American Chamber of Commerce in Egypt

Research Note

Mapping Egypt's Legislative Environment for Financial Inclusion

Financial Inclusion
#nobarriers2banking

AmCham Research

Egypt has come a long way since 2014 when the government embarked on numerous initiatives to draw the unbanked population into formal financial channels. According to the World Bank's Global Findex, the number of adults with a bank account grew to 33% of Egypt's population in 2017, more than doubling from 14% in 2014 and tripling from 10% in 2011; market research firm Euromonitor estimated that figure grew to 38% in 2018.[1] Bound by a host of Central Bank of Egypt (CBE) regulations governing asset quality and capital adequacy in the banking system, the government has opened up various non-banking channels to grow financial inclusion in Egypt. These have required numerous regulatory overhauls, which the government developed over the past six years.

Microfinance Act (Law 141 of 2014)

In December 2014, the government ratified legislation to regulate microcredit provided by non-banking finance (NBF) service providers, putting them under the supervision of the Financial Regulatory Authority (FRA, previously the Egyptian Financial Supervisory Authority until it rebranded in November 2017). The law, the government's first in a series to grow the NBF sector in Egypt, gave the green light for specialized non-banking microfinance lenders to enter the market. Previously, only banks and non-governmental organizations (NGOs) could extend microcredit, where NGOs were regulated by the Ministry of Social Solidarity (in accordance with the Non-Profit Organization Law 84 of 2018 – known as the NGO Law). Banks remain regulated by the CBE.

The 2014 law defined microcredit as a loan not exceeding EGP 100,000 provided for commercial purposes to borrowers in the services, industrial, agricultural and other economic sectors. Microfinance companies were put under the exclusive jurisdiction of the FRA and required to be licensed by the authority, take the legal form of a joint-stock company and have an issued capital of at least EGP 5 million and paid-up capital of at least 50% of that amount.

Data on microlending only became publicly available in 2016, but industry experts estimated there were 400 microfinance lenders in 2014 extending credit to 1.6 million borrowers. To date, there are just under 1,000 microfinance lenders: The majority (99%) are NGOs, with 11 microfinance companies (1%) that have set up shop since the law was passed. Microfinance companies currently account for about 50% of the market share in terms of both total loan value and volume. According to the FRA, the total number of borrowers has registered a compound annual growth rate (CAGR) of 15% between 2016 and 2020, from 1.8 million to 3.1 million borrowers. The aggregate value of microloans grew fourfold from EGP 4.5 billion in 2016 to EGP 18 billion in 2020, posting a CAGR of 41%. Microenterprises operating in the commercial[2] sector continue to account for the lion's share of microcredit borrowers: As of Q3 2020, they accounted for 65% of the total volume of microloans, followed by agriculture (15%), services (13%) and industrial borrowers (7%).

1 The figure is still significantly lower than the 2017 global average of 69% and the low-middle income countries' average of 57%. According to surveys conducted in 2017 by the World Bank and U.S.-based research company Gallup, just over 6% of Egyptian households had a loan from a formal financial institution, while 38% borrowed from family and friends. Of those surveyed, only 25% had a debit card, 3% had a credit card and just 4% had a housing loan.

2 These include companies engaged in importing and exporting, internal trading, logistics and similar business activities.

Financial Leasing and Factoring Act (Law 176 of 2018)

In August 2018, the government replaced the 1995 financial leasing and 2003 factoring laws by ratifying Law 176 of 2018. Both NBF services are key in growing the economic contribution of micro, small and medium enterprises (MSMEs) in Egypt, which represent over 95% of businesses, 75% of the country's total employment and 35% of annual GDP. Financial leasing helps scale up business volume and thereby steers higher production and economic growth, while factoring helps accelerate the availability of cash flows without the need for costly, lengthy banking procedures and accompanying personal or commercial guarantees.

As per the law, financial leasing or factoring activities may only be carried out by FRA-licensed joint-stock companies with paid-up capital of not less than EGP 10 million or the equivalent in foreign currency. Contracts qualifying as financial leasing must be for assets directly needed by the lessee; the law does not govern contracts related to usage and/or exploitation of natural resources such as oil and gas, or assets that are not commercially used. The bill also took into account the Movable Collaterals Act (Law 115 of 2015) by allowing for the use of movable assets as collateral for obtaining financing.

The law has still not fully activated the potential of both industries. The number of financially leased commercial assets grew from 2,329 in 2014 to 2,362 in 2018 and 2,621 in 11M2020, posting a seven-year CAGR of only 2%. However, their aggregate value increased more than sixfold from EGP 7 billion in 2014 to EGP 41.6 billion in 2018 and EGP 58.6 billion in 2020, registering a CAGR of 42% since 2014. This is likely directly related to the types of assets MSMEs are more inclined to lease: According to the FRA, property and real estate account for the bulk of leased assets, accounting for 85% of the market's total value as of Q3 2020.

The factoring market has also been slowly growing. In volume terms, the number of factored contracts increased from 182 in 2014 to 308 in 2018 and 422 in 11M2020, while their aggregate value registered EGP 11.3 billion in 2020, up from EGP 10.6 billion in 2018 and EGP 1.2 billion in 2014; this represents a CAGR of 15% and 45% in volume and value terms, respectively, between 2014 and 2020.

E-payments Act (Law 18 of 2019)

The Egyptian population's excessive reliance on cash has increased the volume and value of unrecorded transactions in the economy, growing the gray economy further. The government has therefore been focusing on integrating electronic payment methods and advocating for cashless transactions. Drafted by the CBE, the E-payments law was passed in April 2019, obliging all state authorities to offer digital payment methods. The executive regulations of the law (ER 1776/2020) require the government and private sector entities to make all payments to subsidiaries, suppliers and contractors electronically. State-owned companies and/or companies with a majority stake owned by the government are mandated to use non-cash payments for:

- Salaries and social insurance contributions for employees, consultants, chairmen and members of boards of directors, and committees;
- Cash financing grants;
- Distribution of profits;
- Payment of dues of members of syndicates and entitlements of participants in special insurance funds and insurance compensations.

The bill also introduced an electronic payment system for citizens to pay for all government services and state fees including taxes, customs duties[3] and fines. Civil society organizations are also now required to use electronic payment methods to receive donations or funding. As of Q1 2021, cash payment limits for various business-to-consumer (B2C), business-to-business (B2B) and government-to-consumer (G2C) services will be effective.

3 Ministry of Finance decree 760 of 2018 stipulates that payments for all governmental dues, including tax and customs in excess of EGP 100,000 should be executed through an electronic payment and collection system.

Cash Payments Caps as per Law 18/2019

Cash Payment Limit	Category
EGP 1	Public sector payments—including by public entities, government authorities and companies fully/partially owned by the state—to suppliers, contractors and service providers
EGP 500	• Public and private tuition fees • Metro and public transportation passes • Retail loan installments • Syndicate members' entitlements • Donation and grant payments • Tax, customs and administrative penalty collections • Government service fees
EGP 1,000	• Mobile phone and internet bills • Car fuel
EGP 2,000	• Property and non-peer-to-peer car rentals • Microfinance, leasing and factoring installment payments • Dividends from equity capital in companies and investment funds
EGP 3,000	• Monthly gas bills
EGP 5,000	• Non-peer-to-peer property and car sales • Monthly rental/usufruct of property, land or vehicle payments • Private sector payments to suppliers, contractors, service providers and subsidiaries • Private insurance compensation • Monthly electricity and water bills
EGP 10,000	• Car and property sales • Plane and boat tickets • Collection of donations and grants
EGP 500,000	Payments of installment financing, insurance premiums, syndicates' contributions and private insurance contributions

Parties that fail to comply are subject to a penalty equivalent to 2-10% of the transaction's value, with a maximum fine of EGP 1 million. Fines will be doubled for repeated offenders.

In order to promote cashless payments, the law's executive regulations also rolled out several incentives, including:

- Discounts of 5% to individuals opting for e-payments;
- Refund of up to 3% to individuals opting for e-payments;
- A point system that entitles regular e-payment users to up to a 5% cash-back voucher.

In December 2019, the government began rolling out Meeza, a debit card for state employees and unbanked consumers to use for transactions exceeding EGP 500. The state-backed card allows holders to pay for online and offline government services, purchase merchandise, receive salaries and use on local e-commerce websites. As of January 2021, about 23 million Meeza cards had been disbursed.[4]

4 *Meeza cards are disbursed through Egypt's major banks including the National Bank of Egypt, Commercial International Bank (CIB), AlexBank, Banque Misr, Banque du Caire, Qatar National Bank Al Ahli (QNB AA), The United Bank, National Bank of Kuwait and others.*

Consumer Credit Act (Law 18 of 2020)

The consumer financing bill was rolled out to regulate non-banking consumer financing companies, also under the regulatory umbrella of the FRA, which extend credit to finance purchases of consumer goods and services. There are currently 25 companies operating in the market, growing at an estimated 20% per year, with a collective lending portfolio of EGP 70 billion and 2 million beneficiaries as of Q1 2020.

The law categorizes creditors into two categories:

- Consumer finance companies: licensed to extend credit via commercial payment cards or other CBE-approved payment methods through a contractual arrangement with a network of suppliers of goods and services.
- Consumer finance providers: producers or distributors of goods or services who finance consumer purchases of their merchandise.

Goods and services that fall under the scope of consumer finance companies include vehicles, durable goods (including electronic devices), educational services, medical services, travel and tourism services, as well as any other goods or services approved by the FRA. Consumer finance providers are limited to vehicles and durable goods such as home appliances and electronics.

As of September 2020, all FRA-approved consumer finance companies must:

- Be a joint-stock company with an ownership structure that has at least 25% held by a financial institution and 50% held by a juristic person;
- Meet minimum capital requirements of EGP 10 million;
- Conduct FRA-compliant contractual agreements with clients;
- Abide by confidentiality, advertisement and marketing requirements laid out by the FRA, as well as make certain disclosures to the regulator with respect to the calculation of interest.

MSME Development Act (Law 152 of 2020)

The MSME bill had been a work in progress since 2016 with input from various government authorities including the Ministry of Finance, FRA, Ministry of Trade and Industry, and CBE, among others. The bill was ratified in July 2020, setting the guiding principles to entice more SMEs into joining Egypt's formal economy and grow their contribution to production, employment and national income.

The law defines MSMEs based on company size and annual turnover, as per CBE recommendations issued in 2018.

MSME Categories as Defined by Law 152/2020

	Number of Employees	Registered Enterprises[5] (annual turnover)	Newly Established Enterprises (paid-up capital)
Micro	< 10	< EGP 1 million	< EGP 50,000
Small	< 200	EGP 1-50 million	Industrial: EGP 50,000-5 million Non-industrial: EGP 50,000-3 million
Medium		EGP 51-200 million	Industrial: EGP 5-50 million Non-industrial: EGP 3-5 million

The legislation provides tax, customs and non-tax incentives for informal economic projects that register as formal businesses. The same incentives are also extended to already registered MSMEs operating in digital transformation, industrial intelligence, agriculture, animal production, IT-related services, new and renewable energy as well as industrial projects that deepen the local component value chain and/or replace and renew machinery and equipment and technological systems related to the production process.

5 *Registered for less than 2 years*

Non-tax incentives

- Land allocation to investors for a significantly discounted fee (cost of supplying utilities to the land plot);
- Partial or total refund of the cost of supplying utilities to the plot once the project is operational;
- Total or partial exemptions from interest on payment delays;
- Various cash flow incentives;
- Free participation in local exhibitions/trade fairs;
- Exemptions from financial guarantees required by the government prior to finalizing land allocation processes;
- A mandate that at least 20% of the government's commercial transactions be contracted[6] to medium-sized enterprises and at least 20% to small and microenterprises;
- Annual government aid equivalent to 0.3% of Egypt's GDP (a minimum of EGP 1.5 billion) from the state budget to extend financing to MSMEs;
- Temporary land allocation to MSMEs through lease/sale of usufruct rights, lease or lease-to-own models;
- Legal protection from any suspension decisions that a legally competent authority can issue against licensed projects.[7]

Tax and customs incentives

- A five-year exemption from stamp tax; notary public government fees; and fees for licensing, contracts for establishing companies, credit facilities contracts and mortgages;
- Exemption from taxes and fees imposed on land registration contracts to establish enterprises;
- A fixed discount on tariffs equivalent to 2% of the value on all imported machinery, equipment and industrial parts (except passenger vehicles) needed for business activity;
- Capital gains tax exemption for registered enterprises on the disposal of assets or machinery, given that the gains realized from their disposal are utilized to purchase new assets or machinery within one year from the date of disposal.[8]

The law also imposes significantly lower tax rates for MSMEs. Microenterprises are levied flat rates on annual income, while rates for small and medium businesses are based on a negligible share of their annual income. MSMEs under the new bill are exempted from provisions of Income Tax Law 10 of 2019 (which replaced Law 91 of 2005), including tax return submissions and financial record keeping. The law instead gives the Ministry of Finance the authority to issue alternative regulations with considerably more simplified procedures for MSME record keeping.

MSME Special Tax Treatment as per Law 152/2020

Annual Revenues	Income Tax Dues
Microenterprises	
< EGP 250,000	EGP 1,000
EGP 250,000-500,000	EGP 2,500
EGP 500,000-1 million	EGP 5,000
Small & medium enterprises	
EGP 1-2 million	0.5% of annual income
EGP 2-3 million	0.75% of annual income
EGP 3-10 million	1% of annual income (valid only for 5 years)

6 These can take the form of product purchases, tenders, technical works, consulting services and business contracts with government bodies.

7 Unless licensed MSMEs commit a violation that requires legal closure, in which case the government's MSME development authority is notified ahead of the decision, and the competent authority has to notify the MSME of the violation and the period specified for its suspension.

8 Further details on this incentive will be included in the law's executive regulations.

MSMEs will be allowed to revert back to the 2005 Income Tax Law if they are recording losses or would be paying a higher effective tax rate under the new law. However, should they revert back to old income tax provisions, they will be unable to switch back to the new tax treatment for at least five years.

Realizing the impact of entrepreneurship on the economy, the MSME Act has also included startups and relevant supporting entities in the law's provisions. Supporting entities—including banks, financial institutions and non-banking corporations licensed to finance MSMEs—will be granted the same non-tax incentives if they set up industrial, production, crafts or services complexes to grant MSMEs spaces for their activities or are incubators/accelerators and working with micro, small and medium startups.

Amendments to the Banking and Central Bank Law 88 of 2003 (Law 194 of 2020)

The government's new banking legislation was ratified in October 2020. The law applies to the CBE and banking sector at large, including foreign exchange companies, money transfer companies, information and credit rating companies, credit guarantee companies, payment system operators (PSOs) and payment service providers (PSPs).[9] The amendments expand the role of the CBE's board of directors by vesting it with several authorities and functions in the issuance of decrees, regulations and licensing requirements. Law 194/2020 also authorizes several tools to streamline the digital transformation of the banking and financial sectors and grow financial inclusion. These tools include digital finance, digital settlement of cheques, e-money, cryptocurrency, fintech and regtech.[10] Article 8 of the law states that the CBE shall take all the necessary means to enhance financial inclusion, expand the banked population and reduce cash transactions in the economy. Digital banks, which the law defines as financial institutions that provide all-inclusive banking services to clients via digital channels and or/platforms using fintech, can now operate in the market after being licensed by the CBE. They will be exempt from minimum capital requirements imposed on physical banks, which the new amendments increased to EGP 5 billion for local banks and USD 150 million for foreign banks.[11]

The legislation also gives the CBE regulatory control over PSOs and PSPs, which were previously directly supervised by the banks they partner with to provide their services. Both PSOs and PSPs will be required to obtain approvals and licenses from the CBE and deposit a bond to guarantee performance of contractual obligations. According to article 85, the CBE's board of directors will issue detailed licensing conditions regarding minimum capital requirements, legal form of companies, technical efficiency requirements, financial solvency, shareholding structure, type of technology used and operating rules. Per the law, licensing fees will not exceed EGP 500,000 for PSOs and EGP 100,000 for PSPs.

The executive regulations for Law 194/2020 should be issued in H1 2021, with a grace period extending to mid-September 2021 for entities to comply.

9 PSOs and PSPs are non-banking payment providers and/or facilitators. PSOs process and facilitate transactions, while PSPs are platforms that offer payment services via banks and PSOs.

10 Regulatory technology refers to new technology used to enhance regulatory processes, particularly in the financial sector. Often regarded as a subcategory of fintech, regtech is most used in regulatory monitoring, reporting and compliance.

11 Under Law 88/2003, the minimum capital requirements were set at EGP 500 million for local banks and USD 50 million for branches of foreign banks.

Amendments to Microfinance Act (Law 201 of 2020)

In October 2020, the government ratified amendments to the Microfinance Act (Law 141/2014) to further expand the outreach of MSME financing and tighten up regulation of the industry. Most importantly, the amendments raised the lending threshold for microfinance up to EGP 200,000 for a single borrower (or 10% of a company's equity), with the possibility of raising the limit further in the future.

The amendments also authorized SME-focused lenders to operate in the market, provided that they meet the FRA's minimum issued capital requirement of EGP 20 million. According to FRA decree 211 of 2020, SME lenders must integrate appropriate risk assessment and capital adequacy protocols, appoint experienced executive boards and seek approval from the FRA should a single party plan to hold over more than 25% of the company. SME lenders are now required to:

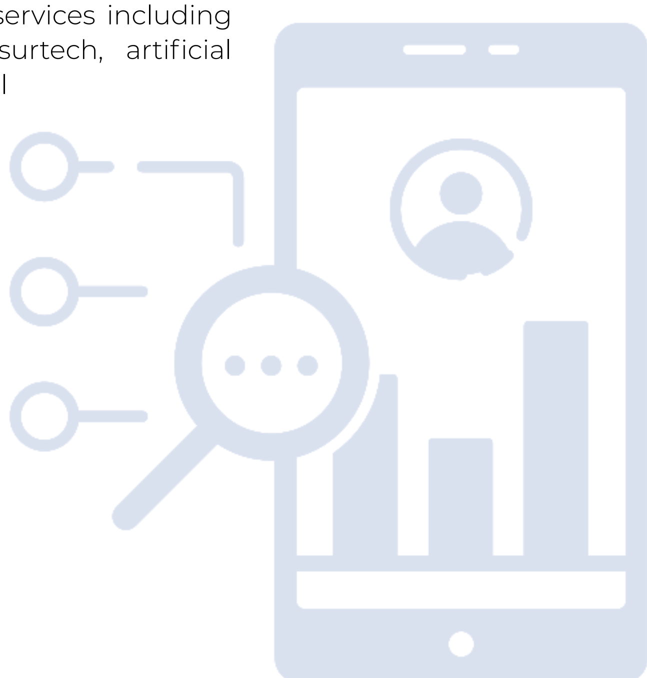
- Maintain a capital adequacy ratio of 12%;
- Set aside 15% of operating profit as a contingency against operational risks;
- Take on debt only up to 9x of their equity base;
- Have 100% of liquidity needed to cover outbound cash flows for a 30-day period at all times;
- Lend no more than 10% of capital to a single borrower;
- Lend no more than 25% of capital to borrowers in the same industry.

The law's provisions also cap loans to employees and/or relatives (up to the second degree) at 5% of a company's total financing portfolio. Violations include fines ranging from EGP 200,000 to EGP 1 million and short-term imprisonment.

Fintech Law (drafted)

In July 2020, the FRA drafted a law to regulate the use of fintech to deliver NBF services in Egypt. The draft law aims to facilitate the integration of innovative technologies into financial services provision, provide a set of regulatory guidelines for fintech businesses, ensure transparency and create the legal framework needed to support NBF services. It covers a wide array of services including crowdfunding, robo-advisory, microfinance, insurtech, artificial intelligence, mobile applications and digital platforms. To ensure regulation falls in line with global standards, the authority is planning to refine the legislation's technicalities with an unnamed international agency.

The upcoming legislation is expected to dovetail with the E-payments Act, the Central Bank and Banking Act and the Personal Data Protection Act (Law 151 of 2020).



State-backed Initiatives for Financial Inclusion

A number of government initiatives have launched over the past few years to scale up financial inclusion.

Social Housing and Mortgage Finance Fund (SHMFF): In 2015, the government set up the SHMFF to provide 1 million housing units to low-income families through a national social housing program, which the fund is executing in partnership with the World Bank, the Ministry of Finance, and 29 public and private banks and mortgage finance companies. The program aims not only to eliminate informal settlements in Egypt, but also break the local stigma of credit by drawing more consumers into debt financing, thus shrinking the size of the informal economy. A low-income household financing the purchase of a social housing unit through a 20-year mortgage is eligible for an SHMFF subsidy of up to 15% of the unit's value. As of 2019's end, the program had funneled EGP 27 billion in loans to 1+ million applicants since its inception; 65% of those applicants were new to the banking system and opened accounts for the first time.

CBE quota for MSME lending: In 2016, the CBE mandated that local banks allocate 20% of their lending portfolio to SMEs by 2020. The target was for banks to offer EGP 200 billion in loans to 350,000 SMEs and generate 4 million new jobs. In 2017, the regulator allowed banks' microfinance lending to count towards the quota, and in 2019, it allowed for banks' equity investments in SME-focused funds to also count. As of 2019's end, Egypt's 38 banks had doled out EGP 146 billion in loans to SMEs. To target microenterprises specifically, the government earmarked EGP 30 billion in 2017 to funnel microloans to 10 million beneficiaries through the end of 2021. In response to COVID-19, the CBE allocated EGP 360 billion to support SMEs through the economic repercussions of the pandemic throughout 2020.

National Council for Payments (NCP): In February 2017, presidential decree 89 of 2017 established the NCP under the president's chairmanship. The council's primary mandate is to reduce the circulation of money supply outside the banking system, support and encourage the use of e-payments, and develop a national payment system for all governmental payment and collection services as well as payments services provided by banks to customers, including internet, mobile and phone banking. The creation of the NCP was the precursor to the E-payments law rollout, and the council is also mentioned in the new banking law (Law 194/2020), given the CBE's technical role in developing the national payment system. Since its establishment, the NCP has been integrating various goods and services into the payment system that consumers and businesses can pay for electronically; expanding partnerships with banks, financial services and other payment processors; and facilitating procedures required to open bank accounts.

Micro, Small & Medium Enterprises Development Agency: prime ministerial decree 947 of 2017 established the Micro, Small & Medium Enterprises Development Agency to replace the Social Fund for Development established in 1991. Tasked with overseeing a national program to scale up MSMEs' contribution to the Egyptian economy, the new agency provides financing, capacity building, technical support and business facilitation services to MSMEs. It operates through a network of 33 branches across Egypt's governorates and partnerships with 1,800 bank branches and 600 NGOs that provide microfinance. As of 2020's end, the development agency had provided EGP 28 billion in funding to MSMEs since 2014 (when it was still the Social Fund for Development).

CBE Fintech Strategy: In 2019, the central bank rolled out a strategy to kickstart the fintech industry's growth and promote more digital financial services. The three-year, multilayered strategy includes a USD 60 million innovation fund that will directly and indirectly channel investments into fintech startups through venture capital funds, incubators, accelerators, angel investors and other industry-specific financiers. It was slated to go live in Q1 2020 but was delayed due to onset of the COVID-19 pandemic. The strategy also includes setting up Fintech Egypt, a platform and digital research lab to connect fintech market players and facilitate cooperation between startups and investors, policymakers, field experts, financial institutions and service providers. Through the platform, startups have access to a cohort-based "regulatory sandbox" to test innovative solutions live in a relaxed regulatory environment. The structured, supervised nature of the sandbox helps identify and manage risks associated with new technologies before products hit the mass market; this in turn helps the CBE develop regulations and consumer safeguards in line with global best practices.

Digital financial inclusion initiative: Most recently, the FRA launched a digital financial inclusion initiative in January 2021 to increase digital payment tools in the NBF sector. The initiative falls under article 3 of the E-payments Act, which obliges all entities providing cash financing – including microfinance companies and NGOs – to apply for licenses by April 2021 and distribute their financing through non-cash payment methods. The initiative will include several awareness and capacity building campaigns and a gradual transition to cashless transactions across all NBF services in Egypt.