

MAXIMIZING FINANCE FOR DEVELOPMENT IN EGYPT'S ENERGY SECTOR

ESMAP support to the Government of Egypt was important in reducing energy subsidies, which paved the way for World Bank Group investment on broader sector reforms. The World Bank Group's comprehensive, programmatic support helped the government to transform the energy sector into a sustainable, and well-managed market that was attractive to private sector investment.

After the Arab Spring, the Government of Egypt was facing growing fiscal pressures. Energy was underpriced, fossil fuels subsidies had increased dramatically, and the government had built up arrears to international oil companies. The country had transitioned from an energy exporter as recently as 2009 to an energy importer by 2014. The power sector could no longer meet the demands of a growing population, resulting in severe power shortages—up to six-hour long outages during the summer months.

subsidies were largely benefiting upper income groups and amounted to more than the combined expenditures on social protection, health, and education. Cost recovery in the sector was only 30 percent, forcing power utilities to operate at a loss. Representing nearly 7 percent of the Gross Domestic Product (GDP), one of the highest in the region, the subsidies were discouraging much-needed investment in the power sector.

Energy subsidy reform became a strategic and pressing priority for the Government of Egypt.

WORLD BANK GROUP AND ESMAP AGREE TO SUPPORT LONG-TERM REFORM EFFORTS

Generally, energy subsidies are meant to assist the poor, but often disproportionately benefit the wealthy, who own houses, run air conditioners, and operate personal vehicles. Egypt was no exception. High fossil fuel

ADDRESSING WASTEFUL ENERGY SUBSIDIES

Energy subsidies had been relied on by Egyptians for decades, so attempts to reduce or remove them would be politically sensitive. On the request of the government, the Energy Sector Management Assistance Program (ESMAP) rapidly mobilized technical resources,



"Targeting the subsidies in the right way equals good education." *From Government of Egypt campaign collaterals.*

providing data and advice for reform and capacity building to various ministries following a cross-sectorial and phased approach.

During the first phase of technical assistance, ESMAP provided assistance for a simulation of alternative scenarios, including estimated direct and indirect impacts of different subsidy reform options. This modeling convinced the government that subsidy reforms could be implemented without causing disastrous inflation or economic recession. A forward-looking plan for pricing and impact management was prepared with policy development options. This support informed the ambitious fuel and electricity reforms implemented by the government in July 2014.

ESMAP's US\$20 million Energy Subsidy Reform Technical Assistance Facility was set up in 2013 to help countries remove fossil fuel subsidies while protecting the poor. ESRF provides technical assistance to governments, develops tools for assessment and decision making, and facilitates knowledge exchange for a global community of policy makers.

Building on this initial engagement, ESMAP's Energy Subsidy Reform Technical Assistance Facility (ESRF) provided on-going support to the Egyptian government on subsidy reform decisions. The assistance focused on strengthening the government's capacity to model fuel price reforms, developing an evidence-based communications strategy, and strengthening social protection mechanisms to mitigate the impacts on the population and ensure sustainability.

For the poorest Egyptians, fuel purchases constituted 12 percent of household expenditures, which meant that the removal of energy subsidies was going to have the greatest adverse effect on them. In a significant reallocation of public spending, the fiscal savings resulting from the 2014 reform of energy subsidies—which had been reduced from approximately 7 percent to 3 percent of GDP—were redirected toward social spending. In 2015, for the first time, spending on health and education surpassed spending on energy subsidies.

An ESMAP report helped make the case for strengthening social safety nets to mitigate the impact of energy

subsidy reforms on the poor, underpinning the design of the US\$400 million World Bank Strengthening Social Safety Net Project. ESMAP technical assistance to the Ministry of Social Solidarity helped to modernize the management information system (MIS), giving the government the ability to implement a targeted social protection program by directing cash transfers to the most vulnerable. The successful Takaful and Karama programs, which offer both conditional and unconditional pensions, cover more than 2 million households—reaching 9 million Egyptians, almost 88 percent of which are women. By 2018, spending on social protection for the poorest 20 percent of the population had doubled, and subsidies began to target those groups that needed them most.

SUBSIDY REFORMS SPARK BROADER CHANGE

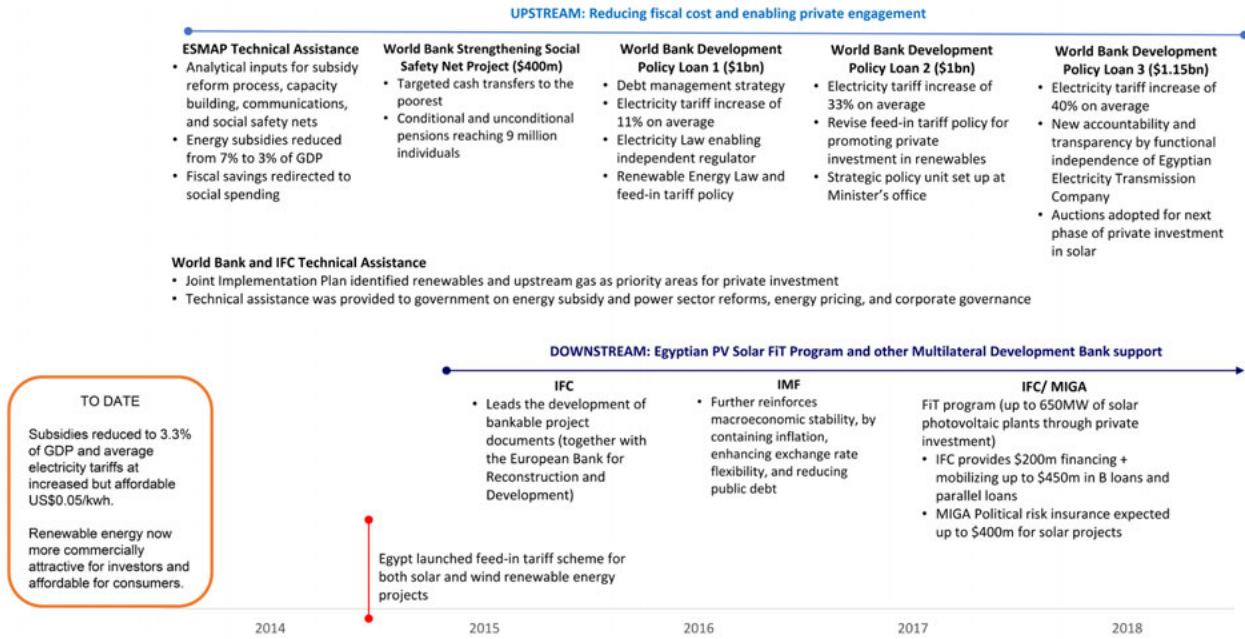
The subsidy reforms laid the groundwork for a broader dialogue on how to rebuild the economy amid macro-economic and social vulnerabilities. The World Bank stepped in with a package of loans that supported the government in further reducing energy subsidies, restructuring the electricity sector, and promoting private sector investment in renewable energy.

ESMAP analysis and technical assistance aided the government in developing a five-year tariff plan for electricity, pricing reforms for fuel, and a new gas law, which formed the basis for key aspects of the three-year, multi-billion-dollar, multi-donor loan series. The international package—worth a total of US\$3.15 billion—was



Source: <https://www.worldbank.org/en/news/video/2018/03/05/us315-billion-program-supports-egypt-with-improving-the-economy-and-creating-jobs>

Transformational Change to Egypt's Energy Sector



Source: Arab Republic of Egypt Energy Sector: Maximizing Finance for Development in the Energy Sector (World Bank Case Study). Amended for this publication.

financed in parallel with the African Development Bank (AfDB) and the Agence Française de Développement (AFD).

The subsidy reforms also became a part of a three-year, US\$12 billion extended arrangement with the International Monetary Fund (IMF) to restore macroeconomic stability and promote inclusive growth. The program worked to liberalize the foreign exchange rate, encourage investment, implement structural reforms that promoted inclusive growth, increase employment opportunities for youth and women, and further strengthen social safety nets by increasing spending on food subsidies and cash transfers.

CROWDING IN PRIVATE SECTOR FINANCING

The World Bank's programmatic approach, coupled with the government's effort to encourage investment in renewables, helped create a financially viable sector and opened the door to private sector investment. To develop a more favorable climate for investment, the government introduced new renewable energy laws and established regulations for competitive bidding for independent power producers. The timing was perfect—aided by

rising international oil prices, the subsidy reforms had maximum impact. The rising fuel prices were making renewables more competitive. Without subsidies, Egypt's utilities had to reduce their losses and were now seen as credible partners to private sector investors. Renewable energy was now more commercially attractive for investors and affordable for customers.

The government worked closely with the International Finance Corporation (IFC) to assemble nine international banks that invested for the first time in Egypt's renewable energy sector. A US\$653 million private financing package—the largest for a solar photovoltaic plant in the region—was approved for the construction of 13 solar power plants as part of the Benban Solar Park.

The Benban Solar Park is helping Egypt to realize its solar energy potential, curb its carbon footprint, and reduce its reliance on fossil fuels. It will generate up to 1,650 megawatts of cost-effective and eco-friendly power for over 350,000 homes and create 6,000 local jobs. In addition, it will help eliminate 2 million tons of greenhouse gas emissions a year, the equivalent of removing about 400,000 cars from the road.

The World Bank Group's Multilateral Investment Guarantee Agency (MIGA) engaged directly with investors

“Egypt is a clear example of how targeted reforms can spark improvements across the entire sector. Phasing out fossil fuel subsidies and modernizing laws fostered the market confidence needed to bring in private capital.”

Riccardo Puliti, Senior Director, Energy and Extractives Global Practice, World Bank Group

in the solar park project with the offer to mitigate the noncommercial risks and provide an additional level of comfort. MIGA is providing US\$210 million worth of political risk insurance to private lenders and investors involved in the solar park.

More than US\$15 billion in private investment has been mobilized in the gas sector and US\$2 billion in the renewable energy sector, reducing the government’s fiscal expenditure by US\$4 billion annually. These savings are being reinvested in Egypt’s social programs. Today, in addition to the two new cash transfer programs, the food subsidy has been increased by 300 percent to provide food security to the country’s poorest, and the school lunch program is now able to feed significantly more children.

COMMUNICATING EFFECTIVELY WITH THE PUBLIC

Communication and outreach are important factors in the successful implementation of subsidy reforms. Informing public opinion builds trust and consensus. ESMAP provided the Government of Egypt with a comprehensive communications strategy, based on stakeholder analysis,

that helped to shape the positive narrative around the ongoing subsidy reforms. Using video clips for social media, advertisements for radio and television, and roadside billboards the Egyptian government successfully raised awareness about the cost of the existing subsidies and the benefits of the reforms.

MAXIMIZING FINANCE FOR DEVELOPMENT

ESMAP support to the Government of Egypt on energy subsidy reform was a catalyst for change. Analysis and technical assistance led the way for comprehensive World Bank Group support that helped the government to transform the energy sector into a sustainable and well-managed market that has improved access to services for those who need them most. Capacity building, partnerships, public communications, and private sector financing were brought to bear to create an energy market in a fiscally, environmentally, and socially sustainable way that will better meet the needs of the Egyptian people.



“I am against wasteful subsidies. I am with improvement and development.” *From Government of Egypt campaign collaterals.*

ESMAP MISSION

The Energy Sector Management Assistance Program (ESMAP) is a global knowledge and technical assistance program administered by The World Bank. It provides analytical and advisory services to low- and middle-income countries to increase their know-how and institutional capacity to achieve environmentally sustainable energy solutions for poverty reduction and economic growth. ESMAP is funded by Australia, Austria, Canada, ClimateWorks Foundation, Denmark, the European Commission, Finland, France, Germany, Iceland, Italy, Japan, Lithuania, Luxembourg, the Netherlands, Norway, the Rockefeller Foundation, Sweden, Switzerland, the United Kingdom, and the World Bank.