MEDA PROJECT

Microfinance at the University
University of Torino

Case study

"The involvement of commercial banks in microfinance: the Egyptian experience"

Chiara Segrado
August 2005

The author would like to thank: Professor Sergio Bortolani, Dr. Akmal Y. Bassili, Mr Hassan El – Shabrawishi, Mr. Magdy Moussa, Ms Miranda Beshara, Mr Karim Fanous, Dr Angelo Cicogna, Professor Abdel Rahim Mubarak Hashem, Mr Amro Abouesh, Mr Kamel Shehata Sallam, Mr Youssef Assad

Table of contents

List of acronyms: 3

1. Introduction **4**

2. Downscaling: a definition **9**

3. Overview of the financial and microfinancial activities in Egypt. Commercial banks involved in microcredit. 10

4. Banque du Caire: 15

4.1 General information 15

4.1.1. Background: why did the bank choose to be involved in microfinance? 15

5. Banque Misr 17

5.1 General information 17

5.2 Outreach 19

5.3 Financial sustainability 19

5. Future perspectives 20

6. References 25

List of acronyms:

ABA Alexandria Business Association

CGAP The Consultative Group to Assist the Poor

CIB Commercial International Bank of Egypt

DAG Donor Assistance Group

EBI Egyptian Banking Institute

IMF International Monetary Found

MFI microfinance institution

NBD National Bank for Development

NGO Non Governmental Organization

PBDAC Principal Bank for Development and Agricultural Credit

SME Small and Medium Enterprise

SFD Social Fund for Development

1. Introduction

Despite the general impression, poor people need financial services. This idea constitutes the basis of the “microfinance revolution”. Poverty is a broad concept and poor are not a homogeneous group of people. This is why it is quite clear that microfinance cannot be used as an effective tool to fight poverty at any level. Microfinance is not a panacea, but at a certain stage of poverty it is likely to be one of the most effective tools to help poor people in a self development perspective. In any case, in order to meet their needs the poor refer to a wide range of financial services, most of all composed by informal networks such as moneylenders, savings and credits clubs and mutual insurance societies, and as savings to be utilized when any need arises, animals, buildings or small amounts of cash.

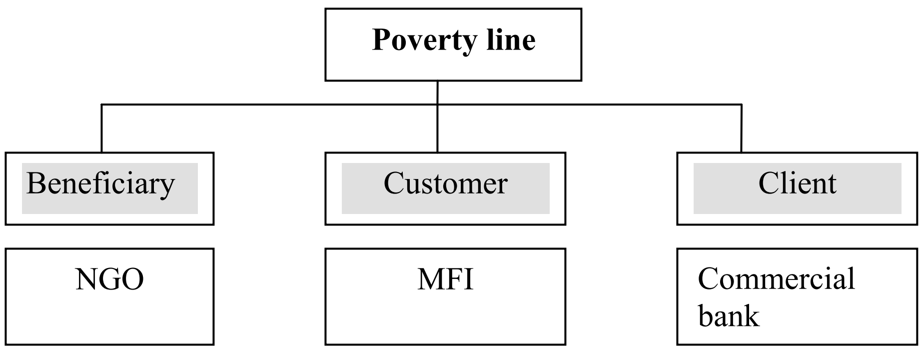
This is one of the reasons why the main target of microfinance is generally constituted by microentrepreneurs, those who are already setting some tools and acquiring some skill to move out of a situation of poverty. Very poor people, malnourished, ill and unskilled individuals cannot be a target for microfinance, simply because this intervention would not be efficient to solve their problems. They need, first of all, to be fed, cured and trained, because they need to meet their basic needs, before concentrating on establishing an income generating activity. As Robinson stated: “ For these people microfinance is the next step – after they are able to work”[1]

Regarding the Egyptian context, in year 2004 local microfinance practitioners, governmental and donor representatives and international organizations started a vast work finalized at building a new strategy for the country. Monthly meetings, travels abroad and drafting of papers constituted a path that led to a definition on what Egypt needs in terms of microfinancial products to poor people and microenterpreneurs.
So far, this constitutes the starting point for all those who are willing to investigate microfinance in the country.
One of the most interesting issues that rose from this work was the major role of commercial banks in the commercialization, seen as a process to be sought after in microfinance in order to achieve exponential growth and the diffusion of a complete range of products in this field. Poor people, in fact, do not necessitate only of credit services to meet their financial needs: they also require savings, insurance, money transfers, leasing and so on, along with non financial services such as technical assistance.

[1] Robinson M.S. “ The Microfinance Revolution, Vol. 1, Sustainable Finance for the Poor” Washington DC 2001

So, what are the missing chances for growth for customers and institutions in Egypt? This paper will try to answer this question, analyzing the services provided to those who are targeted by microfinance institutions: beneficiaries and clients.
The starting point for this analysis is that there are different varieties of customers as well as institutions that offer microfinance and as well as products offered.

The classification of the customers could be placed in a continuum, whose central point is the poverty line[2].



At the left side, it is possible to place the beneficiaries of broader development interventions, that together with food aid, water and sanitation, gender programs and so on, also include a microcredit component. Usually these interventions are provided by

[2] According to the American University in Cairo, poverty incidence in Egypt under the lower poverty line has increased from 17.1% in 1981/82 to 24.2% in 1990/91 then decreased to 22.9% in 1995/96 and finally to 16.7% in 99/2000, which means that 10.7 million individuals are unable to meet their basic food and non-food needs, compared to 7.3 million in 1981/82, at an increasing rate of 2.15% annually.
The number decreased over the period (1990/91-99/2000) at –2% annually. Using the upper poverty line, the number increases to 26.9 million compared to 12.9 million in 81/82, 20.7 million in 90/91, at an annual increasing rate 4.2% over the period (81/82-99/2000) and 3% during (90/91-99/2000), which is higher than the population growth rates during those two periods: 2.25% and 2.1% annually.

NGO, and provide a more holistic assistance to the beneficiary, rather than focusing on financial services only. The beneficiaries at this stage need to acquire awareness both on what their rights are and on what they need together with some skills (for example, a clear definition of credit and saving).

At the middle of the continuum, it is possible to place those who live slightly under or above the poverty line, who are well aware of what they need (also in financial terms) but have no access to a system that could meet their necessities. Usually they are (or constitute potential) microentrepreneurs. They can better be served by MFIs who are specialized in small and micro enterprises development, and usually give financial services as well as technical assistance.

At the very right side of the continuum, it is possible to place those who have higher awareness, and different needs. They could be small entrepreneurs who might be interested in leasing to buy machinery or insurance for their crops. In this case, they can be considered clients and easily approached by commercial banks, who have the expertise to handle individuals with a higher financial maturity.

The growth of the customer, from beneficiary to client, in which he/she acquires more awareness but also economic power, should be followed by a growth in the way institutions serve their needs. Institutions, from NGOs to banks, have to start their activities by focusing on their target's needs: deprived people need broad interventions, food, water and good health, a house and so on. NGOs are the perfect subjects to give these services, together with microfinance, when needed. Microenterpreneurs need capital and other financial services. MFIs can better serve them, and the range of people who live on the edge of the poverty line. Micro and small entrepreneurs deserve and require more sophisticated products that can be easily provided by banks and other financial institutions who already offer them to their traditional clients.
This distinction tends to constitute a scheme and a theoretic exercise: of course there are and there have to be many points of intersection between the three providers. Anyway, it tends to prove that:

- People, even when poor, deserve and demand tailored services
- Specialization is important to better serve the clients. Institutions cannot handle all the effective and potential clients of microfinance, also because they are very heterogeneous.
- Diversification of the products is essential to cover the needs
- Competition can be a good incentive to improve each institution's performance but all of them should concentrate on communication and cooperation with other institutions who are specialized in different areas, not neglecting the points of intersection that could represent a good

opportunity of enrichment and a positive experience of growth through sharing.

In this context, commercial banks in Egypt showed interest in being involved in the process of disbursing microloans and other financial services to people that are traditionally considered *non bankable* because they are not able to provide collaterals when requiring credit for their activities. These banks understood the value of social capital and its role as collateral. Traditionally, microcredit is related with group lending where *peer pressure* works as a mean to assure that the capital (plus interest) will be repaid. In Egypt individual lending works better than group lending and usually banks prefer the first approach. For them, social capital constitutes a form of guaranteeing their loans, especially in a society where community life still is so important.

As Littlefield and Rosenberg[3] observed, "the general picture so far has been that financial services for the poor, despite their extensive outreach and promising new developments, suffer from being fragmented in niche institutions that are not well-integrated into the mainstream financial system".
Anyhow, although commercial banks are in a perfect position to extend financial services to microfinance clients, especially for their competitive advantages, such as broad networks and easier access to financing, they still prove to be reluctant to lend to microentrepreneurs.

Many reasons lead to this attitude, such as:

a. **High costs and small profits** associated with small loans.
b. The perceived **high risk** associated with microlending.
c. Inadequacy of the present methodologies used to assess the creditworthiness of their clients adopted by banks. For this reason, the creation of effective **credit bureaus**[4] is highly auspicated in the country.
d. **The banks' lack of marketing, appraisal and supervision capacity for microenterprises lending**. For four decades, until the mid-nineties, the banking

[3] Littlefield E., Rosenberg R. "Microfinance and the Poor:Breaking Down the Walls between Microfinance and the Formal Financial System" *Finance & Development* 41, no. 2 (June 2004), 38 - 40
[4] "A **credit bureau** is a data bank/repository of individuals' demographic records and payment history of various types of credit obligations, both open and paid. It also contains payment history of credit obligations on SMEs. The credit information reflects both good and poor repayment habits. A Credit Bureau does not assign credit ratings to the credit records of individuals nor does it decide an individual's credit worthiness – this is left to the user of the information. The rating of credit data is supplied by the company that has extended credit to individuals and subsequently provides the information to the credit bureau." Definition given by EBI, Egyptian Banking Institute. As one of the concerns that impede the full involvement of commercial banks in microfinance is the lack of information of the credit history of potential clients, a loan register would provide the information required by the financial institution allowing it to manage in a better way the risk exposure of their portfolios.

sector was working under a system of credit allocation that favored large public sector enterprises. As a result, banks have developed no marketing, appraisal or supervision capacity to lend to smaller clients. At present, anyway, the liberalization of the banking sector is introducing these new skills, still centered around larger institutions.

e. **Inadequacy of current lending terms and conditions for small business lending**, especially because these businesses are obliged to establish credibility for borrowing under the currently prevailing, and inadequate, credit evaluation criteria.

f. The inadequacy of collateral – based lending techniques for the SME market. At this point it is very important to underline that most of the times collateral is not lacking: the problem dos not lie in the physical absence of guarantee. Rather, the problem lies in its official invisibility, given to the fact that holdings possessed by the majority of potential micro clients are not registered so they cannot prove the ownership or use them as a collateral in any case[5].

As the financial services sector becomes increasingly competitive anyway, banks feel the pressure to move downscale, also because this constitutes the access to a market niche in which they could acquire new and loyal clients but also because of the proven profitability of the business[6].

Commercial banks can be involved in microfinance both indirectly and directly.
In the first case, the can offer:

- Technical support to an MFI or NGO
- Refinancing of an MFI
- Participation in the MFI's equity

Otherwise, they can:

- Create *ad hoc* products and services for a targeted clientele usually considered a prerogative of NGOs
- Create branches or windows dedicated to microfinance

---

[5] This concept has been broadly tackled by Hernando De Soto in his book called "The Mystery of Capital"

[6] International experience proved that the involvement of commercial banks in microfinance can be very successful (for example: Equity Building Society in Kenya, State Bank of India and ICICI Bank, Ag Bank in Mongolia, ABN AMRO in the Netherlands and also the world's largest bank, Citigroup.

1. Downscaling: a definition

The word *downscaling* expresses the involvement of commercial banks in microfinance, which implies reducing the volume of their affaires by opening to a new even if more risky market niche: poor people and microentrepreneurs. Starting from the assumption that microfinance is a development tool which is very effective to fight poverty but cannot address the poorest of the poor and be utilized in cases of extreme poverty, it is possible to find some intersection between the clients usually served by MFIs and those served by traditional banks, who broaden their market and at the same time offer new products.

Downscaling can be seen as a way to commercialize microfinance, together with commercial investing and transformation[7]. Following this distinction, three definitions occur:

- **Downscaling**: a bank or other formal financial institution expands its services to work with clients traditionally served by MFIs. Such an expansion can mean serving microfinance clients in one or many financial areas.
- **Commercial investing**: driven primarily by the promise of financial returns, private funds are placed into institutions already profiting from microfinance. Funds may be invested in MFIs directly or through an intermediary
- **Transformation (**or **upgrading):** an NGO or socially motivated MFI changes its organizational and legal structure to become self-sufficient and profit driven.

To reach these objectives, commercial banks need sound macroeconomic policies and an appropriate regulatory and prudential framework, very important because it an effective management. They also need reliable credit information on microentrepreneurs, for example information on past payment history, level of indebtedness, and default information (this is one of the reasons why, as stated before, credit bureaus are acquiring such a huge importance). A third prerequisite is a better understanding of the markets in which microentrepreneurs operate. Commercial banks need, for example, primary and secondary market researches on the types and size of businesses run by microentrepreneurs and the characteristics of the industries they work in. In any case, it is fundamental to underline that commercialization can be considered both as a process to be sought after in microfinance in order to achieve exponential growth and as a mean that fosters greatest competition, allows an extension in the range of products and services offered, innovates methodologies and the lowers the costs. This is why it is viewed as a tool to promote sustainable operations while providing a larger number of people with access to better financial services.

---

[7] Siddartha H. Chowdri "Downscaling Institutions and Competitive Microfinance Markets: Reflections and Case – Studies from Latin America", August 2004 Edited by Alex Silva, Omtrix Inc., Commissioned by CALMEADOW

3. Overview of the financial and microfinancial activities in Egypt. Commercial banks involved in microcredit.

Total population	**66,372,000**
Estimated number of people below the poverty line	**28,540,000**
Estimated number of households below the poverty line	**4,077,137**
Estimated number of households needing access to credit – market potential	**1,630,855**
Number of active borrowers	**256,159**
Percentage of people currently having access as percentage of market potential	**16%**
Market gap in numbers	**1,374,696**
Market gap in percentage	**84%**

Source: Microfinance in the Arab States Building inclusive financial sectors UNCDF, 2004

The banking sector in Egypt consists of a Central Bank, large public sector banks and a number of joint ventures and private commercial banks. The Central Bank of Egypt (Bank al-Markazy al-Misry), established in 1960, is an autonomous public legal entity. Among the bank's responsibilities are issuing banknotes, formulating monetary policy, maintaining the stability of the Egyptian pound, managing state gold reserves, controlling banks and managing the government's debt. Egypt's inflation, having reached a high of 21.2% in 1990, diminished to 3.8% in 1999 and has remained at that level, with 4.2% inflation in 2002.

During the 1981 – 1991 decade, Egypt faced a phase of economic reforms, characterized by an attempt to create more financial intermediation. Even so, during this period the state – owned banks dominated the financial sector in Egypt (see Arestis, 2003). In 1991 the country embarked on structural adjustment programs following the World Bank and IMF prescriptions as well as financial reforms. From 1996, the reforms focused on privatization, deregulation, foreign trade and prices liberalization. At the same, a special structure called **Social Fund for Development** was created to mitigate the effects of these reforms.

The Central Bank during the last years approved further reforms of the banking sector, including privatization of the public sector banks and mergers of some of the smaller banks. Egyptian banks are regulated by the new law n. 88 of 2003. At the moment, the **National Bank of Egypt** and **Banque Misr** are the public banks that dominate the commercial banking system. Together with the **Banque du Caire** and the **Bank of Alexandria**, Egypt's other two leading public sector banks, they control well over half of the total assets of the banking system. Since 1976 anyway, a large number of joint ventures and privately owned commercial banks compete in the market. Among them, are the Commercial International Bank of Egypt (CIB), the Egyptian American Bank, the Misr International Bank, the Suez Canal Bank, and the Cairo-Amman Bank. The Arab African International Bank and Arab International Bank are Arab multinational banks, and Faisal Islamic Bank of Egypt is the country's largest Islamic bank. Some 21 foreign banks, such as CitiBank Egypt and Arab Bank (Amman), have been allowed, since 1992, to offer full ranges of commercial banking services in local as well as in foreign exchange. The Egyptian banking system has the infrastructure and capacity to reach thousands of potential borrowers – together these 64 banks have 2.325 branches. (Dhumale, Sapcanin and Tuker, 1999)

Since 2001 anyway, a number of banking scandals have come to light, mostly involving bad loans to influential businessmen and officials. As of 2003, each of these cases has been prosecuted and heavy sentences have been handed down for those convicted. Loan defaults between 1999 and 2003 are estimated to have cost the banking system between US$ 8 and 10 billion, or 10% of GDP annually. Banque du Caire was particularly hard hit, and as of 2003 carries US$ 1.3 billion in non-performing loans[8].

Microfinance arises as a sector in which commercial banks can be involved in supporting poor segments of the population by giving them a chance through the disbursement of financial services. Usually commercial banks are not aware of the existence of this niche of market or do not show particular interest in microfinance, fearing that a direct involvement would imply a waste of resources, high risks and low rewards.

Microfinance was active in Egypt since the 1950's. Back then, small loans and related services used to be provided by NGOs and various governmental projects, such as:

1. The Productive Families Project

[8] Source: UNDP Egypt

2. Bank Nasser
3. Mubarak Social Solidarity Program

The Government started the so called **Productive families project (PFP)**, implemented through the Ministry of Social Affairs, was established in 1964 and means to mobilize the potentials of Egyptian families by engaging them in profitable home enterprises. Low income families (especially those earning less than 100 Egyptian pounds per month) are selected, receive training and finally start their own activity. The project provides the beneficiaries with technical assistance, in kind inputs such as raw material (clothes, stripes of leather and so on), equipment, tools and marketing services provided through outlets and fairs managed by the PFP[9].

Once the beneficiaries start their activity and start producing their goods, the Government acquires them and attempts to put them on the market. Unfortunately, due to the lack of quality of the goods produced, the majority of them are still stored in governmental warehouses.

Bank Nasser instead provides loans ranging from 1.000 Egyptian pounds to 10.000 Egyptian pounds. They are to be repaid in monthly installments over 3 to 5 years at a 6% yearly interest rate.

Mubarak Social Solidarity Program finances income generating projects and training activities.

Until recently, microfinance services in Egypt were carried out within broader human development strategies frameworks. In the early 1990's anyway, USAID[10] started working on microfinance through a program managed by two NGOs, one in Cairo (Egyptian Small Enterprises Development Association) and one in Alexandria (ABA), together with a commercial bank, namely the **National Bank for Development** (NBD).

NBD was the first bank that got involved with the micro – sector by the establishment of the Small and Micro – enterprises Division in 1987 under a project funded by USAID.

---

[9] UNDP "The role of Social Assistance and Insurance in Alleviating Poverty" Egypt Human Development Report 1997/98

[10] Since 1990, USAID/Egypt has been the largest financier of microfinance initiatives in Egypt, with estimates of supporting more than 70 % of all activities in this sector. USAID assisted in establishing seven not-for-profit business associations and a private credit guarantee company, and helped develop micro-lending programs at two banks. These institutions are now managing an outstanding loan portfolio of LE 380 million serving about 275,000 borrowers. More than 55% of these borrowers are poor female-headed household women located in Egypt's economically disadvantaged areas (source: USAID website)

Also PBDAC (Principal Bank for Development and Agricultural Credit) started engaging in microfinance during the same years (1993), but its activity was restricted and specialized in the agricultural field.

At year end 2003 Egypt had over 250,000 active clients of whom more than 80% were served by 7 fully sustainable MFIs. Over $ 55 million was outstanding in microloans. The remarkable growth in the country can be attributed to two key factors: product diversification through the introduction of group lending (for women) provided essentially by seven USAID partner Foundations and the revitalization of downscaling programs through banks, both initiatives sponsored by the major donor in the sector, USAID[11].

NBD is considered a success story in the Egyptian microfinance environment. Modeled in part after the Grameen Bank its program combines the attitude of NGOs and the sound financial principles of banks, with a flexible lending procedure, client oriented service delivery and well trained staff.

In June 2001 a new bank entered the market: **Banque du Caire**. The bank entered microfinance for different reasons:

1. a restructuring scheme and the privatization procedures
2. a new BOD with international exposure and background that started exploring new ways of doing business
3. a process of semi – automatization that led to an excess of personnel and redundant labor that needed to be employed in some other way

When the bank got involved in microfinance, the redundant labor was employed in the industry (which implies labor intensive activities): underemployed staff working in 97 branches joined the microlending program as loan officers, thus allowing the bank to reach a good performance, exceeding with the net yield portfolio of microfinance 6 times the corporate loans. From 2001 to 2003 it became operational in 99 branches.

Banque Misr is the biggest bank in Egypt with stakeholder majority in other banks and in big private companies such as Egypt Air, Misr Travel and Misr Petroleum[12]. The starting point from which the decision to downscale into microfinance has been taken is exactly the opposite if compared to the one that pushed Banque du Caire. The bank is understaffed, especially in Upper Egypt. For this reason, it had to come up with a new formula: recruit new labor and supply and flank new hires with a good credit expert. Its

[11] UNDCF, 2004 ibid.
[12] During the period from 1920 to 1960, BANQUE MISR established 26 companies in various economic fields, including spinning and weaving, insurance, transport, aviation and cinema.

activities in microfinance have been partially financed by IFC; technical assistance was provided by EQI and its expenses were borne in the first phase 60% by IFC and 40% by the bank. Regarding the second phase, the processes was vice versa.

Banque Misr started its activities in areas where Banque du Caire had previously launched its own in order to establish in a competitive environment, aware that if it would have worked there it would have worked anywhere else. And so it did. It started its activities with 5 branches in Upper Egypt in areas where Banque du Caire had been active since 3 years.

The two banks started operating in microfinance mostly at the same conditions but:

1. Banque Misr benefited from a higher commitment from its management, which is considered the most important condition for a successful downscaling program[13]
2. Banque Misr is not funded by donors, which gives higher freedom in choosing the policies because there are no restrictions from outside and higher power for negotiation

[13] Making loans to microbusinesses is a strategic choice and not every bank should make that choice. Only when the bank sees a strategic fit between its objectives and this target group should it engage in microfinance – UNCFD, 2004 ibid.

4. Banque du Caire

4.1 General information

4.1.1. Background: why did the bank choose to be involved in microfinance?

As stated before, Banque du Caire used to be one of the four large State owned banks in Egypt. Microfinance is a fairly new sector in Egyptian traditional banking system and the bank discovered it quite recently. The reasons why it started downscaling into microfinance are both internal and external. In 2001 it found itself on the edge of bankruptcy, mostly due to mismanagement. Between the measures taken to face this crisis was the hiring of 11 people coming from the private sector who analyzed the bank's situation and found proper solutions to its problems. One of the main problems was the abundance of labor: at that time experts found that out of 12.000 employees, 3.500 only were useful for a good performance of the institution.

Microfinance constituted a good opportunity for:

- Labor absorption: by the end of 2003, 660 people from the bank's staff volunteered to join the microfinance program, were trained and received substantial performance bonuses, finally being productive and feeling useful for the bank's activities
- Risk distribution (larger number of clients in a wider geographical area)
- Profit making, even when dealing without traditional guarantees, but utilizing social capital as collateral

The external causes that led Banque du Caire to the involvement in microfinance were:

- Presence of a market. The bank realized that there was a market niche that needed to be covered by these services
- The financial support of USAID and the technical assistance of EQI
- Presence of **competitors**, such as NGOs and two other commercial banks, National Bank and Banque Misr. The bank feels the competition with NGOs, who are well established in the country and have gained the trust of people, especially at grass roots level and consequently a good control of the territory.

In two and a half years, Banque du Caire has reached over 45.000 active clients and a portfolio outstanding of over $ 14 million and the profitability of its microloan portfolio is more than double that of a normal performing loan portfolio in the best performing banks.

The bank used its own fund for onlending and no external guarantees were used[14].

Banque du Caire recognizes that so far it was lacking the tools to reach the traditional target groups for microfinance and it is planning to expand its activities in two ways:

a. vertical expansion – reach the *merkaz* (regions) opening 80 specialized bureaus, from which they have already opened 5
b. product mix broadening – adding new products to loans, such as:
    - microsavings
    - microinsurance
    - university funds for children
    - consumer loans (except for housing equipment)

Year of establishment: of the microfinance program July 2001
Legal status: commercial bank
Region: 25 out of 26 Egyptian Governorates (soon establishing a branch also in Sharm El Sheikh)
Number of branches: 102 + 5 specialized bureaus
Products offered: so far, microenterprises lending
Other services provided: none (no technical assistance)
Largest funder: USAID
Number of active clients: 81.748

[14] UNCDF, 2004 ibid.

5. Banque Misr

5.1 General information

Banque Misr started its activities in microfinance with the main purpose of transforming the unbankable segment of the Egyptian population into clients of the bank. Following a microentrepreneur since its first approaches with financial services transforms him into a loyal client of the bank, thus reaching two main goals: giving access to financial services to those who would never have any other chance to do so and acquiring new, loyal clients for the bank. The banks in fact can relay on two main factors when they aim at growing and being strong enough to face competition: clients and variety of products.

Banque Misr does not feel the competition with NGOs for a series of reasons:

1. NGOs have a different approach and a different target
2. NGOs rely on donor funding and do not use their own capital
3. NGOs target the grass roots, the poorer of the poor and are strongly committed in fighting poverty, with no interest in profit making and profitability. Most of them anyway, aim at the sustainability of the financial institutions they create
4. NGOs already collaborate with the bank by depositing their resources there: the bank itself can make profits from the NGOs and at the same time support them with its own technical skills.

Regarding the microfinance program, the idea arose by the necessity of facing competition in the market and the inevitability of broadening the range of products offered to a broader range of clients or potential clients. Besides all this, a great support was given by the strong commitment showed by the bank's management, seriously intentioned to "take the banker's hat out to leave space to the microfinance hat". A different perspective and a different approach.

When Banque Misr started operating in the field of microfinance Banque du Caire was already active in some Governorates, and Banque Misr followed its path, concentrating its activities in Upper Egypt, the Southern and poorer area of the country. Two are the main reasons that led to this: first of all this is the neediest area. Secondly, it is an area where social pressure is still very strong, where not repaying a loan can be considered a shame in front of the whole community and its gives higher cover from the risks to the bank itself.

Year of establishment: banking activities -1920 ; microfinance program – September 2003

Legal status: commercial bank

Region: Egypt; microfinance activities especially concentrated in Upper Egypt (South)

Number of branches: banking activities – 420

Number of staff: 14,000

Products offered: microlending to microenterpreneurs

Other services provided: technical assistance through EQI

Main fund sources: bank's own sources (equity + depositors)

Group – individual lending: individual

Average loan size: 3,000 LE (Three Thousand Egyptian Pounds)

Average loan term: 6 months

Guarantees/ collaterals: none

Eligibility requirements:

Main sectors financed:

Number of active borrowers: 9.000

Number of savers: 1.000

5.2 Outreach

Women borrowers: 10%
Rural clients: 100%
Clients starting microenterprise for the first time: none, the bank lends working capital for existing projects

5.3 Financial sustainability

Real effective interest rate: 16%
Given the fact that Banque Misr is a commercial bank, most of the indicators of financial sustainability[15] are considered confidential and thus not available to the public.

[15] Subsidy Dependance Index (SDI), operational self-sufficiency, financial self-sufficiency, volume savings/volume loans outstanding, arrears rate, portaolio at risk, risk coverage, loan loss rate, internal source to loan ratio, personnel expense ratio, ROA, ROE, portaolio yield.

5. Future perspectives

Microfinance in Egypt is an evolving sector. While in many countries the field is still driven by governments, donors and NGOs, in others commercial orientation is rapidly growing: partnerships are being created, public and private sectors' assets are being leveraged and know how starts being shared.

Egyptian microfinance industry is moving towards this last path: its main actors are going to be the Social Fund for Development, NGOs and Foundations as well as commercial banks. A sort of integration is taking place: the internal financial markets, also in terms of microfinance, are maturing, international donors and institutions, after having set capital, technical assistance and know how, are slowly taking a more marginal place. In any case, the bulk of support to the sector continues to be financed by donors and the government through direct institutional investments rather than support to the sector as a whole. This sustain will neither be adequate to satisfy the full demand nor to ensure sustainability of access to poor and low income households[16]. This is why the need for gradual integration of microfinance into the traditional financial sector took place, thereby offering microenterprises a diversified range of financial services. This also means that there is a need for a reform of the banking sector, focusing in particular on product diversification. Integration of microfinance in the formal financial sector is also one of the key points of the Sector Development Approach drafted by the "Building a National Strategy on Microfinance" roundtables. According to this apporach, the success of the sector development is ultimately measured by the level of involvement of the financial sector in responding to the variety of demand for different microfinance services by the different target groups that are currently underserved (notably women, rural poor, youth and start up businesses) in the absence of donor support. This will require a broader**, inclusive multi-tired financial system with lower barriers to entry where a variety of market players** (banks, NGOs, Foundations, and so on) [17] **provide a broad range of services to small enterprises and the poor through a market based, sustainable, competitive sector**.

NGOs, with their strong social background and deep knowledge of local communities are more likely to be focusing on grassroots levels, home based enterprises, women and gender and solidarity lending. At the same time, this kind of specialization and focus of the NGOs is almost "forced" in Egypt, where the law does not allow them to collect savings and thus grow as MFIs.

[16] UNCDF 2004, ibid.

[17] Building a National Strategy for Microfinance – Draft Outline, June 14th 2005

Banks are more likely to specialize in individual lending and the provision of various financial services such as credit for different purposes, credit guarantees and microinsurance.
Basically, microloans are already divided into those which are provided by NGOs only (too small for commercial banks) and those which are provided by banks and NGOs, as follows:

From 50 to 500 LE	NGOs only
From 300 to 1,500 LE	NGOs only
From 1,500 to 10,000 LE	Banks and NGOs
From 10,000 LE up	Banks and NGOs

In any case, as recognized by Littlefield and Rosenberg, "there is a growing recognition that building financial systems for the poor means building sound domestic financial intermediaries that can mobilize and recycle domestic savings. Foreign donor and social investor capital diminishes as individual institutions and entire markets mature. For this reason, more and more MFIs are getting licensed as banks or specialized financial companies (…) and the move toward specialized MFIs sometimes overlooks opportunities to involve mainstream commercial banks in microfinance". In countries as different as Haiti, Georgia and Mexico, partnerships between commercial banks and MFIs are an alternative to MFIs seeking their own financial license (and) vary in their degree of engagement and risk sharing, ranging from sharing or renting front offices to actual portfolio purchases and equity investments[18].
CGAP summarized this scenario, basing the information on the successful International experiences:

[18] Littlefield E., Rosenberg R., 2004 ibid

Forging New Links
Commercial banks and MFIs are forming partnerships.

Higher level of engagement

Bank creates loan service company	**Sogebank (Haiti)** created Sogesol, a microloan service company, in 2002
Bank invests equity in an MFI	**Jammal Trust Bank and Credit Libanais (Lebanon)** have equity stakes in Ameen, a microfinance program
Bank buys MFI portfolio and/or contracts MFI operations	**ICICI Bank (India)** contracts microfinance operations with self-help groups and MFIs
Wholesale lending	**Raffeissen Bank (Bosnia)** lends to multiple MFIs in Bosnia
Sharing/renting facilities	**Mcrofinance Bank (Georgia)** rents space in its offices to Constanta, a local nongovernmental organization

Lower level of engagement

Source: CGAP 2004

While integration and specialization are the key words in the future perspectives of microfinance in Egypt, competition quickly becomes a "hallmark of the environment in which MFIs operate. The profits created by pioneering NGOs generate a demonstration effect attracting others to follow (them) and offer similar services. This, in turn, forces microfinance institutions to begin to make changes in product design, prices, delivery mechanisms or other basic features of classic businesses to preserve or increase their market share"[19].

In many countries then, microfinance institutions are losing their monopolistic control over the market, and customers are slowly becoming experienced purchasers of a wide variety of financial services. The emerging reality of increasing competition and a more discerning clientele necessitates a different approach to microfinance both from MFIs and from commercial banks. For both, customer satisfaction but most of all loyalty is becoming a pretty fundamental issue. MFIs are willing to incorporate the clients' feed back in their product design and delivery, in order to improve their performance and face the competition with banks. Banks instead focus on building a new and loyal generation of clients by penetrating the market which stands at the frontier between formal and informal finance. Delivering services to microclients will have the double effect of allowing these clients to grow (especially regarding their financial activities) and to appreciate the fact that that specific bank trusted them and their business. They will feel comfortable and save when dealing with that specific institution and as their business grow and consequently their financial needs arise, they will be loyal clients and ask "their" bank for advice and services.

A good strategy for the growth of the sector in Egypt would necessarily have to imply:

1. The establishment of a partnership between banks and microfinance intermediaries[20] with a deep outreach – the banks themselves could not reach microfinance clients on a sufficient scale and they are perfectly aware of this limit of theirs although they are spread in all 26 Egyptian governorates.

[19] Christen R.P., "Commercialization and Mission Drift: The Transformation of Microfinance in Latin America", CGAP Occasional Paper, Washington DC, No. 5, 2000

[20] NGOs (ie Save the children US – Egypt Program), MFIs (ie Alexandria Business Association – ABA Dakalya Businessmen's Association for Community Development, Al Tadamun) and also the National Postal Authority, that already signed an agreement with the SFD and can play an important role in the field both because it offers savings accounts with competitive interest rates and because it controls a huge network (3.400 post offices and 6.000 postal agencies). Moreover, it serves 11 million people around the country, who keep LE 22.5 billion in postal savings accounts.

2. The creation of broader variety of financial institutions such as co – op banks, specialized microfinance banks and credit – only institutions which would allow to improve outreach
3. Broadening the choice of products. So far, NGOs were the main actors of the microfinance industry. The NGO law n. 84 does not allow these organizations to provide any other financial service than credit: most of all, they are not allowed to collect savings. With the access of new pioneering institutions, such as banks, in the market, the range of products offered can be broadened. Of course, a parallel institutional support is needed: approval procedures should be facilitated by the Ministry of Finance.
   These products include:
   - savings: it is estimated[21] that less than 50% of SMEs access formal channels for savings and that 95% of SMEs do not have a bank account. Clearly, there is a huge demand for this king of services
   - microinsurance[22]: main providers in the insurance sector are basically state owned companies such as Misr Insurance, Al Shark Insurance and Al Ahli Insurance, regulated by Law n. 91 of 1995, that divides their activities into life and non life. Banque du Caire is planning to expand its products to microinsurance, not providing them directly but through one of these companies.
   - Leasing
   - ATM cards
   - Money transfers
4. Funding of the industry: the major sources for financing are banks, insurance companies, government and international institutions. The sector in any case relies more on grants than in sustainable sources. From this, urges the necessity to attract commercial capital on a sustainable basis.
5. Need of further coordination, between all the actors involved: Ministers, banks, Central Bank of Egypt, SFD, NGOs, donors (especially at the DAG subgroup), local and international organizations. In this sense, Sanabel is playing a very useful role, not only in Egypt, where its headquarters are located, but in the whole North Africa and Middle East area.

Besides each specialization, there is a need to build bridges between banks and NGOs, in order to better serve the clients.

[21] Source: Egyptian Ministry of Foreign Trade

[22] **Microinsurance** is a system by which people, businesses and other organizations make payments to share risk. Access to insurance enables entrepreneurs to concentrate more on growing their businesses while mitigating other risks affecting property, health or the ability to work (definition of the

6. References

- **Africap Seminar report** “Financing MFI growth in Africa through commercial capital”, 25 April 2003 , Dakar, Senegal
- **Arestis P**. “Financial Sector Reforms in Developing Countries with Special Reference to Egypt”, July 2003 The Levy Economics Institute of Board College
- **Chowdri Siddartha H**. “Downscaling Institutions and Competitive Microfinance Markets: Reflections and Case – Studies from Latin America”, August 2004 Edited by Alex Silva, Omtrix Inc., Commissioned by CALMEADOW
- **Christen R**.P., “Commercialization and Mission Drift: The Transformation of Microfinance in Latin America”, CGAP Occasional Paper, Washington DC, No. 5, 2000
- **De Soto H**. “The Mystery of Capital”
- **Dhumale, Sapcanin and Tuker** “Commercial Banking and Microfinance in Egypt: National Bank for Development. Case study”, 1999
- **Drake D., Rhyne E.,** “The Commercialization of Microfinance: Balancing Business and Development” Kumarian Press, 2002
- **Halperin S., “**Microfinance in the New Millennium: Efficiency, Customer Satisfaction and Commercialization” Paperback, 2000
- **Harper M., S.Singh Arora** “ Small Customers, Big Market” TERI Press, New Delhi, India, 2005
- **Littlefield E., Rosenberg R.** “Microfinance and the Poor:Breaking Down the Walls between Microfinance and the Formal Financial System” *Finance & Development* 41, no. 2 (June 2004), 38 – 40

- **Robinson M.S.** " The Microfinance Revolution, Vol. 1, Sustainable Finance for the Poor" Washington DC 2001
- **Timewell S**. "Microfinance gains momentum" article published by The Banker on 2nd February, 2005
- **UNCDF Brandsma J., Burjorjee D.** "Microfinance in the Arab States. Building inclusive financial sectors", October 2004
- **UNDP** "The role of Social Assistance and Insurance in Alleviating Poverty" Egypt Human Development Report 1997/98
- **Viganò L.** (a cura di) "Microfinanza in Europa", Fondazione G. Dell'Amore, Fondazione Europea G. Venosta, Giuffrè Editore, 2004