however, whether the rules and the discretionary power of ENPO are part of a comprehensive market-reform strategy to enhance competition and efficiency in the postal services market.

To regulate postal services, the strategy must focus only on areas where there is reason to believe a market failure exists (increasing returns to scale in delivery) and where a non-commercial obligation needs to be met (universal service). Other competitive services, such as parcel delivery, should be clearly liberalized both for the incumbent operator and its competitors.

Steps to Clarify and Reduce Reserved Area Services

ENPO's reserved areas are compensation for its non-commercial service obligation. This means that the size of the reserved area has to be based on the actual or expected cost of the universal service obligation. In the case of Egypt's regulated domestic pricing, the standard reserved area is not attractive to private companies because of its below-cost prices. The government's universal service commitment for non-standard services discriminates against ENPO by maintaining a uniform price that does not account for the actual cost of providing the service to different geographical areas. By contrast, private courier prices—determined by the market—vary drastically, with prices lower than ENPO's in the Greater Cairo area, and prices exponentially higher for delivery to remote areas.

ENPO's constraint on domestic express mail service and other non-standard letter and parcel delivery must be reconsidered. Either ENPO's prices should be free to compete with private providers or a price floor no lower than ENPO's service within cities must be imposed on private couriers. The first option is superior because it would enhance competition. But, if the government's intention is to subsidize express mail delivery to remote areas, then ENPO will have to be compensated for the cost differential.

Conclusions and Policy Recommendations

Egypt's postal service indicators suggest that a vicious cycle of low demand, low investment, and low quality of service characterize the performance of the industry. Furthermore, competition from expanding IT and telecommunication services will impose more pressure on the industry's performance. Recent steps by new management at ENPO, with private sector orientations, show some improvement, such as better and more (financial) services, increased profitability, and potential to self-finance further modernization of Egypt's postal system.

Further reform of the institutional and regulatory environment governing the Egyptian postal services market needs to be addressed. One might conclude that the corporation of ENPO meets (in theory) most of the independence requirements necessary for its solid financial robustness. In practice, however, many social and public finance constraints limit this independence, the most important of which are heavily controlled domestic prices.

These constraints have seriously handicapped ENPO's commercialization efforts. Yet, there are potential gains from addressing economies of scope in the operator's expansion of its financial and IT services, which can benefit from the existing extensive network of offices, especially in remote and rural areas. Comprehensive postal market reform in Egypt has not yet been truly initiated. From this perspective, a government-sector strategy that targets enhanced competition, separation of regulatory and management roles, and the need to reduce the burden of universal service obligation is crucial in the industry's next phase of reforms.

Given the limited economic importance of the mail, it will be equally relevant to assess the postal financial service and the potential of new ICT services and applications, and to use the assessment in determining the eventual course of reform.

2—Postal Financial Services in a Market Perspective

Postal Savings

ENPO provides a range of postal financial services, and both money orders and postal savings have presumably been offered in Egypt for more than a century. The Postal Savings Fund is not a separate legal entity, but is held by the government and operated like a division of ENPO. It does not have an authorized share capital and it is not supervised by the Central Bank of Egypt.

Postal savings accounts are available to any individual who can provide identification or, in the case of minors, has the explicit permission of their parents. The initial deposit requirement is as low as EGP 1 (USD 0.25), and postal savings passbooks are maintained in the administration as long as a deposit of 1 piaster (EGP 0.01) is kept. By contrast, banks require a minimum of EGP 1,000; and several banks require EGP 10,000 or more and proof of regular income. On the other hand, the Postal Savings Fund limits balances to EGP 300,000 in order to assure the tax exemption and government guarantee privileges for well-to-do individuals.

To the eyes of policymakers, bankers, and Western-trained Egyptians, the services of the Postal Savings Fund look old-fashioned. Nevertheless, demand for postal saving accounts continues to grow. Between 1997 and 2004, the number of passbooks doubled from 6 million to 12 million, representing 20 percent of the total population, or 30–35 percent of the adult population.

	1997	1998	1999	2000	2001	2002	2004
Postal savings accounts (in millions)	6.1	6.7	7.5	8.4	9.0	9.9	12
Average balance per account (in EGP)	705	835	1066	1154	1315	1787	1833
End-of-year postal savings (in EGP billions)	4.3	5.6	8.0	9.7	12.5	17.7	22

Transaction volumes have remained low, in the range of 1.5 to 2 transactions per account per year. This is common in many postal savings banks around the world: it induces one to believe that only 20–25 percent of the savers are actually regular, active savers, while most of the other accounts are dormant. Dormant does not necessarily mean that savers cease to use the account. They may have inherited money and deposited it as an emergency reserve or provision for old age. An analysis of the Postal Savings Fund’s clients and depositors, their motives, and behavior has never been done, although it is perceived as an institution for lower-income groups.

The postal savings product has some good features. Accounts can be opened on the spot at all government post offices and have unique numbers. Deposits and withdrawals can be made at any post office into any savings account, although disbursement of withdrawals can take some time while the post office clerk obtains required approval. The postal savings passbook is a very basic product, useful to people who are not familiar with more sophisticated products. The book gives the client the feeling of "proof" and security, elements, which are quite essential in Egypt.

The Fund does accumulate reserves, and the reserve funds are reported as 1.3 percent of total assets. As the equity of the Postal Savings Fund, this might be considered adequate given the nature of the operation—collection of deposits only and investment of the funds with the government-owned National Investment Bank—but the Postal Savings Fund would need a substantial capital injection if it were to develop and operate as a bank.

Key Features of the Postal Savings Fund

- It serves 12 million savings account clients (up from 6 million in 1997), about 30% of the adult population.
- It is the only formal institution in Egypt offering a savings product to small savers, with a low minimum deposit.
- It provides its service through a 6,000-branch network widely present in rural and poor urban areas.
- It shows continued, stable growth despite being regarded as an antiquated service.
- It has no product differentiation; it does not reward active savers over dormant savers.
- It is also in charge of the Postal Giro Service which has less than 10,000 accounts, all held by public agencies for payment services.
- It reports profitability, generating 70% of the revenues of the Egypt Post; its cost allocation not defined.
- There is no asset management; funds are channeled into the National Investment Bank (a fund under the Ministry of the Economy that finances public infrastructure and social security).
- It has limited MIS, and no clearly defined marketing and management targets; hence there is no relevant system of managerial accountability.
- Pilot projects are underway to provide computerized services linked with cashless payment instruments (smart cards, ATMs, EFT, POS).
- It plays no role in international remittances.

Organization

The Postal Savings Fund is a part of ENPO. There are six divisions within ENPO, and two people with the rank of Director General manage the divisions of savings and financial affairs. The Director General for Financial Affairs is responsible for four departments: postal checks, budget and costs, procurement, and accounts. The Director General of the Savings Fund is responsible for another four departments: balance, deposits and investments, and documentary audits.

The accounts department keeps files of postal savings accounts with back-ups, and reconciles all postal savings transactions executed at post offices. The accounts department has a computerized platform, and an increasing number of post offices are linked with ICT to this platform.

ENPO's organization features a mix of functions for the financial management of ENPO and management of client deposits. Responsibilities for MIS are not clearly defined.

MIS and Product Profitability

Without a management information system, it is impossible to assess the profit contribution for the different business lines. Internal breakdown of revenues and cost show that post services (mail, parcels) operate at a loss and the postal savings profitable. It is unclear how and if the cost of the infrastructure has been allocated to the different product groups. It is possible that postal services are cross-subsidized by postal savings interest margin income or, just the opposite, that postal savings receive subsidized access to postal staff and offices. Moreover, it is unclear if and how the capital expenditure and amortization is allocated. An in-depth analysis could show which product and service really contribute to profit, where cost-reduction or volume increase would help, and where reform is needed.

The analysis should be relevant for assessing the commercial and economic feasibility of the current project using modern payment instruments (ATMs, EFT, POS). An important driver in these projects has been the perceived cost related to the pension payments (nearly 3 million per month), and the aim is—inter alia—to reduce this cost through modern technology and free up space in the post offices for more profitable transactions. Refined product profitability should even become critical when planning links between payments and savings products.

Postal Payments

Postal payments are also a traditional service provided by ENPO. The range of payments services extends from postal money orders to postal check and giro services to modern payment instruments (credit and debit bank cards, and credit and debit accounts on a pilot basis).

The volume of ordinary postal money orders is small—less than 1 million transactions per year—and decreasing. In addition, ENPO processes about 40 million disbursements for pensions and social security. The bulk of these disbursements is paid out in cash at post offices, a small part into postal savings accounts, and another part into newly introduced payment accounts (with ATM card). ENPO also processes more than 10 million payments for utility bills, subscriptions, etc. This volume is close to the volume of payments (12 million checks) processed by the banking sector in 2002.

The check clearing house in Cairo was computerized in 2002, but the other four or five clearing houses clear checks manually (paper-based). In this context, the small but efficient postal giro service appears to be valuable. It maintains nearly 10,000 accounts for public sector entities (e.g., municipalities, hospitals, utilities) and settled about 60,000 (high-value) giro transfers in 2002. Settlement of these payments takes 1–2 days. This differs from check payments that may take several days or weeks depending on the banks and clearinghouses, and the distances involved.

Theoretically, it is possible to transfer money from postal giro to bank accounts and vice versa. In practice, it operates as a closed circuit (which limits the risks for ENPO versus banks). In view of the plans to introduce more advanced payments services, links between ENPO and the banking sector will have to be established. The joint venture Giro-Nil which uses Banque Misr and CIB to process utility bills is a step in this direction. This could also solve one of the regulatory hurdles, since the joint venture’s operations could be connected to the clearing houses, based on the membership of the two banks involved.

International Remittances

Through its postal savings passbooks and bilateral agreements with the postal administrations in the Middle East, ENPO used to provide a handy remittance product for the large group of Egyptian workers in the Middle East. The remittance product—exposed to a variety of operational, currency exchange risk, and regulatory risks—disappeared and no substitutes have been engineered. ENPO also offers a traditional postal money order, but the volume and value of this service faces decline in a fast-growing market. In fact, with fewer than 7,000 transactions and a value of less than USD 1.5 million in 2002, in a market estimated at more than USD 5 billion, it represents an insignificant share.

Reportedly in summer 2003, ENPO selected Western Union—through a public auction—to launch its money transfers service in the post offices. The service is not operational yet, suggesting that ENPO or Western Union met substantial obstacles to implementation. In the Giro-Nil joint venture, CIB, one of the partner banks, recently became a member of the Eurogiro Network to develop cross-border payments between Egypt and the associated postal banks and administrations. This service, too, is not operational yet. Electronic money-order exchange services have been established between the postal operators in other countries, e.g., United Arab Emirates and Sudan, and Tunisia and Yemen, but not with Egypt.

With nearly 5 million Egyptians living abroad and the huge size of the remittance flow (USD 4.5 billion), international money transfers are a key, short-term opportunity for ENPO to improve and expand its financial services. ENPO's challenge will not be a “stand-alone” product, like Western Union, but a product whereby remittances can be captured in postal savings accounts, and /or the new postal payment accounts linked to a debit card.

Financial Sector Background

ENPO is part of the postal sector, and as such, its financial service operations are not regulated or supervised by the Central Bank of Egypt. Occasional discussions on repositioning or even privatizing the Postal Savings Fund have been held over the past eight years. Such a decision could seriously affect ENPO's mail operations, keeping them small and operating at a loss. Nothing will change unless the mail and parcel services are ensured of commercial viability. Another issue that has impacted the discussion to reposition the Postal Savings Fund is its investments in the National Investment Bank. Although this is a relatively small amount (less than 5 percent), there appears some resistance in the absence of an adequately developed capital and money market. With its current services, ENPO appears to fill in a void left by the banking sector.

Some banks do offer comprehensive retail financial services, but their outreach is very small. Fewer than 2.5 million Egyptians (of 65 million) have accounts with banks. About 9 million are said to have savings accounts in banks. The four largest banks in Egypt are state-owned and account for than half of the banking sector. The development of efficient retail financial services is not a key priority. The products these banks offer are neither accessible nor attractive to many low and middle-income Egyptian households, which helps explain why Postal Savings attracts so many clients. Despite a steady reduction of the importance of the public sector in the financial system, its role remains dominant, especially through its ownership of large banking and insurance institutions.

The dominance of the publicly-owned institutions in the Egyptian economy and their inability to match the performance of their international and private counterparts has limited the scope and depth of the financial market and its development. The range of financial products available is insufficient to meet the needs of private sector, and access of small and medium-size enterprises to these financial products is constrained. It is also reflected in the very limited outreach of modern retail banking and payments services. Reportedly, fewer than 2.5 million Egyptians have plastic bank cards and checking accounts like those in OECD countries.

International experience indicates that banking systems dominated by state banks can be reformed effectively through well-designed and well-managed privatization that focuses on improving governance and introducing market discipline. The four state-owned banks in Egypt (National Bank of Egypt, Bank of Alexandria, Banque du Caire, and Banque Misr) account for more than 60 percent of all loans and advances outstanding. Any program to develop the financial markets needs to address the effect of their public ownership on the development. Some preparatory steps have been taken with participation of private-sector management in the state-owned banks, but no clear schedules for privatization of any the state banks have been published yet.

Access to financial sector data has been limited, making judgments on the health of the financial system difficult. However, based on data provided by the authorities, Egypt's prudential standards conform to international standards. While capital adequacy requirements meet the minimums established by the Basel Committee, and regulations regarding loan classification and provisioning are in line with international standards, disclosure practices need further improvement. Non-performing loans have risen slightly as share of total portfolios (according to Central Bank of Egypt data, from 9.6 percent at the end of 1999 to 10.5 percent at the end of 2000). International experience indicates that rapid credit growth of the type seen in Egypt during the past decade is likely to be associated with a decline in lending standards. Banks, therefore, may be vulnerable to a deceleration of economic activity.

Under these circumstances, further strengthening of regulation and supervision standards needs to be given priority. This should be done in parallel with the extensive training effort being undertaken by the Central Bank of Egypt to upgrade banking skills across the board. The focus on these issues will, however, distract attention and potential sources from developing easily accessible financial services for the public at large and small entrepreneurs.

There are also issues related to the non-bank financial sector, such as implementing a well-designed mortgage law to facilitate better housing finance, developing the corporate bond markets, reforming the insurance sector, introducing new financial services, introducing new instruments (risk management instruments are particularly lacking), and assuring more market-based rural credit. However, in terms of strategic priority, the issue of the health of the banking system and modernization of the regulatory framework for the capital markets receive most emphasis from the government and international financial institutions.

Therefore, major initiatives to provide broad-based access to simple, efficient deposit and payments instruments are unlikely to be implemented. A repositioning of the Postal Savings Fund within the banking sector, e.g., by linking or merging it with one of the existing commercial banks, would not necessarily be an improvement or provide more services to individuals or small entrepreneurs.

ICT and Financial Services

MCIT, the ministry that leads ENPO and regulates the postal sector, has also undertaken significant initiatives to modernize and liberalize the financial sector. MCIT has formed committees with the Central Bank of Egypt and the banking community. These initiatives may not immediately improve access to financial services, but may create conditions that could facilitate the development of efficient and solid retail financial services in the medium and long term. These committees have developed a framework for establishing the first retail credit information center, or credit bureau. Credit bureaus play an instrumental role in expanding microcredit services and are essential for the growth of the bank card industry and the transformation to a cashless society.

To encourage e-business in Egypt, the government is working to draft an Electronic Signature Law that will create an enabling regulatory and legal environment for conducting online transactions. The law is one of the new cyber-laws that should have a major impact on developing a thriving e-business in Egypt. Signing transactions online will soon become a reality, making both banking and e-government services in Egypt faster and easier to use. A law authenticating e-signatures has been drafted in co-operation with all concerned public and private sector partners and has been submitted for approval to the cabinet and parliament.

A number of projects to help establish a business environment conducive to ICT-driven commerce have been launched. MCIT has developed a framework to network chambers of commerce to facilitate the flow of information and improve trading and economic performance. Each chamber of commerce will have an internal network (local area network, or LAN) and access to a shared electronic database. A wide area network will be established to connect them with MCIT, which will provide the necessary infrastructure for this purpose.

Almost all banks currently operating in Egypt are fully automated and have core banking applications with SWIFT and fast-cash services, as well as their own switching software for online transactions. Over the past decade, the banks were automated, and routers, mail servers, and LAN switches installed. More than 70 percent of all Egyptian banks have developed or are in the process of developing, e-banking solutions that give both individual and business clients access to accounts and other banking services. Some have set up systems for e-banking, e-commerce, archiving systems, interconnected databases, and smart cards for customers' deposits. During fiscal years 2002 and 2003, there were nearly 217,000 SWIFT electronic transfers, related to settlements between banks through the Central Bank

An information network linking the Central Bank of Egypt with 50 banks using frame-relay technology has been established. In addition, banks possess communication links between their branches. The information network is vital to efficient utilization of the financial information systems at the Central Bank. These systems include an electronic check-clearing system that handled over 10 million checks during the fiscal years 2002 and 2003, totaling about EGP 245 billion. The information systems adopted at the Central Bank also include the credit risks' management system, and the foreign currency exchange system.

This trend toward adopting ICT solutions in banking began in the early 1990s with the implementation of consumer credit programs and automatic teller machines (ATMs). Egypt currently has over 1200 ATMs—particularly used by tourists—and the number is increasing annually by an average of 40 percent. Major merchants and retail stores in the Greater Cairo area have almost 15,000 point of sale (POS) devices that accept local and international credit cards. The estimated value of transactions through ATMs and POS is over EGP 15 billion. The annual growth rate in the number of credit and debit bank cards issued exceeds 30 percent, with over 2 million cards in use. Banks issue debit cards to give customers access to their accounts, and banks have, on average, issued cards to more than 70 percent of their customers. There are projects currently being implemented at the National Post Authority and in commercial banks to provide pension payments through ATM machines.

Several banks in Egypt have started mobile and Internet-banking pilot projects to make it easier for people to do their banking from their home or office. Internet access and a browser that supports 128-bit encryption, such as Netscape Navigator or Microsoft Internet Explorer, are almost all that is needed for Internet banking. Comprehensive account services are available with Internet banking, including account information, trust checking accounts, savings accounts, certificates of deposit, loans, transaction inquiries. Currently, seven Egyptian banks are licensed by the Central Bank of Egypt to offer e-banking. The Egyptian Banking Company for Technological Development operates a system for linking and switching transactions for electronic fund transfer from 865 ATMs owned by 30 Egyptian banks with links to regional and international networks, such as Diners Club, American Express, and MasterCard.

These important steps are creating a legal and IT framework, and although application is running at a relatively small scale, it should gradually gain momentum. As seen in several other countries, these services could remain privileged to a small group or gain wide spread use. The Postal Savings Fund's database and its postal network could have a critical role in expanding the new services to provide broad-based access to cashless (electronic) payments instruments and hence to more efficient retail financial services.

Microfinance

Although Egypt may have more than 60 banks and a network of over 2,000 branches,[4] the financial sector does not meet the needs of the microentrepreneurs, as banks have not typically offered loans smaller than EGP 25,000 (the equivalent of about USD 4,025). However, the Economic Reform and Structural Adjustment Program that Egypt has undertaken includes the liberalization of the financial sector. The Central Bank of Egypt thus no longer sets an interest rate ceiling which opens the possibility for banks to develop a strategy for serving the market. On the other hand, government ownership of commercial banks continues, with the state-owned banks dominating the sector. (The four public-sector commercial banks have 883 branches versus 298 branches of private and joint venture commercial banks.) The four public banks, National Bank of Egypt, the Bank of Alexandria, the Banque du Caire and the Banque Misr, account for 62 percent of the banking system’s assets. There are 32 business and investment banks, as well as four specialized banks, including the Principal Bank for Development and Agricultural Credit with its network.

The National Bank for Development

The National Bank for Development (NBD) began its program in 1991 (with start-up aid from USAID, the Ford Foundation, UNICEF, and CIDA), as the first commercial bank in the region to branch into microfinance. Microfinance services are now actively provided in 44 of its 66 branches in 17 governates. The program reportedly is now self-sustaining, and NBD has matched all credit funds provided by international donors. Some 20 of the 44 branches are donor-financed and 24 are self-funded. It also provides a program for small and medium entrepreneurs in all 66 branches, funded by its own resources. NBD had 22,600 active borrowers with USD 8 million in outstanding loans. To extend its program, NBD reduced the maximum loan size from EGP 10,000 to 3,000 in 2003. The average loan size is USD 480. NBD has also introduced a successful insurance product.

A unique feature of NBD’s microfinance program is its mobile banking units, which although costly, has extended outreach by delivering services to the doorstep. A mini-van with a driver, tellers, and loan officers visits areas in Cairo where the bank has no branches. Loan payments are collected, new loans are disbursed, and applications are reviewed. Even in areas where the bank has branches, NBD has adopted standard microfinance practices and loan officers visit borrowers every week to collect payments.

There are two exceptions to the barriers to small loans in the banking sector: two commercial banks, the National Bank for Development and the Banque du Caire, have implemented their own microfinance strategies to provide direct loans to microentrepreneurs. The success of these two programs could and should demonstrate to the rest of the sector that microfinance can be a viable business line. In both banks, the microfinance programs have been set up as separate units with different practices and procedures than the rest of the bank. Other exceptions to small loans among commercial banks are the partners who participate in the Social Fund for Development programs.

[4] Included in the 2,000 branches are about 1,800 branches of the Principal Bank for Development and Agricultural Credit (PBDAC). The PBDAC does provide microloans and small loans primarily for agriculture and rural needs, through village banks in the countryside.

Microfinance Institutions in Egypt

Outreach • **Borrowers** • **Savers**	 220,000 n/a
Loan portfolio	USD 52 million
Savings	n/a
Average loan size	USD 736
Points of service	n/a
Estimated market penetration	5%

The banks operating microfinance programs are subject to the regulation of the Central Bank of Egypt. Although, as previously noted, the Central Bank no longer imposes interest rate ceilings, there are two large microfinance programs, which are subject to some special regulations. The PBDAC is subjected to reduced interest rates by sovereign decrees. The Social Fund for Development loans are subject to the same decrees, which means they must offer lower interest rates than non-Social Fund for Development bank loans. Both programs are also sometimes subjected to government imposed constraints to their collection policies, through forced debt forgiveness and/or debt rescheduling.

Microfinance in Egypt dates from the early 1990s, when it developed with substantial support from several international donors. Whether potential is measured by the size of the microentrepreneurial sector or defined population sectors, Egypt has the largest potential market for microfinance in the Arab world, but is far from realizing the full potential of its microfinance market with 220,000 clients. In a recent survey of microfinance in the Middle East, Egypt had 32 percent of the active borrowers and 39 percent of the total microfinance portfolio. (Large government-run programs were excluded from the survey.) Morocco, with a smaller population, had 250,000 microfinance clients, which represented 52 percent of the active borrowers and 35 percent of the loan portfolio outstanding. The number of existing microentrepreneurs (non-agricultural) in Egypt is estimated at between 1.5 and 2 million, of an estimated population of 68 million (which is growing at more than 2 percent per annum). The potential number of microenterprises is estimated at between 2 and 3 million, if access to financial services were available.

In both absolute and relative terms, however, penetration of microfinance into the market is still quite shallow, with only 220,000-plus microentrepreneurs having access to services, according to a 2003 survey. It is widely assumed that this figure underestimates the client base because it excludes those clients funded by Social Fund for Development clients and other providers who did not participate in the 2003 survey. (The Social Fund for Development small enterprise loan portfolio at year-end 2000 totaled USD 115 million.) Morocco, with a population of 30 million with 500,000 existing microenterprises (estimated), has a dynamic microfinance sector serving over 250,000 clients. Most observers feel that only 5 percent of the demand for microcredit is currently being met.

To date, donors and the Egyptian government have financed the bulk of support to the microfinance sector, through direct institutional investments. There has been little effort to look at the sector as a whole. A suitable legal framework does not exist. Most MFIs operate as non-governmental organizations (NGOs), governed by the Ministry of Social Affairs. As such, they face several problems, including inability to mobilize savings, difficulty in accessing commercial banks and other commercial sources to fund their expansion, onerous collateral requirements for commercial bank funding, and structures and governance which are unsuitable for microfinance.

MFI Market

The informal sector in Egypt is large and is generally given credit for providing as much as 50 percent of the economic activity, although no reliable data exists. With 99 percent of the population concentrated in the Nile valley and delta, the high population density should facilitate the expansion of financial services to the informal sector. The informal sector absorbs a major part of the labor in Egypt, providing a wide variety of goods and services. In addition to the NGOs involved in delivering financial services to the informal sector, family members, ROSCAs, pawn brokers, supplier creditors, and moneylenders provide finance to the microenterprises.

In an Egyptian context, microfinance loans are defined by either their size, less than EGP 10,000 (USD $1,610, or 130 percent of per capita GDP) or fewer than five employees. There is considerable variance in the size of loans made by the different microfinance operators in Egypt. In ESED Bank, for example, loans to microentrepreneurs range from USD 150–5,000, for everything from small working capital to purchases of small machinery. The 2003 UNDP survey expected that the 200,000 clients at the end of 2003 would double by 2005. As noted, the survey did not include the Social Fund for Development program, which is substantial. USAID-supported microfinance programs constitute 92.9 percent of the existing 200,000 client base.

The legal forms in Egypt available to MFIs include NGO structures and formal financial institutions (FFIs). The NGO structure for microfinance in Egypt requires all NGOs to be registered under the Ministry of Social Affairs. Specifically, it requires their boards of directors to play an active management role in some types of institutions, including signing all checks, for example. The ministry has the authority to inspect NGOs and to require a change in their boards if the inspection is unsatisfactory. FFIs are subject to regulation by the Central Audit Agency, the Central Bank of Egypt, and the Egypt Bank's Union. FFIs are subject to other requirements, which include paid-in capital, a license from Central Bank of Egypt, legal reserves at Central Bank of Egypt, and conformity with Central Bank of Egypt reporting requirements.

Scope of USAID-Supported Microloan Programs in Egypt*

MFI	Number of Active Borrowers	Loan Portfolio (USD)	Number of Branches
I. USAID-Supported MFIs			
ABA	43,532	8,714,762	
ESED	31,267	7,333,575	
SEDAP	3,980	904,892	
ASBA	35,452	8,191,254	
SBACD	12,470	2,514,476	4
DBACD	19,606	3,841,833	
Banque du Caire[5]	38,757	11,754,791	233**
Other institutions	3,928	1,035,344	
Subtotal USAID	***185,708***	***43,860,573***	
II. OTHER MFIS			
National Bank for Development	22,600	8,200,000	44

[5] The Banque du Caire is a rapidly growing program, and may have surpassed ABA, by the time of this writing, to become the largest program in Egypt.

Subtotal Other MFIs	***22,600***	***8,200,000***	
TOTAL	**208,308**	**52,060,573**	

* www.planetrating.org. Ratings Report, SBACD, April 2004, based on data from September 2003.

** Microfinance services are available in all BdC branches, according to Elizabeth Littlefield and Richard Rosenberg in "Microfinance and the Poor," *Finance and Development* 41, no.2 (June 2004).

There are 14 NGO programs per 1998 data, compared to the two commercial banks. Despite more NGO programs, the two commercial bank programs provide USD 20 million of a total USD 52 million in loans to the sector.

Egypt has five MFIs that are fully financially sustainable, and six MFIs that are almost financially sustainable (>80 percent), according to a recent SANABEL survey.[6] In Egypt, individual lending is the dominant form of microfinance, although there are a few village banking systems. Individual loans represent 70 percent of the portfolio. The average loan size was estimated to be around USD 736[7] in 1998, well below per-capita income levels, suggesting that the existing programs are targeting the poor. Women clients are under-represented, only 20 percent of the client base, indicating depth of the social barriers which confront the outreach efforts of the MFIs.

Donor Support

To date, there have been no pilots or experiments with microfinance and the post offices. Inside ENPO, there has been some discussion about microcredit and consumer loans. Microfinance does not fall within the scope of the Postal Savings Fund. In the context of developing stronger and more efficient ICT-based financial services, and the early stage of partnership with two commercial banks, providing small credit is a medium term priority.

3—Options for Development

ENPO plays a valuable role in providing broad-based access to basic financial services. With a network that is more than four times larger than the entire banking sector, it provides low-threshold access to deposit mobilization and payments services. With its low minimum-deposit requirement, dense network of post offices, and image as a non-bank, ENPO can attract a growing number of depositors even though its products are somewhat antiquated. As post offices become computerized, the postal savings service can offer fairly efficient, reliable, and straightforward products, compared to what the four Egyptian state banks offer, to lower- and middle-income groups. The number of postal savers has doubled from 6 million in 1997 to 12 million in 2004; the postal savings amount to EGP 22 billion (approximately USD 5.1 billion).

Postal savings are reinvested with the National Investment Bank, a government fund that is also in charge of investing social security funds and reserve management. It invests money in long-term public sector projects. The postal savings and its operations are operated and regulated under the postal sector law, and thus fall outside of the supervision by the Central Bank of Egypt. The Ministry of Communications and Information Technology is responsible for postal sector development and is the owner of ENPO.

[6] Judith Brandsma, "The Third Microfinance Survey in the Arab World: Preliminary Results," presentation at the First Annual Conference of SANABEL, Microfinance Network of Arab Countries, December 2003.

[7] Judith Brandsma and Rafika Chaouali, "Making Microfinance Work in the Middle East and North Africa," Working Paper No. 23076 (Washington, DC: World Bank, 1998). A more recent SANABEL survey in 2002 put the average loan size at USD 349, but it is based on a less-inclusive survey.

The postal savings interest margin income is ENPO's largest revenue component, more than 60 percent of total revenues The spread between client interest rate and the rate paid by the National Investment Bank is 0.5 percent, and seems to exert a pressure on ENPO to operate efficiently.

The continued growth in postal savings balances and, hence, interest margin income have made ENPO a profitable organization, in spite of its declining mail volumes and heavily regulated pricing (low postal prices that do not cover the cost of mail service). With fewer than three mail items per capita posted per year, Egypt's mail demand is low and, given the market condition, is unlikely to increase much in the medium to long-term. There is no historical bulk-mail market (bank account statements, public utility bills, etc.) and, should demand ever evolve, postal services would be pitted against increasingly available alternative communications. Also, the prospects for mail volume growth from direct marketing and e-commerce are very limited in the short to medium term. Demand for courier, express, parcel, and international mail is concentrated in the business sections of Cairo and Alexandria. These types of mail service have been formally opened to the private sector (e.g., UPS, DHL, FedEx, and TNT), and de facto liberalization has occurred through a large number of other private operators. Substantial growth perspectives for ENPO in mail and parcel services seem non-existent in the short-term, but could evolve in the longer term with support of hybrid mail and e-commerce.

Although there is no publicly available postal sector policy or postal reform strategy, it appears that priority is given to strengthening ENPO's role with ICT as a nationwide network and delivery channel that provides access to electronic financial services and modern information and communications facilities. Initiatives to build links with the banking sector through a joint venture may also be useful first steps toward developing stronger partnerships between one or more financial institutions and the postal network. Such partnerships could help to expand the range of financial services available at post offices, while operating and managing these services on a competitive basis and in compliance with the financial sector regulations. Nationwide rollout from current small-scale pilots is still a long way off.

One positive aspect is that ENPO generates pre-tax profit currently in excess of USD 5 million, which is critical as a funding source for investing in the modernization of postal services and products nationwide. Although there is a fairly stable outlook for a continued positive cash flow generated through growing postal savings and increasingly cost-efficient postal payments, this is not ensured. The risks to which this revenue stream is exposed vary from (1) volatility in the financial markets (interest rates, emerging competition, technology scams) that could have a negative impact on the behavior of postal savers; to (2) political problems if the National Investment Bank is restructured in view of reforming the social security and pension systems, and/or government finance; and (3) if the decline of postal mail volume accelerates and/or if capital expenditure in postal mail processing is prioritized. The risks are difficult to assess and to manage particularly because there are no market and management information systems within ENPO.

ENPO's current approach of initiating pilot programs to test new products and services or applications may appear sensible. But if they are to be rolled out and sustained, it is critically important that these pilot programs include detailed market and consumer research prior, during, and after the pilot, such as:

- detailed financial planning, budgeting, and control so that the economic and financial impact of the pilot programs can be assessed (Ideally, each pilot should be based on a project finance plan, including a separate cost-benefit analysis with cash-flow forecasts.);
- an evaluation of project and product profitability, subsequent extension of MIS, and the establishment of a broader, company-wide set of planning, budgeting, accounting, control, and internal audit functions;
- organizational (re)design as follow-up to the pilots and the availability of more sophisticated MIS (It would also become necessary to separate the financial *management* function from the financial *services* function. One is a staff department supporting the management in financial planning, budgeting, and control; the other is a business unit responsible for marketing and the operations of clients’ postal savings and payment services. A separate *treasury* function would be responsible for the overall cash and liquidity management of the postal financial services, correspondent bank relations, and the asset management.); and

- steps likely to lead to broader company-wide restructuring, including creation of business units (profit centers) for the mail and parcel services and the retail network, and eventually to provide a basis for overall commercial and corporate development of ENPO.

While the above steps would be key components in a two-year program to strengthen ENPO as an institution, it would be useful for ENPO to consider at least two other pilot programs and apply the experiences to the program testing new products and services (above):

- a pilot testing more advanced international remittance products, utilizing fast electronic communications, in combination with the option of directly crediting the remittance into a postal savings account or into a newly-launched postal accounts with debit cards; and
- a pilot to test microfinance on a small scale in a rural area in collaboration with a reputable microfinance institutions; where the program aims at testing the viability of using the postal network as an agent or channel for microfinance products, such processing credit applications and collecting periodic payments.

The pilot tests should provide practical and locally-applicable experience in setting up new financial services through the postal network, based on modern ICT. The results of the pilots should provide a design for a revised development strategy of ENPO within the changing financial and communication sector. A next step would likely include an organizational redesign of ENPO to strengthen it and help it develop commercially and financially in a sustainable manner. These steps would eventually allow options for private sector participation in ENPO to be assessed in a structured and balanced manner.