THE IMPACT OF USAID ASSISTANCE IN THE INSURANCE AND PRIVATE PENSION SECTORS IN EGYPT

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LIST OF ACRONYMS

CLDP	Commercial Law Development Program
DSP	Development Support Program
EISA	Egyptian Insurance Supervisory Authority
GATS	General Agreement on Trades and Services
GOE	Government of Egypt
ISIS	Insurance Supervisory Information System
MEIS	Modernizing Egyptian Insurance Supervision
MOEFT	Ministry of Economy and Foreign Trade
RIM	Reforming Insurance Markets
SPR	Sector Policy Reform Program
SRS	System Requirements Specification
WTO	World Trade Organization

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EXECUTIVE SUMMARY

USAID/Egypt commissioned this study to provide an assessment for use by USAID staff in evaluating the impact of USAID assistance in the process of promoting reform of the insurance sector in Egypt. Findings represent the independent conclusions of the author concerning whether and how USAID support has been a significant element in assisting the Egyptian government to strengthen the insurance sector.

USAID has provided assistance to the Government of Egypt (GOE) for over ten years to support the privatization of Egypt's insurance market and strengthen the institutional capacity of Egypt's insurance sector. Through the cash transfer programs, the US and Egyptian governments have worked together to identify ways to strengthen the legal and regulatory framework in support of insurance liberalization. Additionally, targeted technical assistance programs developed by USAID in collaboration with the Ministry of Economy and Foreign Trade (MOEFT) have supported the government in meeting its obligations under the cash transfer agreements. Technical assistance activities have aimed to strengthen the legal and regulatory framework governing insurance, enhance the government's supervisory processes of the insurance industry, and educate the public about the role that insurance plays in strengthening the economy.

This study finds that following USAID assistance, the Egyptian Insurance Supervisory Authority (EISA) has strengthened its ability to monitor the market and protect consumers, and the legislative and regulatory framework has improved. The Egyptian insurance market has opened up to private insurers, increased the number of private pension funds, and benefited Egyptian consumers. Insurance premiums have grown an average of 10 percent per year in current Egyptian pounds since the promulgation of a new 1998 law, 16 private sector insurance companies are now operating in the market, (up from only two private companies prior to this), and the number of private pension funds offering retirement plans to Egyptian workers has increased by 12 percent. Market liberalization and greater competition have brought new product innovations, increased product availability, improved customer service, and better treatment of claimants. The USAID cash transfer programs and technical assistance packages were important elements to assisting government officials in EISA and the MOEFT to implement agreed-upon reforms and identify new measures in support of market liberalization. Other large donors, including the World Bank and European Union, have not been active in the area of insurance reform in Egypt.

In addition to USAID assistance, other factors were also at work to support this process. In 1995, Egypt became a signatory to the WTO, committing the country to abide by the terms laid out in the WTO/General Agreement on Trade in Services (GATS) which mandated that all members thoroughly liberalize their insurance sectors. GOE officials noted that failure to comply with GATS could result in the suspension of concessions extended to Egypt by other WTO Members under GATS or other WTO agreements, and could have serious effects on Egypt's ability to renegotiate the terms of its international debt. These commitments therefore contributed to "kick starting" the reform effort.

While the country's WTO commitments and USAID assistance promoted the adoption of reform measures, neither would have led to significant change without the commitment of key officials in the MOEFT and EISA to develop a liberalized insurance sector. These policy "champions" pushed through with a number of reforms that went beyond their international and bi-lateral commitments, recognizing the benefit of a strong insurance market to the Egyptian economy.

Egypt's insurance sector still has significant potential for growth. Insurance premiums account for 1.4 percent of GDP (up from 0.7 percent in 1998), which is still far below the regional average of 5 percent and the global average of 7.5 percent. And while total investments of the insurance industry have increased significantly over the past five years, they continue to amount to only 3 percent of GDP, compared with global averages of 6 percent. Additionally, EISA reports that 7.5 million workers now have private retirement accounts, which equals an increase of 134 percent over the past five years. While this is an impressive improvement, it still leaves an estimated 13.21 million workers with no private retirement savings.

While progress has been made, additional policy reforms are needed in the areas of privatization and taxation, and the country is in need of a greater number of certified actuaries. EISA's regulatory authority has improved, but the agency continues to need assistance in ensuring that formal procedures are in place across the agency and that staff are adequately trained, particularly in actuarial sciences. Greater attention is also needed in the area of public awareness, to inform the Egyptian public about the benefits of insurance to themselves and to the larger economy. Reforms addressing many of the above concerns are now under discussion in the Ministry of Investment and EISA, and are slated to be presented by the end of 2005.

1. INTRODUCTION

An active insurance market serves to pool the money of individual and corporate policyholders into various investment instruments, which in turn supports the development of capital markets and promotes overall economic growth. In addition to contributing to the strengthening of the financial sector, insurance and pension markets have the potential to benefit the Egyptian people in a number of ways. In a transparent and vibrant market with a number of competing providers, individuals and companies are able to purchase insurance policies and contribute to private pension schemes that meet their needs at a reasonable cost, which serves to mitigate potential losses and protect their material well-being for the future.

While insurance and other financial intermediaries have much potential to contribute to economic growth and benefit individual consumers, Egypt's insurance sector has traditionally been characterized by limited investment and heavy state dominance. In the early 1990s, the four state-owned companies controlled over 90 percent of the market, with the publicly owned Misr Insurance company alone accounting for approximately 50 percent of both life and non-life business. This, as one expert noted in the early 1990s, "restricted the operations of insurance companies and limited the sophistication and variation of products compared to those in more developed markets." [1] Growth of the sector was also hampered by a lack of public understanding of the potential and diverse roles of insurance in the economy as a whole.

In 1993, the Government of Egypt (GOE) and USAID began to address the need for insurance sector reform through the Sector Policy Reform (SPR) Program. As the government began to liberalize the sector under the terms of the SPR agreements, officials in the Ministry of Economy and Foreign Trade (MOEFT) recognized that the regulatory authority charged with implementing the reforms and supervising new market entrants required assistance in fulfilling its new mandate. USAID and the GOE therefore developed several technical assistance activities to support the government in its efforts to modernize the insurance and private pension fund industries and complement the ongoing cash transfer program initiatives. Three technical assistance programs were implemented from 1999 to 2003: Reforming Insurance Markets (RIM); the Commercial Law Development Program (CLDP); and Modernizing Egyptian Insurance Supervision (MEIS). From 1993 to 2003, USAID was the only donor involved in supporting the GOE to reform its insurance sector.[2]

This study reviews USAID assistance to the GOE in support of insurance reform, assesses what progress the Egyptian government has made in liberalizing the insurance and private pension funds markets, and describes how consumers have benefited. The impact of USAID assistance in this process is analyzed in terms of USAID's role in promoting legal and regulatory reform and in improving on EISA's ability to supervise the growing number of new players in the insurance and private pension fund markets. The study concludes with a discussion of future areas of reform needed.

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[1] American Chamber of Commerce, "The Insurance Sector in Egypt," *Business Studies Series*, August 2001.

[2] Interview with Dr. Regaii Hassan, 4 September 2005.

2. STRENGTHENING THE LEGAL AND REGULATORY FRAMEWORK

In the early 1990s, USAID and the GOE began to discuss policy options that would support the liberalization of the insurance sector within the Sector Policy Reform (SPR) Program.[3] The government's approach was to start first with the privatization of the joint venture insurance companies, and in 1993 under SPR II, the GOE reduced its share in one joint venture company. This resulted in a $10 million disbursement from USAID.

In 1995, Egypt became a signatory to the WTO, committing the country to abide by the terms laid out in the WTO and other related agreements, including the General Agreement on Trade in Services (GATS). GATS mandated that the country thoroughly liberalize its insurance sector "to enhance predictability and provide transparency under the principle of progressive liberalization."[4] Several government officials interviewed noted that, in addition to the country's commitments under the SPR program, Egypt's commitments to comply with the GATS 2003 deadline as well as the stagnant growth of the sector were both significant driving forces behind the early reform effort.

Later the same year, the GOE issued Law 91/1995 initiating the privatization of the insurance sector by requiring public insurance companies to sell their shares in all joint venture insurance companies by April 1998. This provision had also been agreed to under SPR II, and led to another $10 million disbursement from USAID.

Under SPR III, the Egyptian government committed to reducing its share in at least one state insurance company to achieve private sector majority ownership. Another SPR III measure required the GOE to remove restrictions on foreign majority ownership of direct insurance companies. In 1998, Law 145 was passed, permitting the private sector to acquire up to 100 percent of the shares of the four public insurance companies and permitting non-Egyptians to hold top management positions. USAID disbursed $20 million in recognition of these achievements.

With the follow-on Development Support Program, efforts to liberalize the insurance market continued. Under DSP I, USAID agreed to disburse a total of $60 million once the GOE had drafted, approved, and begun to implement a time-phased action plan for reforming the insurance industry; performed valuations for the public sector insurance companies; achieved progress in implementing its plan to privatize the public sector companies; and reduced the compulsory 30 percent that insurance companies had to re-insure with Egypt-Re.

Committed to enacting these new reforms, the GOE requested that the Ministry of Economy and Foreign Trade and USAID collaborate to develop a program of technical assistance to support the MOEFT in fulfilling the above DSP agreements. The Reforming Insurance Markets project (RIM, 1999-2001) was designed to complement efforts being

[3] The SPR, a performance disbursement mechanism agreed to by the Egyptian and US governments supporting a series of reform objectives, was divided into three tranches: SPR I, II, and III.
[4] http://www.wto.org/english/news_e/pres97_e/finance.pdf

undertaken through the cash transfer agreements and to support the GOE in its efforts to continue to refine the legal and regulatory framework governing the insurance market.

In 1999 following a request from the Minister of Economy and Foreign Trade, RIM began by performing a comprehensive assessment of all aspects of current legislation, rules, and regulations pertaining to insurance, private pension funds, and private health insurance and its supervision. RIM advisors worked with the Chairman of the Egyptian Insurance Supervisory Authority as well as EISA's senior managers to identify "gaps" in the existing framework, and to provide recommendations to the Minister on how to bring both the Insurance Supervision and Control Law and the Voluntary Pensions and Retirement Savings Law in line with international best practices. Based on this assessment, EISA, with assistance from RIM experts, drafted amendments for the laws on insurance, private pension funds and private health insurance, and presented them to the Minister for his review. EISA officials also requested that RIM work with them to draft executive regulations of the pending laws to refocus EISA's efforts on supervision, rather than control.

Following up on RIM's contributions, the Modernizing Egyptian Insurance Supervision project (MEIS, 2002-2003) continued to provide technical legal assistance to officials in the MOEFT and EISA. MEIS experts responded to requests from the Chairman of EISA to submit model draft regulations on a number of key areas related to insurance, private pensions, and private health care insurance. MEIS and USAID staff met with EISA officials in collaborative working sessions to gather input, answer questions, and resolve conflicting opinions concerning provisions in the draft regulations.

As a result of these efforts, EISA succeeded in promulgating a number of regulations that enhanced EISA's efforts to monitor and supervise insurance companies and private pension funds and to protect consumers.[5] Several major accomplishments are of particular note. New regulations set a more prudent maximum interest rate for discount calculations for life insurance and retirement fund technical reserves; set premium rate-making standards for insurance companies; prohibited unfair trade practices; set high standards for claim-settlement practices; established a dispute resolution tribunal within EISA to assist policy holders; and established minimum requirements for all life and non-life insurance contracts. Furthermore, as part of the DSP II agreements, the GOE enacted effective anti-money laundering legislation, which led to a disbursement of $150 million. With these strengthened laws and regulations, new private sector companies began to enter the market, offering new products at competitive prices to Egyptian consumers.

3. ENHANCING SUPERVISORY PROCESSES OF EISA

As the insurance sector began to witness the entrance of new foreign and domestic providers and the introduction of new insurance products to the market, EISA management recognized that its earlier experience in regulating the insurance sector would need to be both broadened and deepened. EISA management and staff therefore worked with RIM, CLDP, and MEIS to develop new examination procedures, modernize

[5] See Section 5, Impact, for details on specific legal and regulatory reforms.

workflow processes, and equip staff with the necessary skills to carry out their duties in a competent and timely manner.

3.1 PHASE I: RIM & CLDP TECHNICAL ASSISTANCE IN ORGANIZATIONAL DEVELOPMENT (1999-2001)

Until the 1990s, EISA had operated for two decades as a holding company for the four public-sector insurance companies. With moves to liberalize the market, EISA's role had shifted to become a supervisor and regulator. EISA was in need of new rules, regulations, and procedures to carry out its new functions in order to be able to effectively support Egypt's liberalizing insurance market.

At the onset of RIM technical assistance, senior management within EISA worked with RIM to analyze the current organizational structure, staffing, and policies and procedures used by the Authority. This evaluation was performed to determine current practices, areas in need of enhancement, and issues of concern to management and staff of EISA. RIM held discussions and work sessions with management and staff members in all departments within the organization, and based on this critical review, identified several areas where processes and practices could be enhanced to allow for strengthening of the overall supervisory function.

3.1.1 Development of the Financial and Market Conduct Examination Manuals

The most critical need identified by management involved improving EISA's financial and market conduct examinations procedures so as to best monitor insurance companies' practices and assure their solvency. Techniques currently in place were labor-intensive and inefficient, as different departments would conduct separate analyses for each company at different points in the year. New formal procedures needed to be introduced to ensure that supervision was streamlined, consistent, and transparent.

RIM provided EISA assistance in developing two comprehensive procedures manuals – the Financial Condition Examination Manual and the Market Conduct Examination Manual – which incorporated the latest methodologies and techniques for effective financial and market conduct regulatory oversight. The responsible supervisors within EISA were actively involved in the drafting, testing, revision, and implementation of the chapters of the manuals, which helped to ensure that EISA management were committed to the changes. Furthermore, by identifying individuals within EISA to be responsible for specific sections of the manual, the process ensured that future revisions would be made when necessary, that training was provided to other staff members, and that the manual was appropriate for local conditions.

The process employed by RIM and the final products were lauded by EISA officials. According to the Chief Executive of Insurance and Reinsurance of EISA, the two manuals covered all major relevant topics required by his staff to carry out their supervisory functions, and when the manuals were later implemented under MEIS, they contributed to a much more effective process of company evaluation.[6] EISA's Deputy Chairman furthermore noted that this type of assistance that resulted in a tangible product utilized by senior management and staff was highly appreciated by the Government, and provided a "road map" to be followed in implementing new procedures.[7]

3.1.2 Training

While the examination manuals were being developed, RIM identified, with assistance from EISA management, areas of technical knowledge and operational processes for the development of a complementary training program. RIM conducted a number of interviews with EISA personnel as well as with other parties concerned with insurance disciplines, such as the Insurance Institute of Egypt, the Egyptian Society of Actuaries, university professors, and industry representatives. These informative sessions, a review of training EISA staff had received in recent years, and an overview of the current insurance market in Egypt provided the basis on which the training program was developed.

Training focused on enhancing supervisory procedures and on refining financial analysis techniques, and included courses on actuarial sciences, market conduct regulations, financial condition regulations, and reasons for insurers' failures. Training used actual case studies of insurance companies and pension funds in Egypt and emphasized evaluation techniques to understand the reasons for the changes and to determine if regulatory concerns existed. Training courses were given to all supervisory personnel to allow for additional cross-training between departments and to help build on the concept of an integrated supervisory approach. EISA staff additionally had almost daily interaction with RIM experts in informal meetings and impromptu discussion groups.

As a complement to RIM's in-house staff training, the USAID-Department of Commerce Commercial Law Development Program (CLDP) instituted a training and technical assistance initiative to further educate staff and top management on insurance regulation and supervision.[8] CLDP filled training needs "gaps" in two ways: through the provision of foreign experts (usually US Government officials) to carry out training programs in Cairo, and through study tours for EISA officials and senior staff to the US.

CLDP technical experts provided training to EISA officials on how a regulatory agency monitors health and life rates, insurance rate and form filing, and the principles of financial analysis. CLDP also sponsored study tours to provide an opportunity for MOEFT and EISA officials to study the American model of a privatized insurance market and to train EISA officials on elements of insurance supervision, including solvency regulation, financial analysis, on-site inspections, and public relations.

Study tours in particular were viewed as one of the most effective forms of technical assistance and staff development provided by USAID. Interviewees noted that the US-

[6] Meeting with Hosni Hamed Mohamed, 17 April 2005
[7] Meeting with Yahia Abdel-Ghaffar, 28 March 2005.
[8] CLDP was a USAID-Department of Commerce agreement executed by the US Department of Commerce.

based training courses were excellent, and that it was highly beneficial for them to have met and worked with U.S. government officials during these tours. Given that they largely perform similar functions and face similar problems, their advice was considered applicable and was respected by EISA staff. Working with these US government officials enabled training program and study tour participants to get to see their jobs in new ways, learn new tools or techniques for managing governmental work, and see just what it is they need to know to better carry out their duties. EISA officials also noted the importance of simply experiencing how the US insurance system operates and the efficiency of American insurance regulators.

As a result of these study tours, senior management came back with several new recommendations for EISA. For example, following a study tour comprised of two week internships for EISA employees with state insurance departments and related US insurance institutions, EISA officials requested that RIM develop the working manuals (discussed above) for conducting financial analysis and market conduct on-site exams to emulate the American examination process. Additionally, following a study tour to visit American insurance regulators, the Deputy Chairman of EISA noted that their exposure to American private retirement plans led EISA to place a greater emphasis on developing new retirement plans beyond simple defined benefit schemes, and to request input from RIM on alternative pension structures for the Egyptian market.

3.1.3 Developing a Public Awareness Program for EISA

A significant obstacle facing the growth and development of Egypt's insurance market was a lack of public awareness about what types of insurance are available, the specific products and services offered, the benefits of buying insurance policies, and the ways in which insurance helps mitigate risks facing businesses and families. In order to address these issues, CLDP assisted the EISA Public Relations Department to develop a public awareness campaign focused on increasing the "insurance culture" in Egypt.

In 2000, four members of the PR department visited the Insurance Information Institute (III) in New York City to learn how to deal with the media and how to manage public relations in a crisis. Later the same year, CLDP brought in campaign development advisors to assist EISA officials to devise a public relations strategy for EISA, which the Authority put in place. The campaign involved the development of a press kit, a brochure describing EISA's role, and flier inserts for Egyptian newspapers. EISA staff also received assistance from CLDP advisors to create and produce four commercials regarding EISA, life and non-life insurance, and the benefits of insurance for Egyptian consumers and businesses. CLDP responded to requests from EISA officials to follow up on these efforts by having an advisor travel to Cairo to determine the effect of the campaign and to highlight the next steps in increasing awareness of insurance.

As a result of this assistance, EISA PR staff reported that they have "transformed their relationship with the Egyptian media," and that they now feel more prepared to provide information to the media.[9] Furthermore, following up on advice from a CLDP public

[9] Interview with Iman Hamdy, Public Relations and Advertising Specialist, 17 April 2005.

relations specialist, the EISA IT department developed a web-based form enabling consumers to file complaints through the EISA website and via email, and EISA purchased a five digit "short number" hotline to respond to consumer questions and complaints.[10]

3.1.4 Data Management, Phase 1

A major determinant of the effectiveness of EISA's supervisory capacity involves the extent to which information technology is employed to make processes easier, faster, and more logical. RIM provided guidance to EISA to assist the agency in developing innovative IT solutions to improve data collection and the dissemination of information. When RIM began, financial reports, examination findings, and correspondence between the agency and the industry were collected and maintained primarily within individual departments and were paper-based. With EISA transitioning from a compliance agency into a supervisory agency, the Authority recognized that the ability of multiple staff across departments to access the same information was critical.

EISA management thus requested assistance to develop and implement a comprehensive computer database and information storage system in order to increase efficiency and better assure the integrity of the data. As a senior IT consultant within EISA noted, "data management and sharing was perhaps the most significant task the organization needed to undertake" to improve its performance as a regulatory entity.[11]

IT specialists within EISA collaborated with RIM IT experts to develop a plan, called the System Requirements Specification (SRS), for the creation and installation of an insurance regulatory database named the Insurance Supervisory Information System (ISIS) for EISA. To fulfill the goals of the SRS, EISA's IT team built the ISIS with RIM support. RIM experts procured for EISA certain new equipment and software, and arranged training for EISA staff who would be using the system on a daily basis, as well as for all EISA IT staff who would be administering the system. Once the first phase of ISIS was completed, CLDP brought in IT experts to work with EISA staff to review the status of automation and data collection at EISA, and to evaluate "next steps" in the process of ensuring successful implementation of ISIS.

The ISIS system electronically captures a wealth of information from regulated insurance companies and private pension funds. EISA utilizes the ISIS system as the basis for its comprehensive off-site review work, which enhances the agency's ability to proactively and effectively oversee the insurance sector and to have a thorough understanding of the risks within the industry and individual organizations. According to a review undertaken by a group of IT experts two years following the implementation of ISIS, the financial information contained within the database is "extensive," and with this system, "EISA is well equipped to conduct detailed and profound analysis consistent with best international practices."[12]

[10] The hotline telephone number is 19299.
[11] Meeting with Dr. Ragaii Hassan, 28 March 2005.
[12] Dr. Alex Brudno, "Electronic Archiving/Document Management System for EISA," October 2002.

Furthermore, as part of the implementation of ISIS, EISA officials drafted a decree on electronic filing with RIM assistance requiring insurers to submit required data to EISA not only in paper format, but in EISA-defined formats on specially marked diskettes. Decree 621 implemented in 2001 serves to relieve EISA of a number of administrative burdens and allows staff to focus more clearly on regulating and monitoring the insurance industry.

3.2 PHASE II: MEIS TECHNICAL ASSISTANCE (2002-2003)

Following progress made by RIM and CLDP in developing new supervisory procedures, training staff, promoting public awareness, and modernizing data management systems, MEIS was designed by USAID and the GOE to further strengthen EISA's ability to supervise and regulate the insurance sector. MEIS provided on-the-job training to EISA staff in the areas covered by the financial and market conduct examination manuals; implemented an actuarial training series to complement efforts begun by RIM; and further expanded EISA's utilization of IT solutions to supervise the insurance industry and streamline work processes between departments.

3.2.1 On-the-Job Training

With the successful completion of the examination procedure manuals and the follow-on training sessions under RIM, EISA management noted that staff continued to need assistance in implementing the new examination framework. In 2002, EISA requested that MEIS experts take a hands-on approach to training staff by actually conducting a number of financial and market conduct examinations in collaboration with EISA staff. This form of on-the-job training would serve to institutionalize new procedures that, up to this point, had been introduced "in the classroom," but not actually implemented on the ground. In these follow-on activities, MEIS focused on assisting in the full implementation of these new supervisory tools, enhancing the tools and techniques, and introducing increasingly complex methodologies.

<u>Financial and Market Conduct Examinations</u>

In order to assist EISA in upgrading its examination procedures for insurance and private pension funds, MEIS experts began by working with EISA department heads and staff to implement the Financial Condition and Market Conduct On-Site Examination Manuals produced by RIM. The first examination of the Suez Canal Insurance Company represented a "pilot" scheme, an attempt to establish revised procedures and processes for carrying out an examination of an insurance company. EISA had never previously conducted a risk-based analysis, and for the first time, the examination team comprised staff from all departments. [13] EISA staff led the process, while MEIS experts provided guidance and on-the-job training in the field with the examiners.

[13] Essentially, risk-based supervision is a pro-active method of analysis in which both qualitative and quantitative factors are utilized to rate a company's financial health. In the past, each department would conduct separate, uncoordinated exams at different times of the year, which increased the burden on the regulated companies and decreased the efficiency of EISA's work.

Utilizing the new techniques laid out in the manuals, participants and management were able to see for themselves the tangible benefits of the new supervisory procedures both in the quality of the reports produced as well as the efficiency gains made. Due to the planning and collaboration that took place prior to the actual field work, and to the new targeted "risk-based" methodology, the on-site examination was concluded with only two weeks of field work compared to previous examinations that took nearly 5 months. This new approach enabled field examiners to focus their efforts on identifying true weaknesses in the companies, and to prescribe curative measures to be taken.

Following this effort implementing the Financial Condition and Market Conduct Examination Manuals for an insurance company, EISA officials requested that MEIS work with them to develop a similar comprehensive manual for financial condition examinations for private retirement funds. MEIS experts worked extensively with EISA officials to develop a manual that would clearly define all aspects of the examination process by referring to internationally recognized "best practices" for evaluating private pension funds. The Financial Condition Examination Manual that MEIS and EISA produced is a comprehensive users' guide covering pre-examination planning, on-site examination work, and post-examination and follow-up work.

EISA, in collaboration with MEIS advisors, then field tested this manual during two examinations of large private retirement funds. With the new integrated and targeted examination methodology, the private fund examination procedures were also streamlined, taking only three days each instead of the previous average of three to four weeks.

In total, the EISA/MEIS teams conducted two on-site examinations of insurance companies utilizing the Financial Condition and Market Conduct Examination Manuals, and two on-site examinations of private pension funds utilizing the newly developed Financial Condition Examination Manual for Private Pension Funds. In order to ensure that all staff were trained in the new supervisory tools, EISA and MEIS sponsored Train-the-Trainers informal working groups and weekend sessions, in which staff who had participated in the joint EISA/MEIS exams then trained other colleagues to carry out targeted, risk-focused examinations. By the end of the MEIS activity, 20 staff had been involved in one or more on-site examination team utilizing the new methodology, and a number of additional staff had been trained by their colleagues to do so.

As a result of this new risk-based approach to analysis, EISA's ability to supervise insurance companies and private pension funds was enhanced, which contributed to improving the image of the Egyptian insurance market, and to protecting consumers. For example, in an unprecedented action, EISA revoked the license of an insurance company in 2001 because EISA's on-site financial condition examination revealed that its capital was impaired. Using the early-warning indicators developed under RIM and implemented under MEIS, EISA acted quickly to assist the company to realign its practices. Because of this quick detection and intervention on the part of EISA, the company was not insolvent and no policyholders lost money.

While the new examination methodology resulted in significant improvements in the quality of analysis and the time required to complete the exams during MEIS, EISA has faced challenges in continuing the new methodology with the end of the project. Some officials noted that, as the agency was moved from the Ministry of Economy to the Ministry of Planning, progress was delayed under the new leadership.[14] There are also indications that not all senior managers are convinced of the new supervisory techniques, and that EISA officials therefore require more hands-on demonstrations to see the new processes in action. With the shift to the Ministry of Investment in July 2004 and the new EISA chairman, officials have again begun to discuss how to implement the new supervisory tools first developed under RIM and MEIS. The outcome of these discussions remains to be seen.

Actuarial training

In an open market with competitive prices, EISA officials recognized that staff needed training in how to detect distortions in the market and how to identify insurers who were not maintaining adequate reserves. This was particularly true in the case of the non-life insurance industry, due to the fact that there were no casualty actuaries practicing in Egypt. EISA therefore requested that MEIS develop a training program in high-level actuarial and loss-reserving training for EISA staff.

MEIS advisors developed a series of training sessions on a diverse number of actuarial science topics for EISA insurance examiners, private retirements funds staff, and actuarial division staff. Actuarial training for insurance examiners and private funds staff entailed 13 weeks of courses on practical applications and uses of actuarial techniques for both off-site and on-site examinations. The topics covered life insurance and non-life insurance principles and the actuarial principles underlying loss reserving methodologies, review of premium rates, and reserve calculations for private funds. According to the Chief Executive of Insurance and Reinsurance of EISA, this was the first opportunity that most of the staff had to be introduced to the principles underpinning the technical reserve calculations for life insurance and for non-life insurance.[15] The Deputy Chairman further noted that prior to this, the private funds staff had received little training on how to analyze the actuarial reports prepared by each private fund utilized to establish the reserve for future retirement benefits.[16]

The staff of the EISA actuarial division also received several units of advanced actuarial training from MEIS advisors. Training topics included loss reserving techniques, actuarial mathematics, and actuarial valuation, among others. In order to provide hands-on experience to EISA actuaries, MEIS supplemented the training sessions with analyses of selected actuarial reports undertaken by the EISA actuaries under the guidance of MEIS advisors. In the process of reviewing these reports, it came to the attention of EISA management that unreasonably high interest rates were at times being utilized when performing present value discounting calculations. As a result of this analytical process,

[14] EISA was moved to the Ministry of Planning in November 2001.
[15] Meeting with Hosni Hamed Mohamed, 17 April 2005.
[16] Meeting with Yahia Abdel Gaffar, 17 April 2005.

EISA issued regulations that limit the rate of interest used to determine the actuarial reserves for life insurance and for private retirement funds.

3.2.2 Data Management, Phase 2

As noted above, EISA had made significant progress in modernizing data transfer processes between insurance companies, pension funds, and EISA through the introduction of the Insurance Supervisory Information System (ISIS) under RIM. MEIS followed up on these efforts by completing the second phase of automating EISA's data management system.

MEIS began by developing training sessions in consultation with EISA IT experts regarding the use of ISIS for internal financial analysis and for on-site examinations. This training was designed to refresh EISA staff on the basics of the ISIS system and to provide advanced training in how to put ISIS to work to facilitate their work functions. In order to demonstrate the actual use of ISIS in a real world application, the EISA/MEIS examination teams followed up the training by utilizing ISIS in planning the on-site examinations of the two insurance companies. In order to expand the application of ISIS, MEIS also assisted EISA staff to add reinsurers and insurance intermediaries to the system database. EISA additionally used ISIS to develop a uniform system to standardize the company accounting reports submitted electronically. MEIS provided technical guidance, and trained EISA staff as well as insurance companies on the new system and report format.

As a result of the successful implementation and utilization of ISIS, Egypt became one of the few jurisdictions in the world to have achieved 100 percent electronic filing of insurance company financial information. With ISIS and the electronic filing decree, companies were obliged to submit substantive, comprehensive financial statements to EISA on a quarterly basis. EISA management notes that due to ISIS, EISA is now able to perform more extensive monitoring than in the past, with a larger degree of efficiency and effectiveness.

4. IMPROVEMENTS IN THE INSURANCE SECTOR IN EGYPT

Egypt's insurance sector has witnessed dramatic changes since the onset of the GOE's liberalization efforts. From the 1960s to the late 1990s, the Egyptian insurance industry was characterized by a limited number of insurance companies offering a narrow range of products and services. The Egyptian insurance market was dominated by the four state-owned companies (one of which was the only authorized re-insurance company in the country) controlling over 90 percent of the market. The publicly owned Misr Insurance company alone accounted for approximately 50 percent of both life and non-life business.[17] Because of limited competition, there were few distinctions among product features, prices, and services.

[17] World Bank, "Arab Republic of Egypt: Country Economic Memorandum," Vol. 3, March 1997, p. 63

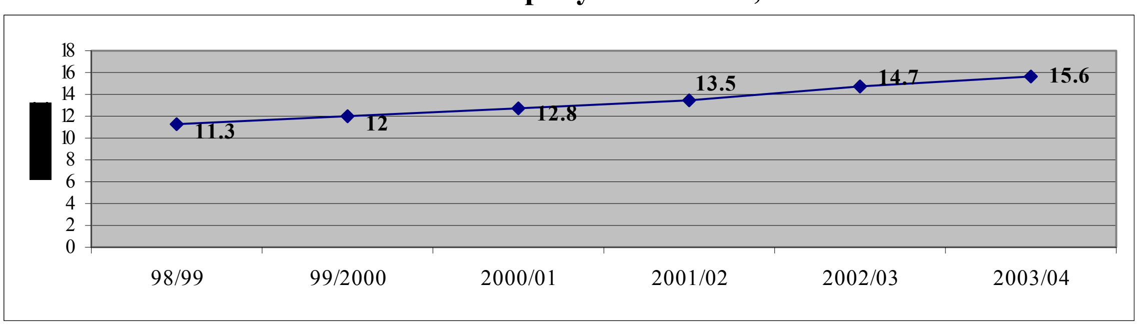
Following the legal and regulatory reforms enacted in the late 1990s, several major international insurers entered the market. These included Allianz, Legal & General (UK), Royal Sun Alliance, and the American International Group. Increased competition brought with it innovations in the design of insurance products, greater availability of products, better prices for products, better services to policyholders and better treatment of claimants.

By 2004, 16 private sector companies and one insurance cooperative society were operating in Egypt.[18] While the four major public providers remain large, their total market share has dropped from more than 90 percent five years ago to approximately 72 percent today.[19]

Several market indicators have also improved in recent years. Insurance premium growth has averaged 10 percent per annum over the past five years, compared to an average global increase over the same time period of about 2 percent.[20] Gross premium income in life and non-life rose from LE 1.9 billion prior to the implementation of Law 156 to LE 3.8 billion in 2004.[21] Shareholders' equity, in turn, now amounts to LE 2.9 billion, a 48 percent increase from 1998, and policyholders' rights have reached LE 11.6 billion, a 55 percent increase over the same period.

Shown below, insurance company investments have also expanded since 1998 by more than one third.[22] These increased investments have been largely channeled into government bonds, securities and shares, and fixed deposits, and have served to infuse much-needed capital into Egypt's financial sector.

Total Insurance Company Investment, 1998-2004



Source: EISA Annual Report, 2002-2003 and MOF Economic Monitor, April 2005

With the entrance of new competitors, employment has increased as well. The 16 private sector companies that have begun to operate since 1998 have created an estimated 3,335 new jobs in the sector, and prospects for future employment growth remain bright.[23] While overall employment in the sector grew only 2 percent in the past year, private

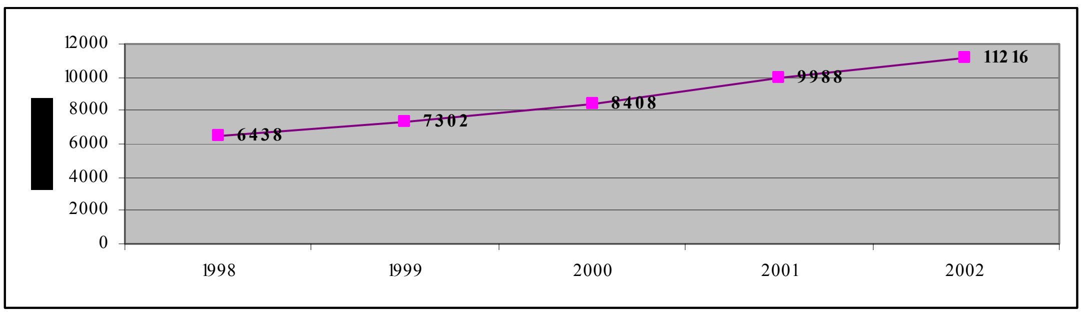
[18] World Economic Forum, "Reform of the Egyptian Financial Sector, Session II," 4/26, 2004.
[19] Market share here is defined as share of total insurance premiums. (American Chamber of Commerce, "Emerging Egypt, 2004")
[20] World Economic Forum, "Reform of the Egyptian Financial Sector, Session II," 4/26, 2004.
[21] Egyptian Insurance Supervisory Authority, Annual Report, 2003-2004.
[22] Egyptian Insurance Supervisory Authority, Annual Report, 2002-2003
[23] HORUS, "Special Report about Egypt Insurance Market & Economy, 2003." Issue 32, September 2004.

sector companies are leading the way in recruiting and training staff. For example, Royal and Sun Alliance, a British insurer, has increased its roster by 20 percent per annum since 2002 when it entered the Egyptian market, and the Deputy Chairman predicts that its demand for skilled staff will continue to grow at a similar rate as the company expands.[24]

The private pension fund market has also grown, from approximately 550 funds when USAID technical assistance began in 1998 to 614 in 2003.[25] With this expansion, the amount of domestic investment flowing into the financial sector from private funds has jumped by an estimated 75 percent, from LE 6.2 billion in 1998 to LE 10.8 billion in 2002.[26] These funds hold combined assets greater than either the life or non-life insurance sector, and amount to about 75 percent of the assets of the consolidated insurance sector.[27]

The value of pension fund reserves (asset accounts dedicated to the payment of pension benefits) has nearly doubled in recent years, reaching LE 11.2 billion in 2002.

Reserves of Private Pension Funds, 1998-2002



Source: EISA Annual Report, 2002-2003

4.1 BENEFITS TO INDIVIDUAL CONSUMERS

The entry of private sector insurance firms and the growth of private pension funds have resulted in tangible benefits to Egyptian consumers. Improvements include: enhanced insurance coverage, more opportunities for employees to save in retirement plans, enhanced consumer rights and protection, and enhanced product selection.

4.1.1 Enhanced Insurance Coverage

Prior to the entrance of foreign providers to the insurance market, Egyptian companies primarily relied on the large state-owned enterprises to provide insurance for their employees. The coverage of these public insurers was considered meager, and the process of claim payments was "at best dilatory and at worst non-existent."[28] Following sector reforms, more insurance companies began to enter the market, and market

[24] Meeting with Hassan Darwish, Deputy Chairman, Sun Alliance, 3 April 2005.
[25] RIM, "Assessment of Current Legislation, Rules, and Regulations Governing the Private Pension Sector," 23 November 1999.
[26] World Economic Forum, "Reform of the Egyptian Financial Sector, Session II," 4/26, 2004.
[27] HORUS, "Special Report about Egypt Insurance Market & Economy," June 2004.
[28] Barents Group, "MEIS Final Report," April 2003.

competition brought enhanced coverage, new products, and better customer service, all of which benefited local Egyptians.

As one example, USAID Foreign Service Nationals (FSNs) previously had their health insurance with the state-owned Misr Insurance Company, which was one of the few underwriters of health insurance at the time. In the late 1990s, new insurance companies brought much-needed competition to the market, and FSN coverage switched to a private sector provider. FSNs now have health coverage that provides 10 times the limit of coverage of the previous policy, eliminates the deductibles and coinsurance of the previous contract, and obviates the need of filing claims in most instances – all for the same price.[29]

4.1.2 Increased opportunities for employees to save

For many employees in the private sector, the present compulsory social insurance arrangements provide insignificant sums. These people require meaningful retirement benefits for themselves and their families. The Minister of Investment has noted that a central goal of the Ministry and EISA is to increase the number of employers providing supplemental pension benefits to their employees. The number of pension plans has increased in recent years, and a larger number of Egyptian workers now benefit from private retirement coverage.

Egyptians also now have the ability to open individual retirement accounts, independent of their employer. This measure, which had been proposed by RIM and MEIS advisors, permits all Egyptian workers to enjoy the benefits of tax-sheltered saving for retirement.

4.1.3 Enhanced Consumer Rights and Protection

In the past, when an insurance claims disputes arose, Egyptians had no recourse against insurance companies other than through expensive and protracted formal legal proceedings. With the introduction of the ombudsman mechanism first developed in collaboration between EISA and MEIS experts, policyholders may now seek a binding determination from EISA regarding the fairness of a claim settlement. Furthermore, the new unfair claim practices regulation issued by EISA circumscribes the ability of insurers to burden insureds unduly with continual demands for paperwork. Insurance companies may make only one request for documentation of the loss. If the policyholder complies with the request, the insurer has no legal ability to claim that the insured did not file a complete proof of loss.[30] The ombudsman mechanism and EISA's new regulations work together to ensure that consumer rights are protected, and that insurance companies honor their obligations to their clients.

With improvement in claims settlement procedures and customer service, the number of complaints registered with EISA and with insurance companies has decreased. From 1998 to 2003, the number of complaints dropped by 26.4 percent, from 158 to 125.[31]

[29] Ibid.
[30] Ibid.
[31] EISA Annual Report, 2002-2003.

Consumer protection has also improved with private pension funds. Following discussions with MEIS advisors, EISA prohibited the practice of permitting retirement funds to accord unfunded and unearned past-service credits. Prior to this, some companies had permitted influential persons to join the fund a year or two prior to pension age and receive credit for as many as 30 years of past service at retirement. This practice had the effect of "looting" the funds of the younger workers.[32] EISA's new practice serves to protect the benefits of all Egyptian workers who belong to private retirement plans.

4.1.4 Enhanced Product Selection and Innovation

Prior to market liberalization, insurance companies had few incentives to diversify the types of products offered on the market or to take into account a customer's actual needs when selling company products. At this time, companies focused almost entirely on raising sales of insurance products, while virtually ignoring consumer requirements and satisfaction.

The growth of the sector and the entrance of foreign firms into the market brought the introduction of new insurance products with innovations and improvements. According to the managing director of one private sector company, new insurers "studied the client base very carefully and divided them into different groupings, such as age, income, marital status, and designed policies to fit their needs." Targeting plans like this did not exist in the country's recent insurance past, and as a result of the reforms, new products are now offered that respond to the various and changing demands of consumers.

For example, new life insurance companies have begun to introduce investment-linked products, which combine investment plans with life insurance. In addition to expanding savings and investment options for Egyptian consumers, the introduction of enhanced life insurance products is also expected to spur significant increases in premium volume in coming years.

A second example is the new law on mortgage loans passed in August 2003, which stipulates that the mortgagor can be required to have a life insurance policy in force for the duration of the loan that makes the mortgagee the beneficiary of the policy. In response, the Egyptian Insurance Federation worked with EISA and the MEIS team to develop a specialized policy to meet the needs of mortgage applicants. Egyptians are now able to satisfy the new legal requirements when applying for a mortgage by purchasing a policy tailor-made to the type of coverage required.[33]

Finally, the newly liberalized market has also encouraged the development of alliances between insurers and banks. "Bancassurance" (merging banking and insurance) began in Egypt in 2001 led by Allianz Group Egypt. Bancassurance is the process by which bank branches provide both banking and insurance products through a single provider. It

[32] Barents Group, "MEIS Final Report," April 2003.
[33] Ibid.

includes consumer credit life insurance (mortgage or motor vehicle), retirement savings accounts, credit cards, and individual savings accounts. While still relatively new in Egypt, banc assurance has the potential to increase income, reduce fixed costs and expand the range of services provided by banks, while also enhancing the quality of marketing and increasing customer satisfaction.[34]

5. THE ROLE OF USAID ASSISTANCE

As indicated above, liberalizations to the insurance sector have led to a number of new market entrants, promoted greater competition, and benefited Egyptian consumers as a result. These improvements are due in large part to the strengthened legal and regulatory framework governing the insurance sector and to EISA's improved abilities to supervise insurance company behavior and ensure that consumers are protected. USAID assistance was an integral component to these improvements. Other donors were not involved in assisting the GOE in insurance reform during this time.[35]

The policy dialogue initiated by USAID and the GOE under the Sector Policy Reform and Development Support Programs helped to pave the way for reformers within the government to pursue their reform agenda for the insurance sector. By undertaking a specific set of regulatory reforms with the new 1998 Law and subsequent decrees, the Egyptian government received several million dollars in cash transfer payments under the SPR and later the DSP programs. USAID technical assistance under RIM, MEIS, and CLDP in turn provided the necessary technical expertise to government officials to implement agreed-upon reforms and to identify new measures in support of market liberalization.

5.1 USAID'S ROLE IN PROMOTING LEGAL AND REGULATORY REFORM

When USAID first began to collaborate with the GOE on insurance and pension reform in 1993 under the SPR program, the industry was hampered by heavy state control and dominated by publicly owned insurance companies. The GOE slowly began to improve the legal and regulatory framework governing insurance with Law 91 of 1995, which required public insurance companies to sell their shares in joint venture insurance companies. However, at this time, the government continued to heavily regulate rates for several classes of insurance, barred foreign insurers from operating in the market as majority shareholders, prevented non-Egyptians from being general managers, and placed high tariff burdens on all types of insurance which raised premium costs significantly.

In 1998, the GOE issued new legislation removing the 49 percent cap on foreign holdings for domestic insurers, abolishing the nationality stipulation for general managers, and allowing the privatization of public sector insurers. Tariffs on insurance began to be eliminated, and rates for all classes of insurance were deregulated, policy provisions that had been topics of extensive discussion by USAID under DSP and by the technical

[34] American Chamber of Commerce, "Banc assurance in Egypt: the first three years" February 18, 2004.
[35] The World Bank and the EU have both been in discussion with EISA management to develop training and technical assistance programs, but nothing has been instituted as of yet.

assistance teams.[36] These moves lowered rates and began to create price competition between companies. Other amendments in the law mandated that all insurance companies publish regular statements of their financial positions, approved by accredited financial auditors. These reforms also demanded that any new company wishing to enter the market must pass an economic needs test. The test helped to determine whether a company would introduce new instruments and thereby increase total retention in the market.[37]

After the promulgation of the new law, USAID and the GOE continued to work together to address remaining policy issues and to discuss strategies for further promoting market liberalization. Under the Development Support Program and the technical assistance packages of RIM and MEIS, a number of additional regulatory reforms were enacted. These reforms were due in part to collaboration between policy makers within the GOE and USAID in the policy dialogue process of the DSP, as well as to the technical support provided by RIM and MEIS experts to assist EISA to draft decrees, to follow international best practices, and to raise awareness of EISA officials of the importance of reform.

From 1999 to 2004, the government issued several executive regulations to increase market competition, enhance consumer protection, promote transparency of the market, and improve the efficiency of EISA supervisory operations. Each of these areas was discussed in length through memoranda and working sessions between the technical assistance teams and EISA, and several of the new decrees had been agreed to under the DSP.

In order to improve consumer protection, the GOE issued Decree 45 in 1999. The Decree stipulated rules of disclosure for insurance brokers, clarified the process by which claims and disputes with insurers were to be settled, and regulated the promotional and media activities of insurance companies. Ministerial Decree 599 issued in 2001 further enhanced claims settlement procedures by introducing an "ombudsman" mechanism to ensure fair prices for insurance products and by issuing guidelines to guarantee that insurance policy wording was clear and accurate. These measures had previously been discussed by EISA and RIM experts based on draft regulations submitted by RIM on Minimum Standards for Insurance Policies and on RIM's GAP analysis discussing unfair claims settlement practices.

Progress was also made by EISA in opening up the re-insurance market to private sector providers. When DSP and the RIM project began, each insurance company was required to purchase reinsurance from the state-owned Egypt-Re for an average of 30 percent of their revenues. Insurance experts assessed that these compulsory cessions to Egypt-Re were imposing a burden on insurance companies since it increased the portion of risk

[36] In June 2000, EISA removed the final barriers to non-competitive pricing practices by abolishing compulsory rates in fire and auto branches. At this time, all rates of insurance products became freely determined.
[37] American Chamber of Commerce, "The Insurance Sector in Egypt," *Business Studies Series*, August 2001.

remaining with the insurers and affected their investment portfolios.[38] This requirement also discouraged foreign reinsurance companies from participating in the Egyptian insurance market. Under DSP, the GOE agreed to gradually reduce these compulsory cessions and in 1999, the GOE issued Decree 105 mandating their elimination by 2003. Swiss Re and Munich Re are now the dominant non-Egyptian re-insurers, and are considered crucial by market insiders to providing much-needed expertise to Egyptian insurers, particularly on large commercial risk.[39]

EISA also enacted regulations in order to assist the agency to perform its supervisory and data dissemination roles more efficiently. Following work with MEIS on how to create transparency and bring bookkeeping practices up to international specifications, Decree No.157/1999 mandated that all companies follow new insurance accounting standards that meet with international standards. This measure had been agreed to under SPR II, and resulted in an $18 million disbursement to the GOE. This was followed by Ministerial Decree 621/2001 obliging insurance companies to submit financial forms to EISA in electronic format. According to the Senior Information Technology Specialist of EISA, the agency is now better able to monitor the industry through the complete computerization of filing for company financial statements and analysis.

The most recent regulations to monitor industry operations have involved GOE efforts to combat money laundering in the insurance sector, a policy provision that had been agreed to under DSP II. Ministerial Decree 15/2002 mandates that institutions transacting insurance and reinsurance take a series of precautions to ensure that no unlawful use of money occurs. In 2003, EISA followed up on this decree by issuing rules for combating money laundering in the Egyptian insurance market. As a result, in February 2004, Egypt's name was removed from the Financial Action Task Force (FATF) Non-Cooperative Countries list, and USAID disbursed $150 million to the GOE.[40]

A number of reforms are also on the agenda of the High Council of Insurance which have been submitted to Parliament and are awaiting final approval. RIM, MEIS, and the cash transfer programs had dedicated a significant amount of time to promoting many of these pending reforms, including:

- The reduction of insurance premium taxes from the highest rate of 21.4% by 5% each year to reach 5%;[41]

[38] Meeting of American Chamber Insurance Committee, "Globalization of the national insurance sector," May 2001.
[39] "Exploiting the Growth Potential of Emerging Insurance Markets: Swiss Re," *HORUS*, Fourth Year, Issue 34, February 1 2005.
[40] The Financial Action Task Force (FATF) is "an inter-governmental body whose purpose is the development and promotion of policies, both at national and international levels, to combat money laundering and terrorist financing… The FATF monitors members' progress in implementing necessary measures, reviews money laundering and terrorist financing techniques and counter-measures, and promotes the adoption and implementation of appropriate measures globally." http://www.fatf-gafi.org/document/45/0,2340,en_32250379_32236836_34313517_1_1_1_1,00.html.
[41] Taxes include 21.4% on the value of each property premium, 16.6% for marine cargo, and 4% on life insurance premiums.

- The utilization of risk-based capital methodology (which includes analyses of company investment, portfolio, and claims exposures) to assess the adequacy of a company's capital;
- Allowing corporate brokerage in direct insurance and reinsurance;
- The introduction of a new law which would subject medical insurance providers to oversight by EISA;
- The introduction of new compulsory liability insurance; and
- Revisiting the role of privatization for state-owned companies.

Furthermore, according to the Ministry of Investment (MOI), Law 54/1975 governing private pension funds is currently being amended, and is expected to be presented to Parliament by the end of the year.[42] The Ministry notes that the amendments to the law "aim at increasing the number of participants, encouraging long-term savings, and improving the asset management of the private pension funds."[43]

While the draft law under discussion is not available to the public, EISA officials have noted that the Proposed Private Pension Supervision and Control Law developed in collaboration with the RIM activity was a useful reference in developing the current draft amendments. It remains to be seen to what extent the amended law will incorporate the technical advice provided by USAID activities. However, the official "Action Reform Plan for the Egyptian Pension System" submitted by the MOI does reflect several recommendations proposed by RIM and MEIS. This includes: promoting transparency and accountability in fund management; encouraging the informal sector to join the formal sector through the introduction of more incentives; permitting private financial intermediaries and institutions to manage funds; and promoting both defined benefit and defined contribution plans.

5.2 USAID'S ROLE IN STRENGTHENING EISA

USAID's capacity building assistance to EISA has in turn resulted in a more effective and efficient agency with a more clearly defined regulatory role. EISA department heads and private sector insurance companies agree that with USAID support, EISA has developed a more systematic approach to dealing with the insurance industry, and that the workload has decreased on the part of both EISA and the companies as processes have been made more efficient. With the introduction of the ISIS data management system and electronic filing during the RIM project, insurers can quickly generate the required information to be submitted to EISA, EISA staff spend less time distributing, collecting, and filing documentation, and the amount of paperwork is significantly reduced. Likewise, with standardized accounting systems implemented with MEIS assistance, EISA spends less time conducting both off-site and on-site examinations, and insurance companies have clear guidance on what the system requirements are to ensure full compliance. One measure of the improved efficiency of the Authority is the fact that, while the number of private funds has increased from 550 to 614 and the number of insurance companies has increased from six to 20 since the late 1990s, EISA technical

[42] EISA was moved under the jurisdiction of the MOI in July 2004.
[43] Egyptian Ministry of Finance, *The Economic Monitor,* April 2005.

teams have been able to manage the increased workload and submit their reports on time without hiring more analysts.[44]

With technical support from the RIM and MEIS teams, EISA has also strengthened its ability to identify new consumer needs as the market expands. As noted in section 4.1 above, EISA has: introduced an ombudsman mechanism to assist consumers with claims disputes; enabled Egyptians to open individual retirement accounts; prohibited retirement funds from granting unfunded and unearned past-service credits to individuals; and developed specialized policies to meet the needs of mortgage applicants following the new 2003 mortgage law. Each of these new provisions was developed by EISA following technical assistance from RIM and MEIS experts.

As recommended by MEIS, the government has additionally expanded the role of the EISA, now the highest supervisory board responsible for regulation.[45] This has placed further responsibility on EISA management to ensure that work processes are as efficient as possible. In consultation with the Supreme Council of Insurance, EISA determines which companies are permitted to enter the market, monitors reserve adequacy and insurance company solvency, and conducts on-site audits and year-end assessment of loss reserves. In a recent review of the insurance sector in Egypt, the World Economic Forum noted that the insurance regulatory and supervisory system employed by EISA is now "observant of most of the core principles of the International Association of Insurance Supervisors (IAIS). Minimum capital levels are high, and the reserve requirements imposed by EISA are adequate."[46] Furthermore, according to the Deputy Director of a private sector insurance firm in Egypt, EISA "now supplies the necessary regulatory and supervisory presence to ensure the operation of the insurance sector on a competitive basis."

No less important is the noticeable change in attitude among much of the staff and agency management following the RIM and MEIS on-the-job training programs. It bears repeating that EISA had acted as a holding company of the public sector insurance companies for years, and had only relatively recently begun to significantly modify its supervisory procedures prior to the commencement of USAID assistance. The executive chairman of one private insurance company noted that "EISA is now more supportive and encouraging of a more competitive, expanded insurance and pension market… [EISA leadership] acknowledges the benefits of a liberalized insurance market, and is committed to change."[47]

[44] In contrast to many public agencies where overemployment is the norm and excess staff have few responsibilities, EISA examiners had already had a significant workload, with each fund examiner responsible for examining an average of 36 funds per year. With the increase in the number of funds, each examiner is now responsible for 41 funds. (Meeting with Dr. Ragaii Hassan, 17 April 2005, and MEIS, "Comments on On-site Examination Report for Private Pension Funds").
[45] Meeting with Yehia Abdel Gafar, 17 April 2005
[46] World Economic Forum, "Reform of the Egyptian Financial Sector, Session II," 4/26, 2004.
[47] John Metcalf, Executive Chairman of Arab International Insurance Company, quoted in "Change of Image for Egyptian Insurance," *The Japan Times*, April, 2002.

6. AREAS FOR FUTURE REFORM

The insurance and private pension funds markets in Egypt still have huge potential for growth. Insurance premiums account for 1.4 percent of GDP (up from 0.7 percent in 1998), which is still far below the regional average of 5 percent and the global average of 7.5 percent.[48] And while total investments of the insurance industry have increased significantly over the past five years, they continue to amount to only 3 percent of GDP. Additionally, EISA reports that 7.5 million workers now have private retirement accounts, which equals an increase of 134 percent over the past five years.[49] While this is an impressive improvement, it still leaves an estimated 13.21 million workers with no private retirement savings.[50]

The primary obstacles to growth include the tax system, as reflected in the large tax levied on premiums paid to insurance companies and the low deduction amounts for retirement contributions, the stalled privatization effort, and a lack of public awareness on the importance of insurance and private long-term savings instruments.

6.1 LEGAL AND REGULATORY REFORM

Liberalization has already resulted in the introduction of a number of private insurers and private funds, improved products, and enhanced customer service. However, there is still a need for the government to continue to work on improving the insurance sector's legal and regulatory framework to match the challenges of foreign competition and new entry in the market by the private sector.

6.1.1 Privatization

While the government has announced plans to privatize the publicly owned insurance companies and has commissioned valuations and due diligence by international investment banks and actuaries, privatization has not been achieved. And while its share of the market has declined in recent years, state-owned companies continue to dominate the insurance sector. This is largely due to the fact that 70 percent of market agents and brokers work for state insurers; most lucrative governmental accounts go to the state insurers (representing a large portion of the market)[51]; and the strong financial position of the state insurers.[52]

[48] American Chamber of Commerce, "Firms on Shaky Ground," *Business Monthly*, February 2005.
[49] Data from EISA, Private Pension Funds Department. There are indications that this figure may be inflated. In 1998, RIM and EISA calculated that 3.2 million workers had private retirement accounts. EISA's current calculations indicate that this number has more than doubled to 7.5 million in the last five years. However, as noted previously, the number of funds has increased by 12 percent. Unless the previous funds dramatically increased the number of employees covered, and/or the new funds cover a massive number of employees, the figure of 7.5 million may be an overestimate. Breakdowns of these figures by fund could not be attained by the researcher.
[50] The CIA World Factbook estimates that there are 20.71 million workers in Egypt. (http://www.cia.gov/cia/publications/factbook/geos/eg.html).
[51] For example, Misr Insurance is known for signing major aviation contracts with EgyptAir, while Al Chark leads in insuring massive engineering and petroleum contracts.
[52] HORUS, Issue 32, September 2004.

These public companies are characterized by "weak internal governance, poor management, and a lack of performance incentives."[53] They are saddled with bloated payrolls, inefficient staff, and mountains of paperwork that makes it difficult to determine outstanding liabilities exactly. Furthermore, valuations are complicated by the insurance firms' extensive holdings in public sector industries and their massive real estate holdings, which distort the companies' values. All of these factors contribute to hindering privatization.

There are also some indications that state companies are pricing premiums at levels too low to cover actual risks, relying on their investment portfolios to cover losses.[54] With the deregulation of tariff rates, several of these companies may lack the required experience to assign rates that reflect the true market value. Additionally, because state employees receive bonuses based on sales, some may be tempted to sell ill-formulated policies at below cost to close as many deals as possible.[55] Not only does this imply that these public companies run the great risk of defaulting on any large claim, but that incentives for foreign investors to enter the market are reduced due to anti-competitive practices.[56] Implementing sound insurance policies to correct these practices could potentially free up greater assets for investment in the economy, since experts note that a large portion of investment income is lost in order to pay for "slip-ups" in the insurance portfolio of these public companies.[57]

The government needs to give up its role as the sector's primary owner and regulator. In order to privatize these companies, considerable restructuring is likely required. State companies must implement modern management systems and eliminate most of the excess workforce. The GOE may therefore need to design and implement early retirement programs and the companies will need to retrain some of their staff. Furthermore, public sector companies should consider following the banking sector's lead in appointing private-sector managers to head operations.[58] Many analysts argue that privatizing management would be the first move towards introducing real change.[59] It would also be useful for public insurance companies to separate problematic accounts and non-insurance related assets such as real estate portfolios.

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[53] World Economic Forum, "Reform of the Egyptian Financial Sector, Session II," 4/26, 2004.

[54] Public insurance companies are "first and foremost investment brokers, bringing in huge amounts of income for the government, which is then reinvested in government bonds, securities and shares, fixed deposits, and real estate" (American Chamber of Commerce, "Emerging Egypt 2004").

[55] Interview with the General Director of a private sector international insurance companies operating in Egypt.

[56] For example, in January 2004, Al Chark insurance became the subject of international attention when Flash Airlines crashed into the Red Sea, killing 148 people. Al Chark, the insurer, announced that each victim's family would be entitled to $350,000, which would run into billions of Egyptian pounds. The quality of Al Chark's reinsurance and its ability to fulfill its obligations are still unclear following the crash.

[57] American Chamber of Commerce, "Emerging Egypt 2004."

[58] Egypt-Re is the only public company with private management in place.

[59] American Chamber of Commerce, "Emerging Egypt 2004."

6.1.2 Tax System

The premium taxes placed on all types of insurance are prohibitively high, and are a significant obstacle to the growth of the insurance market in Egypt. Taxes include a 21.6 percent on the value of each property premium, 16.6 percent for marine cargo, and 4 percent on life insurance premiums. This is compared to an international average tax rate of 3 to10 percent.[60] According to EISA and the Supreme Council of Insurance, this issue will be addressed in Parliament before the end of the year, with recommendations to gradually reduce the taxes over the next three years.

In the area of private pension funds, the maximum tax exemption for contributions has not been raised since 1975. Long-term savings can accumulate more quickly with an adequate system of tax incentives and other rewards. The GOE is under discussion to increase exemptions, which have reportedly been included in the draft pension law recently submitted to Parliament.

6.2 CAPACITY BUILDING FOR EISA

Significant progress has been made in improving the efficiency of EISA's work processes and in strengthening staff ability to adequately supervise the sector. Additional emphasis, however, is needed to ensure that comprehensive, formal procedures and processes across the agency are in place, and that coordination between departments continues to improve.

MEIS developed an effective model of on-the-job training which should be expanded upon. EISA management notes that staff continue to need hands-on skill development in conducting financial analysis and market conduct examinations. Furthermore, actuarial staff require additional advanced-level actuarial training.

EISA, and the larger Egyptian market, are also in need of a greater number of qualified actuaries in the country, particularly in non-life insurance. There are currently only six qualified and licensed actuaries in Egypt, most of whom are above 60.

6.3 PUBLIC AWARENESS AND OUTREACH

Despite the broader base of insurance products offered today, Egyptians buy less insurance than most other emerging countries in the region and far less than countries with mature economies. Egyptians spend an average of less than $9 per person per year, compared to $37 for emerging markets in general and $387 globally.[61] Additionally, less than 1 percent of Egyptians have life insurance.

These low figures imply that individuals and corporations are exposed to higher risks, and that they are incurring a large opportunity cost by not channeling their funds into investment instruments with reasonable yields. Moreover, corporations are also under-insured even against basic risks like fire, theft, and property damage.

[60] Ibid.
[61] World Economic Forum, "Reform of the Egyptian Financial Sector, Session II," 4/26, 2004.

While CLDP initiated the process in 2000 with the development of written materials and commercials, the materials need to be updated and the commercials are no longer running due to financial constraints. EISA now needs to establish a comprehensive awareness program to inform citizens of the importance and benefits of insurance and how they can make use of different insurance coverage matching their level of income and perceived risks. Insurance products are viewed by many Egyptians as not permissible for religious reasons. Furthermore, clients in search of a policy are largely uninformed and buy almost exclusively based on price without being aware of what is and is not covered under the policy. EISA needs to develop strategies to improve consumer awareness and knowledge of the benefits and risks of insurance products and pension funds. Similar efforts should be done on the corporate level to inform local companies about the need to hedge against typical business risks.

7. CONCLUSION

Following USAID assistance, the Egyptian Insurance Supervisory Authority is better equipped to monitor the market and protect consumers, and the legislative and regulatory framework has strengthened. The Egyptian insurance market has opened up to private insurers, increased the number of private pension funds, and benefited Egyptian consumers. Insurance premiums have grown an average of 10 percent per year since the promulgation of the 1998 law, 16 private sector insurance companies are now operating in the market, and the number of private pension funds offering retirement plans to Egyptian workers has increased by 12 percent. Market liberalization and greater competition have brought greater innovations in product design, greater availability of products, better services to policyholders, and better treatment of claimants. The USAID cash transfer programs and technical assistance packages were important elements to assisting government officials in EISA to implement agreed-upon reforms and to identify new measures in support of market liberalization.

In addition to USAID's contributions to furthering the policy dialogue and implementing reforms, progress was also due in part to Egypt's international commitments under the WTO. When Egypt became a signatory to the WTO in 1995, policy makers were aware of the importance of WTO membership and Egypt's obligations to abide by the terms laid out in the General Agreement on Trade in Services (GATS), which mandated that the country thoroughly liberalize its insurance sector.[62] Failure to comply with GATS could result in the suspension of concessions extended to Egypt by other WTO Members under GATS or other WTO agreements, and could have serious effects on Egypt's ability to renegotiate the terms of its international debt. Several government officials interviewed noted that the country's commitment to complying with the General Agreement on Trade in Services 2003 deadline was a significant driving force behind the early reform effort.

It is also important to note that neither the country's WTO commitments nor USAID assistance would have by themselves led to significant reform without the presence of policy reformers within the Ministry of Economy and Foreign Trade and EISA who were intent on developing and promoting new measures to open up Egypt's insurance sector.

[62] http://www.wto.org/english/news_e/pres97_e/finance.pdf

Indeed, several amendments in the 1998 law were not a prerequisite for applying the GATS' requirements nor for complying with the SPR agreements, but were rather introduced "out of the government's belief that they are necessary for adjusting the economy to adapt to the global open market policy, attracting foreign investment and expanding the capacity of existing in-country financial enterprises."[63] A meeting of the American Chamber of Commerce Banking, Finance, and Insurance Committee noted that "the recent legislation aimed at privatizing insurance markets indicates that the Egyptian government does not stop with its proposed commitments under the GATS, but surpasses these commitments by far."[64]

There remains an incredible amount of growth potential for the insurance and private fund markets. Additional legal and regulatory reforms are needed to address constraints presented in the tax system and encourage privatization of the public insurance companies. And while EISA's ability to regulate the sector has improved, assistance is required in ensuring that formal procedures are in place across the agency and that staff are adequately trained, particularly in actuarial sciences. The Egyptian market as a whole is also in need of a greater number of certified actuaries, and the development of actuarial science programs in local universities or new training institutes may be effective in expanding the pool of local professionals.

New reformers brought into the government in 2004 have heightened the optimism of experts and private companies. Reforms addressing many of the above concerns are now under discussion in the Ministry of Investment and EISA, and are slated to be presented by the end of 2005. As competition increases in the insurance sector, Egyptian consumers stand to benefit from better products, prices, and services; the financial sector will receive greater infusions of investment capital; and the economy as a whole should strengthen. The ability of the insurance sector to fulfill these expectations now depends in large part on the government's ability to continue to push through reforms in support of a vibrant, liberalized, market-driven insurance sector.

[63] American Chamber of Commerce, "Liberalization of financial services: Egypt's commitments under GATS," April 20, 2004.
[64] American Chamber of Commerce, "Egypt's Financial Liberalization and the GATS," 2003.

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