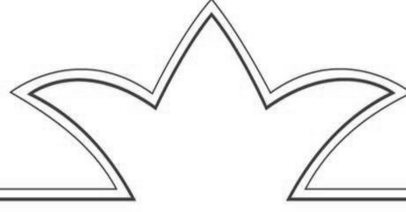

المركز المصرى للدراسات الإقتصادية

ECES

The Egyptian Center for Economic Studies

The Egyptian Banking System:
Liberalization, Competition and Privatization

Alan R. Roe

Working Paper No. 28
June 1998

The author is currently Senior Financial Economist in the Europe and Central Asia Region Department at the World Bank. This paper, however, is written entirely in a personal capacity and in no way reflects the official viewpoint of the Bank. While the paper has benefited greatly from conversations with World Bank specialists on Egypt, none of these colleagues bears any responsibility for the content herewith.

This paper was presented in Cairo in February 1997 at an ECES conference entitled, "Towards an Efficient Financial Market in Egypt." It will also appear in a forthcoming book on the conference.

Abstract

Egypt's efforts to liberalize its financial sector in the 1990s have been impressive. Egyptian authorities have been successful in reversing more than three decades of interventionist policies. The fundamental building blocks of this liberalization process now seem solid. They include a reduced fiscal deficit, and the unification and freeing of exchange rates, interest rates, and lending decisions from administrative control. The initial privatization of large banks has removed some of the extensive ownership links between banks—one likely cause of uncompetitive banking. The benefits of reform are beginning to show: inflation control consistent with growth rates, confidence in local currency, and buoyant stock market activity buttressed by numerous prominent privatizations. Capital flows into the economy have also been much stronger. Nevertheless, the transformation of the Egyptian financial sector into a modern market-oriented system is still in its infancy. In the future, economic changes which policies can affect should go hand in hand with institutional and attitudinal changes which are potentially more difficult to bring about. Policy makers must continue to work hard to build on the foundations they have laid thus far.

ملخص

قامت مصر بجهود رائعة في خلال التسعينيات لتحرير القطاع المالى. وقد نجحت السلطات المصرية فى تحقيق انقلاب كامل فى سياساتها التى كانت قائمة على الدخل والتى استمرت ما يزيد على ثلاث عقود. والآن ثبتت سلامة وصلابة القواعد والأسس التى قامت عليها عملية التحرير، إذ تضمنت تلك الأسس تخفيض عجز الموازنة، وتوحيد وتحرير أسعار الصرف، وتحرير أسعار الفائدة وقرارات الإقراض من القيود الإدارية. كما أدت عملية الخصخصة الولية للبنوك الكبرى إلى إزالة جزء من علاقات الملكية المتشبعة فيما بين البنوك، والتى تغذيها عمليات الخصخصة المتعددة. وفضلاً عم ذلك، فقد ازدادت التدفقات الرأسمالية الداخلة إلى الاقتصادز وعلى أيه حال، فإن عملية تحول القطاع المالى المصرى إلى نظام حديث قائم على أساس السوق، مازالت فى مهدها. وينبغى فى المستقبل أن تكون التغيرات الاقتصادية التى تؤدى إليها السياسات مصحوبة بتغير فى المؤسسات والتنظيمات والإجراءات والسلوكيات وهو أمر أكثر صعوبة. وعلى واضعى السياسات أن يعملوا على ذات السس التى أرسلوا قواعدها حتى الآن.

I. Introduction

Egypt, like many other developing economies, has spent much of its post-independence history operating in an illiberal economic environment in which commodity, labor and financial markets are all subject to significant degrees of official intervention. But, during the 1990s, liberalization has been a prominent theme of Egyptian economic policy. Most major markets, and especially financial markets, have been freed from some of their previous restrictions. Since 1991, this liberalization initiative has opened up many possibilities for deeper and more effective financial markets. But it has also introduced numerous dilemmas for policy makers both in banking and macroeconomic management. It is the purpose of this paper to explore the consequences of the pre-reform situation in the financial sector and some of the opportunities and problems associated with the liberalization of that sector.

Since the author claims no deep familiarity with the Egyptian situation, the paper focuses on certain features and problems associated with the process of financial liberalization in general and attempts to draw possible lessons for Egypt from this general basis. It makes no attempt to explore certain important institutional aspects of Egypt's future banking development including, for example, issues about the need for more universal and less specialized banking and the need for greater geographical decentralization of banking services.

II. Illiberal Finance: Nature and Consequences

The illiberal financial policies applied in many developing countries are well documented and easily summarized (see Box 1).

The *consequences* of these various interventions as shown in numerous country case studies include:

- relatively stable nominal deposit and lending rates at low levels, even in countries suffering high and variable inflation (in other words, real interest rates have been highly variable and frequently very negative);[1]
- credit rationing caused by the administrative setting of non-equilibrium interest rates and the emergence of associated allocative mechanisms for credit based on cost or

[1] See Hanson, J.A., and C. Neal, "A Review of Interest Rate Policy in Selected Developing Countries, 1970-1982," *World Bank Research Report, No. 5391*, Washington, D.C., 1984.

risk minimization (paradoxically, these mechanisms actually reduced the shares of credit going to the supposedly "preferred" sectors);[2]

- the repression of the domestic formal financial system (as measured, for example, by the ratio of financial assets outstanding to GDP), since domestic financial assets become progressively less attractive relative to alternatives, such as inflation hedges and foreign assets;
- the emergence or expansion of various informal sector institutions to substitute for some of the business repressed out from the formal channels;[3]

Box 1. The Main Characteristics of Illiberal Financial Systems[4]

- administrative control on most deposit and lending interest rates;
- considerable administrative control over the allocation of credit to particular sectors (for example, agriculture, government, small-scale business);[5]
- preferential interest rates to certain (though normally the same) sectors;
- high taxation of the basic banking sector through reserve requirements in excess of necessary prudential requirements;
- forced sales of low yielding government securities to banks and other financial institutions often through the device of high liquidity requirements;
- significant controls on new entry into the banking sector and especially new entry involving foreign investment;
- direct state-ownership of banks in some cases; and
- tight controls on external capital movements both inward and outward , motivated in part by a need to protect and preserve the domestic financial sector arrangements shown in the rest of this list.

---

[2] This point is argued more fully in Alan Roe, "Some Theory Concerning the Role and Failings of Financial Intermediation in Developing Countries," in V.V. Bhatt (ed.), *Capital Market Imperfections and Economic Development*, World Bank, 1979.

[3] Although it should be noted that there is considerable dissent from the simple McKinnon-Shaw view that informal financial institutions are likely to decline in importance as formal finance is liberalized. See, for example, Dale Adams, "Taking a Fresh Look at Informal Finance," in Philippe Callier (ed.), *Financial Systems and Development in Africa,* EDI Seminar Series, World Bank, 1991.

[4] The various studies which have provided such a listing include Hansan, J.A., and Neal, ibid.

[5] Some typical examples include: 75 percent of Turkey 's banking loans in the early 1980s were made under government direction; 54-68 percent in the case of Pakistan in the late 1980s and the early 1990s; 80 percent in the case of Brazil in 1986/87; and 56 percent in the case of Columbia. See World Bank, "The East Asian Miracle: Economic Growth and Public Policy, " *Policy Research Report*, July 1993.

- limited diversification of asset and liability structures as well as the institutional structures of the financial sectors and their continued domination by relatively unsophisticated commercial banks;
- a high ratio of non-performing loans associated with directed credits — especially when these loans are granted to public enterprises and are partly political in nature;
- pressures on the profitability and the capital base of banks because of high and under-remunerated reserves and substantial non-performing loans;
- a large proportion of intermediated domestic savings being pre-empted for government use (for example, via high reserve requirements and captive sales of government securities and via seigniorage and inflation tax mechanisms);
- serious constraints on the possibilities of opening up the capital account of the balance of payments due to the limited range of local financial products and their poor risk/return characteristics; and
- *either* high margins between deposit and lending rates of interest in banks caused both by high and unremunerated reserve requirements,[6] and by high levels of non-performing loans, leading to reduced volumes of banking business, *or* high rates of distress in commercial banks to the extent that it is impossible to set lending interest rates high enough to absorb the burdens of high reserve requirements and portfolio losses.[7]

III. Illiberal Finance: The Egyptian Experience

Even a brief perusal of the Egyptian literature used to prepare this paper confirms how relevant most of these features of financial illiberality were for Egypt throughout the 1960s and even after the *Infitah* (Opening Up) period after 1974 and until the end of the 1980s. World Bank,[8] Mohieldin,[9] and studies conducted between 1960 and 1990, identify the following points as features of the Egyptian experience prior to 1990:

---

[6] A model elaborating this set of connections is presented by Mathieson, D.J. and R. McKinnon, "How To Manage a Repressed Economy," *Princeton Papers in International Finance*, 1981.

[7] This could arise either because of the administrative controls on interest rates or because of arguments associated with adverse selection.

[8] World Bank, "Egypt, Financial Policy for Adjustment and Growth," *Report No. 10790 GT*, September 1993.

- Nominal deposit interest rates were near constant at or below 5 percent for most of the period between 1960 and 1980 and remained consistently negative in real terms from the mid-1970s until 1990 in spite of increases in nominal rates to well above 10 percent.[10]
- The negative real interest rates in turn resulted in excess credit demand which the authorities handled by imposing bank specific credit ceilings.
- Reserve requirements on banks were consistently high and were actually increased during the *Infitah* period to 25 percent of deposits. Mohieldin estimates that this added 1.7 percentage points to the interest rate spreads charged by banks.
- Interest rate spreads remained persistently high (up to 6 percent with an average of 4.4 percent after 1976).
- Credit allocations were affected administratively through a variety of interest rate and other devices causing the share of credit going to the public sector to average more than 70 percent of the total during the period between 1960 and 1990.
- Inflation tax revenues during the same period averaged over 6 percent of GDP and the government also extracted additional large revenues from seigniorage and from the implicit tax revenues constituted by the gap between market and administered interest rates.
- High liquidity requirements imposed on banks (the average between 1960 and 1990 was 30 percent of deposits) conspired with other features of the illiberal environment to produce very high levels of actual liquidity in banks through the whole of that period.
- The four public sector banks directly, and indirectly through their stakes in joint venture banks, accounted for the dominant part of total bank assets and branches (90 percent[11]) with restrictions on entry, branching, and the activities which banks were allowed to do to preserve this highly concentrated situation.

---

[9] Mahmoud Mohieldin, “Causes, Measures and Impact of State Intervention in the Financial Sector: The Egyptian Experience,” paper presented at the conference on The Changing Role of the State in Economic Development and Growth, Rabat, Morocco, January 1995.

[10] Ibid., Figure 5.

[11] M.M. Giugale and H. Mobarak, *Private Sector Development in Egypt*, The American University in Cairo Press, 1995, Ch. 7.

- The public banks generally maintained very poor quality portfolios characterized by limited diversification and high rates of non-performing loans variously estimated at 30 percent[12] and 40-45 percent of total loans, respectively.
- A rising interest spread favoring foreign currency deposits provoked an increase in the private holdings of such deposits to more than 50 percent of total deposits in banks by the end of the 1980s.
- Capital flight resulted from that same differential through the 1980s amounting to $30 billion per annum. In the 1980s, the cumulative capital flight was equivalent to over 150 percent of the country's total increase in external debt.
- The demoralization of Egypt's formerly active Securities Markets resulted in a major decline in market capitalization relative to GDP (only 7.1 percent by 1990) and a substantial decline in the proportion of enterprise funding raised from this source.

There are various ways to encapsulate this large list of interventions and summarize their potentially damaging consequences for Egypt's economic performance. The traditional argument contends that there is both a *quantitative* and a *qualitative* dimension to these consequences.

The *quantitative* dimension relates to the possible reduction in total private savings; to the reduced part of total savings which is intermediated through the banking system; and to the loss of investible resources associated with capital flight. In many highly repressed financial systems, the quantitative effects have been very serious and have resulted, for example, in Money/GDP ratios falling to about 10 percent or even less (Uganda and Ghana in the early 1980s and Russia and Ukraine at the present time). This collapse of money holdings and the transfer of money balances into inflation hedges or foreign assets can rapidly generate an unstable macroeconomic situation in which the reduced base for the inflation tax conspires with still-large fiscal deficits to generate higher and eventually spiraling inflation.

For reasons which are not entirely clear, this syndrome of chronic instability was averted in Egypt during its long period of financial sector illiberality — inflation, though quite volatile, rarely moved above 20 percent. The ratio of M2/GDP held up at around 50

---

[12] World Bank, "Egypt, Financial Policy for Adjustment and Growth," *Report No. 10790 GT*, September 1993.

percent or more through the 1980s in spite of fiscal deficits which were consistently above 5 percent of GDP on any definition and frequently above 20 percent using Egyptian definitions.[13] Although there was a substantial foreign currency component in total money, the domestic component remained surprisingly high. One possible explanation of this paradox is that ubiquitous controls, especially on prices and interest rates, short-circuited some of the mechanisms through which the effects of financial repression would normally work their quantitative effects. This short-circuiting, however, may also build up adverse consequences in the domestic banks in the form of weak profitability and capital positions.[14] Another explanation is that the highly socialized nature of the Egyptian economy created physical shortages of commodities and a corresponding passive demand to hold money balances referred to in other contexts as a "monetary overhang."[15]

The adverse *qualitative* effects of many years of financial repression are less ambiguous. The dominance of large public banks in the channeling of credit, as well as tight administrative controls on credit pricing, almost certainly created in Egypt a culture of banking found, albeit in a more extreme form, in all the transition economies of Eastern Europe and the Soviet Union. This is described, for the Ukraine, as follows:

> "Banking services during Soviet times were primarily provided by a government dominated bureaucracy that processed documentation. Bank personnel were used merely to provide financial accounting records on credits obtained by entities for specific projects decided centrally under five-year plans. The banks' activities include no serious financial analyses, or any review of the profitability, credit

---

[13] The Egyptian definitions have generally recorded higher values for the deficit than IMF definitions (see Mohieldin, Figure 1).

[14] For example, very high reserve requirements in banks would normally result in some attempt on the part of banks to charge high interest rates to borrowers to achieve any given profit target. This in turn may reduce loan demand and hence the enthusiasm with which banks would seek to mobilise deposits. It would result in lower levels of deposits in the equilibrium with high reserve requirements than in the equilibrium where such requirements were more modest. Non-commercial charging by banks, however, could short-circuit or delay this effect but only at the expense of bank profitability (perhaps because the banks were fully constrained in their lending rates, and were interested in protecting the interest of their state-owned clients, or because they were uninterested in profit targets).

[15] Mohieldin puts forward the counter argument that there was some implicit contract between depositors and the government. So long as government price controls kept inflation at fairly moderate levels, depositors implicitly agreed to hold money balances which were relatively high in spite of the losses they sustained associated with negative real interest rates. This is not entirely convincing since it suggests behavioural patterns in Egypt which are not found in most other illiberal economies.

> worthiness, or riskiness of projects or the enterprises undertaking them. These traditional 'banking' activities were considered irrelevant by Soviet bankers…. These institutional limitations still bedevil effective banking some six years after the break up of the Soviet Union."[16]

The qualitative effects exemplified in the extreme in the Soviet Union are nevertheless relevant, with only limited modification, to Egypt. They have several components. The first is a serious limit in the range and sophistication of products offered by banks and the range of skills needed in bank staff, especially the skills required in assessing and managing risk. Another component is that, in an economy where bank lending is mainly a business between state-owned enterprises (the borrowers) and state-owned banks (the lenders), both of whom can have losses covered by the budget, incentives to borrow only for "good" projects and to grant "good" loans are likely to be diluted. This together with a distorted pattern of interest rates is likely to result in financial inefficiency (lending which is seriously suboptimal in its risk/return characteristics). Decapitalized banks and enterprises are likely to be empowered to operate for long periods of time as though they were solvent on the grounds that their missing capital is implicitly available from the state. Finally, there is a component of allocative inefficiency: too many productive resources allocated to activities in which the country enjoys little comparative advantage.

In addition to the efficiency losses already incurred, the *dirigisme* to which the Egyptian system was subject for more than three decades has almost certainly left a damaging ongoing legacy which the mere act of liberalizing markets is unlikely to remove. The *financial* inefficiency of much of the lending of the past leaves the legacy of poorly capitalized banks. The *economic* inefficiency of much of that lending leaves the legacy of a suboptimal productive sector economy. The limited scope of banking in an illiberal setting leaves a third legacy in the form of limited diversity of banking products and banking skills. The challenge of liberalization is to establish effective markets which can avoid the further accumulation of such problems, and to do this while the legacies of past policies (the stock problems) continue to exert significant negative effects. This is not an easy matter.

---

[16] Peter Sochen, "The Banking System in Ukraine," Center for Social and Economic Research, *Studies and Analysis Paper No. 65*, Warsaw, March 1996.

IV. Financial Reform Since 1991

The critical underpinning of Egypt's efforts to liberalize financial markets beginning in 1991 is the major *fiscal reform* which has characterized the stabilization program of recent years. Egypt's overall fiscal deficit was reduced from over 18 percent of GDP in 1990/91 to 3.5 percent by 1992/93 and more recently to only about 1 percent. Total public savings, which excludes public investment but includes the deficits of public authorities and public enterprises, has been positive in recent years. This improvement stems from lower public subsidies, transfers, and interest payments and from significant improvements in the performance of Law 203 enterprises[17] which have recorded an overall profit since 1994.

The radical improvement in fiscal performance has made possible much lower inflation which declined to about 7 percent by 1995 from over 21 percent in 1991. This underpinning of improved monetary stability in turn made it possible to introduce the first cautious reforms of the previously illiberal financial policies. In particular, *controls on interest rates* charged by banks were lifted early in 1992, as were the fixed tariffs on certain services. Ceilings on lending were also abolished in the same year and more indirect methods of monetary control were instituted. Although nominal interest rates at first rose slightly—for example, from below 10 percent to almost 17 percent for short-term deposits by mid-1993—they subsequently declined. By June 1995, short-term deposit rates were once again at about 10 percent and rates on bank loans were averaging about 14 percent.

A major structural change also made possible by the success of macroeconomic stabilization is the accelerated program to *privatize state enterprises* introduced by the new Cabinet early in 1996. As one important element of this program, it is now official policy to privatize the government's stakes in all 23 of the joint-venture (JV) banks.[18] This is seen as a step to improve competitiveness in banking. But, even more important, it is expected to lessen the commercial interdependence between different banks (largely achieved in the past by the four large public banks holding large stakes in JV banks). The tone for this divestiture exercise has been set by the National Bank of Egypt's (NBE) sale of half of its existing 42 percent stake in the Commercial International Bank — the

---

[17] This refers to the Public Enterprise Law, No. 203 of 1991.

[18] These banks together account for 260 branches nationwide as compared with 830 for the 4 large state banks.

largest and most successful JV bank. This was achieved through the issue of Global Depository Receipts (GDRs) valued at $120 million on the London Stock Exchange in July 1996 — the first such issue for Egypt. The offer was highly successful and has confirmed the attractiveness of portfolio investment in Egypt by foreign investors. A second JV bank, the Egyptian American Bank, was also successfully privatized via a public offering in the same month. In a few other cases, the foreign partners of JV banks decided in principle to buy the state shares of banks which they already partially own.[19]

The liberalization program also established early on a *unified foreign exchange market* as one of its main pillars. This was achieved in 1991 with the establishment of a free foreign exchange market in which banks were allowed to set buying and selling rates free of administrative restrictions. The convertibility of the Egyptian pound on both current and capital accounts was also achieved. The stability of the exchange rate since that date, combined with positive real interest rates, has encouraged significant capital flows which have helped to keep the rate of about £E3.3 to US$1 very stable. Indeed, interventions by the Central Bank have largely been in the direction of buying dollars to prevent nominal appreciation of the Egyptian pound. Partly as a consequence, official reserves rose to a record level of more than $18 billion by 1996.

A final important plank in the overall reform has been the major change in the policy emphasis regarding *state-owned enterprises* (SOEs). Law 203 of 1991 established four main principles for the SOEs:

1. Profit maximization is the primary objective.
2. Subsidies should not be provided to the SOEs either directly via transfers to loss-makers or indirectly via subsidized inputs from suppliers.
3. SOEs should enjoy management autonomy in all decisions pertaining to their operations.
4. Differentiation should not be made in the terms and conditions on which banks grant loans to SOEs relative to other enterprises.

Together these four guiding principles have helped to narrow the gap between the treatment of private and state-owned enterprises. They have been an important push-

[19] Ministry of Economy and Economic Cooperation, *Egypt Economic Profile,* Cairo, 1996, and USAID, Privatization Project, *Monthly Report*, July 1996.

factor behind the improved SOE profitability mentioned earlier. Credit data also show that within an umbrella of generally increasing real volumes of credit, the government's net claims have declined significantly from 54 percent in 1991 to 27 percent in 1996. The data also indicate a corresponding reduction in the share of credit received by SOEs to only about 19 percent. This means that the private sector of the economy is now receiving about half of all credit provided by banks, including an element of household borrowing. This is significant when compared with the average of less than 30 percent for the period between 1990 and 1996. The privatization of SOEs, however, has been one of the slow moving elements of the reform program and only really got underway in 1996. By July of that year, 28 companies[20] — representing about 5.2 percent of the total book value of Law 203 companies — had been majority privatized. A further 17, representing 9.6 percent, had been minority privatized. The total value of the companies that were sold amounts to about £E10.7 billion or about $3.2 billion.

V. A Note of Caution

The financial reforms initiated by the Egyptian authorities in 1991 have undoubtedly been a success. The establishment of much freer markets has been accomplished together with a high degree of control over inflation. The austerity needed at the outset to achieve this has with relative speed given way to resumed growth at a reasonable rate. In the past three years, for example, GDP growth has averaged in excess of 4 percent. Other indicators of success are also quite easy to find. The share of foreign currency deposits in the total money supply has declined markedly: a sign of improved confidence in the Egyptian pound. The Cairo Stock Exchange has increased its market capitalization from about $1.7 billion in 1990 to more than $8 billion in 1995, in spite of P/E ratios which have remained relatively modest at 6-7. The number of companies listed also rose from 570 to 730 during the same period.[21]

There has been considerable foreign interest in Egypt's privatization offerings, most of which have been oversubscribed. There is also evidence of growing interest in Egypt as a location for foreign direct investment (FDI). These developments collectively have started to generate extravagant predictions that Egypt could become not only a

[20] These are enterprises in the economic sectors of industry, agriculture, trade, and services and do not include the banks.

[21] "A Cheap and Cheerful Market," *The Banker,* July 1996.

manufacturing base for the entire Middle East region, but also a major financial center with its stock market among the more important of all the emerging markets.[22]

Although this hyperbole may eventually prove to be justified, it is important to note that Egypt's transformation into a fully open and effective market economy with solid banking and financial sectors is only in its infancy. The maturing of that process faces several difficult hurdles, some of which are assessed in the remainder of this paper. Most of the problems yet to be faced stem from a number of basic facts:

- A dominant part of the country's productive assets still remain under state control, with management attitudes and limitations still reflective of the pre-reform period.
- The country's largest banks are still state-owned and controlled.
- These and other banks still suffer from cultural and technical limitations and bad loans which are a part of the legacy of 30 or more years of illiberality.
- The fiscal adjustment has been achieved without a conclusive resolution of some of the quasi-fiscal problems of the economy, including the overhang of non-performing loans in banks.
- The early measures of liberalization have established behavior patterns in the central bank and other banks that may prove to be a source of future instability.

The approach to addressing some of these problems is quite obvious. For example, further privatization of banks and non-financial enterprises is an obvious prerequisite for the sustainable transformation of Egypt's economy. The outcome lies in the hands of policy makers. It is less obvious how cultural behavior patterns and mind-sets can be changed and how quickly this can happen. The outcome here lies more in the domain of psychology and expectations than in the domain of economic analysis. Nevertheless, experience from other countries indicates that even these cultural/attitudinal changes can occur very fast once the economic policy direction is clearly charted and the likelihood of significant reversals is removed. New banks offering improved and widened standards of service, for example, will rapidly crowd out those resistant to change unless some form of artificial protection

[22] A symbolic step in this direction is the inclusion of Egypt in IFC's emerging markets index.

from competition is provided. The following will focus on the more economically tractable aspects of the problem.

At this point, it is necessary to review some of the main lessons drawn from financial market liberalization episodes in a number of other countries — relying, in particular, on the 1992 Caprio, Atiyas, and Hanson[23] study which focused mainly on six cases (Chile, Indonesia, Korea, Malaysia, New Zealand and Turkey). Four conclusions from this study are worth stressing. First, the "success" of financial reform is difficult to assess definitively. This is partly because the improved allocative efficiency, which theory suggests as one of the main outcomes, will also be affected by numerous other reforms (such as trade liberalization) which countries often pursue simultaneously; and partly because several complete business cycles — reflecting a variety of circumstances in the real economy — are needed to establish definitive judgments about the quality of performance of reformed financial institutions. Neither boom conditions in which even bad banks can do well, nor slump conditions in which even good banks can do poorly, represent adequate contexts for this assessment.

A second and related point is that the evolution of borrower net worth is a crucial determinant of the health of financial intermediaries and their ability to respond to the needs of deficit sectors. Because some aspects of financial reform, such as the elimination of interest subsidies, are certain to impact the borrower's net worth negatively, such a reform is more likely to work well when other influences on net worth are favorable. There are several cases such as Malaysia and Argentina where relatively aggressive financial sector liberalization had to be aborted in the late 1970s because of adverse contextual factors, such as excessively large fiscal deficits. Unfavorable external shocks occurring during an attempted financial reform could have similar negative consequences.

The third point of special relevance to Egypt is that, even if the fiscal deficit as traditionally measured, is not particularly large, financial reform may encounter problems if the initial health of the banking system is poor to the point that it gives rise to contingent claims on the budget. The US Savings and Loan crisis is an example of this point. In that case, banks with low or negative net worth used the opportunity of financial

[23] Atiyas, Uzak, Gerard Caprio and James Hanson, "Financial Reform: Lessons and Strategies," in Shakil Faruqi (ed.), *Financial Sector Reforms in Asian and Latin American Countries*, EDI Seminar Report, 1993.

deregulation to indulge in new and often reckless forms of lending which eventually imposed a huge burden on the US budget. More relevant to Egypt is the point that banks in formerly controlled systems invariably have large investments of informational capital tied up in their relationships with the heavily protected activities of the old system. The diminished value of this capital associated with reform is likely to put pressure on banks to enter new activities where their informational base is much weaker and where some of their involvement is likely to be high risk. Alternatively, it may provoke a sharp reduction in lending as banks attempt to re-tool for the new environment. In either case, the success of reform is likely to depend on the ability of banks to realize that their world has changed and to make investments using the new risk-management and informational approach necessary for their successful adaptation. One lesson which Caprio et al. draw from these separate cases is that it is better for authorities to acquire a deep awareness of the quality and limitations of their country's banking institutions before going too far with deregulation. Reforms that take account of the initial portfolios of banks, their informational capital, and their stage of institutional development are expected to fare better.

A final point is that the ability of countries to maintain effective monetary policy control consistently with financial liberalization has varied greatly. It was quite successful in New Zealand, Indonesia and Malaysia. Caprio et al. argue that this was because all three countries began their reforms after they had already built up highly capable central banks. Increased substitutability among currencies associated with more open capital accounts, and the challenges of abandoning direct methods of monetary control in favor of market-based approaches, require a great deal of flexibility and technical agility from central banks. In the absence of this, and especially if the added complication of still-large fiscal deficits continues (as in the case of Turkey), the problems facing the technical staff of the central bank are likely to be extremely difficult to resolve. The message is that investment in the research and technical capacities of central banks is a crucial pre-condition for successful reform.

The following section considers a number of selected issues focusing more directly on the immediate challenges facing the Egyptian authorities.

VI. Macroeconomic Management and Capital Inflows

Direct and portfolio inflows of the type which Egypt is beginning to experience have great potential for enhancing the speed of economic development. It is possible to realize

this potential by re-enforcing the available domestic savings and by supplying foreign technical, risk-sharing and managerial enhancement to local physical investments. In the 1990s, these types of private flows have overtaken official flows in the global economy to

Box 2. Benefits and Costs of Foreign Investment

Benefits	Possible Dangers
• Additional resources for productive investment	• Currency appreciation
• Risk sharing with the rest of the world (equity)	• Reduced scope for independent macroeconomic policy actions
• Greater external market discipline on macroeconomic policy	• Greater exposure to external shocks
• Enhanced access to technology and management skills (FDI)	• Demands for protection in local markets (FDI)
• Broader access to export markets through foreign partners (FDI)	• Some loss of control of foreign owned domestic industry (FDI)
• Training and broader exposure of national staff (FDI)	• Disruption of national capital markets, asset inflation (FPI)
• Greater liquidity to meet domestic financing needs (FPI)	• Increased volatility in financial and exchange markets (FPI)
• Broadening and deepening of national capital markets (FPI)	• High sterilization costs (FPI)

FDI = Foreign Direct Investment
FPI = Foreign Portfolio Investment

the point where they now account for 80 percent of *net* flows,[24] and many developing countries have seen very considerable benefits. The downside, however, can be dramatic. It is now well understood from the experiences of Southern Cone economies in the late 1970s and more recently from the 1994/95 crisis in Mexico, that the inadequate management of large-scale capital inflows and domestic debt can create enormous

[24] Total net flows to developing countries rose rapidly in the late 1970s and fell sharply in the aftermath of the 1982 debt crisis to only about $70 million by 1985. Nevertheless, by 1994 they had risen again to almost $210 billion per annum with the private share being over three quarters of this total. By contrast with the 1970s, only a small part of this private flow is now attributable directly to lending by commercial banks.

instability and dangers for sustained economic development. A recent study of the East Asian experience in this regard provides a useful catalogue of the main benefits and costs of large-scale inflows as a framework for subsequent discussion (see Box 2).

In most cases, the larger the part of foreign capital inflows directed or encouraged into increased productive investments, rather than into portfolio investments, the greater the benefit (the cost ratio of foreign capital inflows). In Egypt, this is particularly important given low domestic savings rates and the huge annual investments needed to sustain the growth of jobs for 500,000 new entrants yearly to the labor market. In a market economy, however, this direction of capital flows requires a difficult balancing of fiscal and monetary policies.

The active use of monetary policies on a sustained basis is of limited use in this regard. The relatively high domestic interest rates needed in an economy transiting from high inflation, especially where an effort is made to sterilize capital inflows, can easily produce a damaging combination of expensive money and overvalued exchange rates. This can be very attractive to foreign portfolio investment but extremely damaging to the real productive investments upon which economic growth and the attraction of FDI depends. This will be especially true where the liberalization of trade and other commodity markets necessary for the effective use of FDI proceeds lethargically. At the same time, as Egypt's post-reform experience shows, an active sterilization policy can rapidly build up a large domestic public debt (this rose from less than 30 percent of total public debt in 1990 to over 50 percent by 1993) which, beyond a certain point, will cast doubt on the sustainability of reform.

Sterilization has to a certain extent been a sound strategy for Egypt. But the arithmetic of a negative margin (interest paid on Treasury Bills exceeding earnings on reserves) is obviously against continued sterilization of large inflows. The fiscal cost on inflows of $2.5 billion, for example (larger than in the recent past but not beyond the bounds of near-term possibilities), would be of the order of $100 million a year. Part of the solution to this obvious dilemma would be to intensify the existing strategy of promoting strategic privatization to attract larger volumes of direct foreign investment – a strategy which could provide benefits in terms of both fiscal and export performance which are not associated so directly with portfolio flows.

Tight fiscal policy, and hopefully a significant public savings surplus, provides a conceptually better approach in that it removes some of the demand pressure on domestic

resources and permits lower interest rates, thereby lessening the pull of short-term portfolio inflows. In Egypt, however, where many of the obvious cuts in public expenditure have already been made, important structural changes are also necessary to sustain positive public savings in the longer term. In particular, the pace at which the state divests itself of loss-making as well as profitable state enterprises will need to increase. Privatization revenues will need to be increasingly assigned to reducing government debt rather than to supporting lame duck enterprises. The use of public savings to finance large infrastructural investments which the economy still needs will also need to be assessed critically to determine whether more private initiatives and financing would not provide for greater efficiency.[25] These are changes which would seem to go a long way beyond the rather hesitant privatization initiatives observed thus far.

VII. Bank Regulation and Capital Flows

A highly socialized and directed banking system did not need intensive or sophisticated supervision of banks. Good book-keeping skills were all that were required to ensure that banks did what was asked of them. Likewise, the emphasis of the banking regulatory system in that environment was on bank compliance with well-defined structures of assets and regulatory ratios rather than on their competence to assess business risks and the general performance of their borrowers and other clients. By all accounts, considerable progress has been achieved in the past few years in building a more market-oriented system of bank regulation and supervision in Egypt, including the introduction of loan classification and loan-loss provisioning systems. Nevertheless, casual evidence suggests that this task is not currently assigned the high priority which is needed to minimize the danger of a banking crisis and the derailing of the economic stability achieved since 1991. In this regard, analogies between the former Soviet Union (FSU) and Egypt are disturbingly close.

The FSU and probably the Egyptian authorities have been reluctant to dispense with state-owned and even formerly state-owned banks as agents of quasi-fiscal policies. In particular, banks have continued to be regarded as a convenient way to direct credit (emissions) to particular state enterprises unable to raise resources in any other way. As the *quid pro quo* for this non-commercial lending, those same banks have often

benefited from the sluggish enforcement of prudential rules and especially from the delayed application of full International Accounting Standards (IAS) practices, including full loan loss provisioning. The result has been that many FSU banks continue to publish results

[25] At present, about 40 percent of total domestic investment is contributed by the public sector. This total in turn represents almost 7 percent of Gross Domestic Income.

showing levels of profits and capitalization which are misleadingly high. Also, and more importantly, they continue to pay high taxes and dividends on the basis of fictitious profits, thereby damaging their capitalization levels even further. The high profitability of some Egyptian banks in recent years may also be explained in part in this manner.

One of the consequences of avoiding serious inflation instability in the pre-reform period, and of the further increase in magnetization thereafter, is that the levels of total banking sector assets in Egypt are large relative to the size of the economy—and certainly much larger than in most FSU countries. It follows that the economic and fiscal costs of a major banking crisis, involving 20 percent or more of banking sector assets, would also be large and certainly sufficient to undermine the credibility of Egypt's newly established fiscal stringency. It is therefore indisputable that a major effort needs to be made first to identify the factors most likely to trigger a serious crisis, and second to take supervisory and other steps to avoid them.

First on the agenda should be a concerted program to introduce full IAS accounting practices in all Egypt's banks and to enforce compliance with these new standards – first through the training of bank staff and second through intensified supervisory vigilance. In the short term, while this program is being implemented, all the major banks and especially the large state-owned banks should undergo intensive IAS audits, including portfolio and management reviews, by internationally recognized audit firms. The portfolio reviews should establish best estimates of the loans that need to be classified in the "loss" or "doubtful" categories. The management reviews should establish, as far as possible, whether the managerial or political errors which caused the accumulation of a *stock* of bad loans in the past are continuing in such a manner as to add a significant *flow* element to that stock. This exercise will at least give the authorities a better indication of the scale and nature of the problems which they face and provide the basis needed to define alternative strategies to resolve these problems.

This action needs the support of a concerted effort to persuade banks to actually make the required level of provisions in their accounts, to mark down profits accordingly, and generally to reveal their true financial positions. The experience of banking systems, which are not accustomed to provisioning their portfolios, suggests that a relatively

generous tax treatment of provisions is perhaps necessary to achieve this.[26] The revenue authorities will undoubtedly resist the short-term loss of revenue and may receive political support from others who see banks as inevitably profitable. This revenue loss, however, should be regarded as the price to pay to avoid probably much larger budgetary outlays at a later date. Taxing the fictitious profits of banks in the short term, only to pay out the same money and more at a later date to help rebuild the capital of failed banks, serves no purpose.

The second main action relates to a new but critically important concern for the regulatory authorities in the new Egyptian environment of liberal capital accounts. This aspect of liberalization has made it easy and currently profitable for banks to raise borrowed funds from foreign sources and to lend them at significantly higher rates now available locally.[27] This profit margin depends on the continuation of a relatively stable nominal exchange rate. But should this condition be breached, the banks could be seriously exposed to losses caused by exchange rate devaluation. As a minimum, bank supervisors need to ensure that the banks themselves do not build up significant unmatched (open) foreign exchange positions – something which inexperienced foreign exchange banks may well be tempted to do. But even if the banks themselves are controlled in this way, their vulnerability to a devaluation could still be severe if their borrowers themselves maintain unmatched positions. In this case, the failure of some borrowing enterprises to meet their repayment obligations, as caused by a devaluation of the Egyptian pound, would have a domino effect on the banks, thereby provoking their own distress.

This is one area where Egypt may have most to learn from the experience of the 1994/95 Mexican crisis. With the benefit of hindsight, it seems that Mexican authorities placed excessive confidence in the proposition that the dominance of the private element in the huge capital flows received after 1990,[28] combined with a greatly strengthened

---

[26] Two FSU countries, the Ukraine and Armenia, vividly illustrate this point. In Armenia where loan loss provisions with generous tax deductibility were introduced early in 1996, the banks on average had achieved 50 percent provisioning for their very high level of classified loans by the end of the year. In the Ukraine, by contrast, where loan loss provisioning — but without tax deductibility — has been in force for about the same time, only about 2 percent of the classified loans of the major banks are currently provisioned.

[27] For example, since 1992, there has been a differential in favour of domestic rates of between 5 and 12 percentage points.

[28] Those expressing confidence drew a contrast with the inflows after 1990 and inflows prior to the 1982 crisis, where the bulk of the borrowing was by, or linked to, the public sector.

bank supervision process, could insulate the budget from the effects of a reversal of the flows. In reality, the large official support to distressed banks in 1994 is arguably an important ingredient of the Mexican crisis which occurred later in that same year.[29] The lesson to learn is that loan classification has to be done with considerable care and be based on the repayment capacity of borrowers, including any downside risks associated with over-exposure to foreign currency borrowings.

In both these and other related areas of strengthened bank supervision, the legacy of relatively limited banking skills will most likely compromise the probability of success. The Central Bank of Egypt cannot expect to confront a universe of sophisticated bankers, fully aware of the justification for regulatory tightening of the type just described. An intensive educational campaign should therefore be an important part of the overall strategy, though one or more major bank failures may unfortunately occur as part of that educational process.

VIII. Capital Inflows and Domestic Debt

The effort of the Egyptian authorities to sterilize capital inflows after 1992 resulted in a significant increase in outstanding domestic debt and in its share of total public debt. World Bank data indicate a total stock of debt at the end of 1995 equivalent to about 80 percent of GDP, two-thirds (or 50 percent of GDP compared with 37 percent in 1992) of which was accounted for by domestic debt, and the balance by external debt, adjusted for its high concessional element. The composition and growth of the main components of this debt are shown in Table 1. This level of debt is not alarming in itself but obvious dangers exist which must be monitored in designing the next stages of policy.

The first danger is that the accumulation of domestic debt is to a large extent the mirror image of capital inflows and the large accumulation of official reserves which has occurred during the same period. But, in the light of the interest differentials which have prevailed since 1992, this method of adding to reserves is fiscally expensive: the yield on the reserves being much less than the interest rate on domestic borrowing.

[29] Views expressed by Guillermo Ortiz at an Economic Development Institute seminar are summarized in Roe (1994, p. 22) as follows: “Ortiz argued that because so much of the corporate borrowing of the country was now done using the companies’ own paper rather than borrowing through the banks, some of the earlier risks of external borrowing had been lessened. More specifically, he saw no particular reason why the commercial banks should bail out industrial companies that found themselves in difficulties because of international funds being withdrawn or drying up. Thus the government too was insulated to some extent from the likelihood of turning implicit guarantees to banks into explicit payments if difficulties emerge in the private sector.”

Table 1. Egypt's Domestic Government Debt, 1987-1996 (£E billion)

	1987/88	1995/96	% Increase
Treasury Bonds, Bills and Loans	23.6	78.5	232.6
National Investment Bank	11.2	44.6	298.2
Energy Bonds	0.7	5.1	628.6
Social Insurance Fund Bonds	3.0	3.0	0
Total Domestic Government Debt	38.5	131.2	240.8
Total in $ billion	11.7	39.8	–

Source: Ministry of Finance

Depending on the part of the domestic debt which is associated with sterilization, the fiscal cost could be between 1 and 2 percent of GDP. Therefore, with targets for the overall deficit now at only about 1 percent of GDP, there are clearly fiscal constraints on the amount of further sterilization which is possible. As noted earlier, the strategic escape
from this serious dilemma could lie in some early reconfiguration of inflows to give more prominence to direct rather than portfolio flows.

A second danger arises from the fact that it is difficult to know how much of the capital flows which have been sterilized are true autonomous flows motivated by Egypt's
improved fundamentals and how much they are merely induced on a fragile temporary basis by the favorable interest differential. Michael Dooley, in commenting on the possible causes of the large inflows into Mexico in the early 1990s, identified three possible explanations of the large capital account surplus, which at the time were equal to 8 percent of GDP. The first was a significant improvement in the fundamentals of growth and inflation in the recipient country. The second was a speculative bubble whereby mainly poorly informed private investors were playing a follow-the-leader type of strategy based only peripherally, if at all, on economic fundamentals. The third, which he argued from the vantage point of February 1993 and which was the most credible, was that the monetary authorities themselves, via their interest and exchange rate policies, were creating arbitrage opportunities. Foreign investors were more than happy to exploit these opportunities until the implicit guarantees underpinning them (high interest rates and a stable or appreciating currency) were removed. It is this last possibility above all

that the Egyptian authorities need to be aware of since capital flows motivated in this way are almost certain to suffer a rapid reversal at some future date.

A third point is that the arithmetic of debt dynamics indicates quite a number of ways in which the present debt ratio (debt/GDP) might rise even if there is no further sterilization of inflows. One way would be if the authorities conducted their monetary policies in such a manner that nominal interest rates on domestic borrowings rose above the long-term growth rate of the economy. This is something that could even happen by accident in a system such as Egypt's where much of the debt is short term, where the authorities are relatively unused to indirect methods of monetary control and, by all accounts, are also poorly supplied with the timely information flows needed to use these methods with precision. Were this to happen, the overall deficit could rise quite fast, even if the primary deficit stayed low. This in turn may likely bring renewed pressures to monetize the deficit to avoid further build up of debt, thereby rapidly reversing the credibility of the authorities. Furthermore, there is considerable ambiguity about Egypt's prospects for accelerating its growth rate above the relatively modest levels of the early 1990s. While there is much euphoria about the successes achieved, even senior officials acknowledge that "there is not yet a tiger on the Nile."

Growth in the region of 7-8 percent per annum will certainly need a more successful and diversified export performance. But this in turn will require substantially higher investment, with much of it financed through large increases in the domestic savings rate. An economy buoyed up on high levels of foreign portfolio inflows and a strong exchange rate does not create much of an incentive either for increased savings or for increased export activity. The obvious danger is that the inflows lead to excessive consumption and to a debt burden which is excessive in relation to the country's export earning capabilities.

Another way in which the debt situation could get out of hand would be if the primary budget deficit needed to rise quite rapidly to deal with the resolution of an, as yet, unrecognized fiscal obligation. The main trigger of this new obligation could be an enforced recapitalization of some of the large state banks in response to a banking crisis. Even a once-for-all shock such as this could add substantially to the total stock of debt. Third, with a large amount of domestic debt held by foreigners, a banking crisis or an external shock, including possible adverse developments in Middle East politics, could cause problems in refinancing maturing issues and, again, pressure to monetize deficits.

These concerns have important institutional and technical implications of which only a few are mentioned here. The overriding one is that the Central Bank must move rapidly to improve its monitoring and intervention skills to achieve a very high level of competence.
The information flows which alert it to all the non-discretionary influences on reserve money (for example, net receipts and payments through the government's own accounts, including operations in securities and non-intervention transactions in foreign exchange) need to be absolutely first rate and extremely prompt in their availability. In particular, the obfuscation which often accompanies the likely fiscal costs of bank rescues and other quasi-fiscal interventions needs to be kept to a minimum — the monetary surprises contributing to Mexico's 1994 crisis partly arose from failure in this department. Second, the Central Bank needs to have real control over the supposed "discretionary" elements of the monetary base (for example, central bank discounting of bank loans, short-term money market interventions, and the amounts and terms of lending to the government).

Third, the considerable complexity of money management in the more open environment in which Egypt has now chosen to operate needs the guidance of very clear and unambiguous policy targets supported by a great deal of serious economic and econometric analysis. Different economic objectives which figure prominently in the statements of leading policy makers, however legitimate, give rise to serious ambiguities about the correct stance of monetary policies. For example, the call for intensified export earnings requires some relaxation of monetary policy to prompt a more competitive exchange rate, while the call for continued diligence regarding inflation requires the opposite. The improved investment target calls for easier money to generate somewhat lower real interest rates, while the need for improved savings calls for the opposite. All of these complexities are further overlaid by the need for great diligence in the management of external debt and the close link, already discussed above, between the build up of debt and the rate of economic growth.

Economic management for the next few years will be very difficult since it needs to factor in major structural changes (the full impacts of which are inevitably difficult to foresee) and needs to be conducted in an institutional environment of financial markets which is still being shaped. This management, however, calls for a greatly enhanced capacity for analysis so that the nature of these numerous trade-offs can be fully documented and incorporated into decision making. It also calls for decision-making

procedures that lead to resolute and largely unambiguous judgments about the specific policy targets which should be prioritized and how policy levers should be used to achieve these targets. Multiple and possibly inconsistent objectives can be very dangerous when a country is beginning to rely, as Egypt is, on something as capricious as international capital movements.

IX. Conclusion

Egyptian authorities have made an impressive start in liberalizing the country's financial sector and thereby undoing more than three decades of generally interventionist policies. The fundamental building blocks of this liberalization seem to have been well laid. They include the reduced fiscal deficit, the unification and freeing of the exchange rate, the freeing of interest rates and lending decisions from administrative control, and the initial privatization of large banks which has removed some of the extensive ownership links between banks — one likely cause of uncompetitive banking.

The benefits of this reform program are also beginning to show. Inflation control has been achieved consistently with growth rates since 1992, which have been strong if not spectacular. There is also an obvious improvement in confidence in the local currency. Stock market activity, supported by a number of prominent privatizations, has been quite buoyant. Capital flows into the economy have also been much stronger than in the past. As this paper, however, has endeavored to point out, the transformation of the Egyptian financial sector into a modern market-oriented system is still in its infancy. Egypt still diverges considerably in its main characteristics from the booming economies found in East Asia and in a few other developing economies. Its savings rate at only about 11 percent of GDP is much lower. The deficit between domestic savings and domestic investment is large. And, official development assistance is still large relative to private FDI and other capital flows. Moreover, as a brief review of other country experiences shows, there is no smooth linear transition from the current financial system to the larger and deeper system which a modern market-oriented economy needs. The economic changes which policy can influence should go hand in hand with institutional and attitudinal changes which are potentially much more difficult to bring about. Policy makers must continue to work hard to build on the foundations they have laid thus far.

This paper has stressed just a few of the problems policy makers will face. First, the new opportunities associated with capital inflows need to be managed carefully to ensure that these flows find their way into productive investment and do not become the cause of some future macroeconomic instability, as was the case in Mexico. In particular, the present dominance of portfolio flows over direct investment flows should be regarded as desirable only in the short term and as needing reversal in the medium and longer term. Policies such as privatization need to be motivated in this light. This requires a careful and technically difficult balancing of monetary and fiscal policies and some reassessment of the structural role of the public sector in the economy.

Second, there has to be a realistic assessment and management of the broad fiscal situation, including contingent government liabilities hidden for the moment in large unrevealed bad loans in some major banks. Higher priority should be given to the Central Bank's accounting, reporting, and supervision of commercial banks and to an enhanced sophistication of the techniques of supervision which it employs.

Third, the domestic debt of the economy has now assumed a much greater quantitative importance and will need to be managed somewhat differently if the fiscal costs of this debt are to be kept in reasonable bounds, and the risks of uncontrollable debt growth avoided. Fourth, the role of technical economic analysis and the institutions which provide it must take on a completely different and greater role in the more open environment which Egypt has now chosen.

There is finally the over-arching problems associated with the continued large dependence of the productive economy on state enterprises, many of which are unprofitable as well as economically inefficient. Their privatization may be difficult and their liquidation even more difficult, but their continued support either by direct fiscal transfers or through "soft" lending by banks will be wholly counterproductive, and will undermine sound solutions to other problems. Their restructuring should therefore appear high on the agenda in the next stages of financial sector liberalization if the high hopes for this process are to be realized.

References

Adams, Dale (1991), "Taking a Fresh Look at Informal Finance," in Philippe Callier (ed.), *Financial Systems and Development in Africa*, EDI Seminar Series, World Bank, Washington, D.C.

Atiyas, Izak, Gerard Caprio and James Hanson (1993), "Financial Reform: Lessons and Strategies," in Shakil Faruqi, (ed.) *Financial Sector Reforms in Asian and Latin American Countries*, EDI Seminar Report.

Financial Times (1996), "A Cheap and Cheerful Market," *The Banker*, July.

Giugale, M.M. and H. Mobarak (1995), *Private Sector Development in Egypt*, The American University in Cairo Press, Ch. 7.

Hanson, J.A., and C. Neal (1984), "A Review of Interest Rate Policy in Selected Developing Countries, 1970-1982," *World Bank Research Report, No. 5391*, World Bank, Washington D.C.

Mathieson, D.J. and R. McKinnon (1981), "How to Manage a Repressed Economy," *Princeton Papers in International Finance*.

Ministry of Economy and International Cooperation (1996), *Egypt Economic Profile*, Cairo.

Mohieldin, Mahmoud (1995), "Causes, Measures and Impact of State Intervention in the Financial Sector: The Egyptian Experience," paper presented at the conference on The Changing Role of the State in Economic Development and Growth, Rabat, Morocco, January.

Ortiz, Guillermo (1994), as quoted in Alan R. Roe "Seminar Proceedings: A Summary," in Shakil Faruqi (ed.), *Financial Sector Reforms, Economic Growth and Stability*, EDI Seminar Report.

Roe, Alan (1979), "Some Theory Concerning the Role and Failings of Financial Intermediation in Developing Countries," in V.V. Bhatt (ed.), *Capital Market Imperfections and Economic Development*, World Bank, Washington D.C.

Sochen, Peter (1996), "The Banking System in Ukraine," Center for Social and Economic Research, *Studies and Analysis Paper No. 65*, Warsaw, March.

USAID (1996), "Privatization Project," *Monthly Report*, July.

World Bank (1993), "The East Asian Miracle: Economic Growth and Public Policy," *Policy Research Report*, World Bank, Washington D.C., July.

World Bank (1993), "Egypt, Financial Policy for Adjustment and Growth," *Report No. 10790 GT*, World Bank, Washington D.C., September.