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CASE STUDY

Middle East • Egypt

GiroNil: Building A Payments Highway in Egypt

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Sector • Basic Accounts

Enterprise Class • Foreign company/MNC



Executive Summary

GiroNil presents an interesting case of offering banking services to the under-served population of the Egyptian economy. Since 2004, the local banking and financial sector has undergone significant reform¹ and is looking to expand their reach to larger segments of a 90% unbanked market potential. A largely cash-based economy indicates that the banking sector could be more efficient in its role to attract and hold a larger number of bank deposits and thus stimulate Egypt's economic growth.

Similar to other emerging markets, certain challenges have led to a lag in banks' investment towards providing adequate financial products and services to capture low-income segments of the market. Fragmented and risk-averse, the structure of the local banking sector consisted of institutions working in closed systems servicing a small customer base of wealthy individuals and corporate accounts. Therefore, the focus on developing retail banking products targeting poor, low or middle-income customers was excluded. Serving low-income customers is a different initiative that looks to profit from including high-volumes of low-value financial transactions, as in the Egyptian context. Since it is difficult and costly for a single financial institution to effectively process transactions occurring at a rate of millions per day, partnering between institutions to create an inter-banking infrastructure or network is a solution to capture this high growth business potential.

GiroNil was established in January 2005 in Cairo, Egypt, as a joint venture, a public-private partnership of local and international banks and financial institutions, such as ING. The company piloted closely with local banks and large institutions to develop and implement a shared cashless (giro) payment system. Largely based on their investments and business model, in April 2010, GiroNil was selected by the Central Bank of Egypt, to co-develop the national Automated Clearing House for Egypt.

As part of their work on national payment systems, GiroNil now looks forward to developing mobile banking and microfinance solutions to offer more inclusive financial products and services in the future. With a fully functioning ACH, they estimate the system could process up to 2 billion transactions per year by 2017.

¹ Through privatization and consolidation, reducing public sector banking market share.



Introduction

Described as “*one of the best deals to happen for Egypt in 2010*”² the co-development of the national Automated Clearing House (ACH), by the Egyptian Banks Company (EBC) and GiroNil Egypt, has made a breakthrough this year. The EBC and GiroNil are technology providers building the electronic network that officially went live in June 2010 when the Central Bank of Egypt (CBE) and all 38 banks operating in the market were successfully interlinked. This joint effort marks the development of appropriate financial infrastructures for a ‘cashless society’ vision for Egypt.

As a nation-wide payment system³ the ACH has specific capacity to process large volumes of multiple credit and debit transactions in batches (or bulk transfers). According to the CBE’s Payment Systems Department, the ACH system will handle small (and retail) value payments, increasing the use of cash substitutes, particularly electronic (SMART) cards. The CBE is targeting to issue over 12 million debit cards for salary, pension and other government service payments over the next three years. By the end of 2010, a fully functioning ACH is expected to take developments to the next level introducing systems that process micro-payments to offer products such as mobile and bill payments.

Commitment to structural adjustments, increased technology and the formation of new partnerships are changing the financial landscape in Egypt and has begun to alter how the banking sector views the value of lower income market segments. Getting onboard the ACH process would provide banks (and companies) in Egypt with a significant source of new business, investment leverage and product innovation in their outlook for growth. The ACH and ensuing micro-payments systems imply enhancements in the quality of life for millions of Egyptian citizens across socio-economic segments, whether they are currently included in the banked or unbanked population.

The process of technological systems development is also largely dependent on simultaneous renovation of partnerships, business vision and strategic management practices. Together with the EBC, GiroNil’s collaborative success lies in effective transfer of business knowledge, as well as technical financial tools. Also, as a national, high-stakes business venture, accessing a potential financial market of more than 50 million consumers in Egypt, the negotiation of roles and responsibilities of stakeholders is fused with long term investments in building trust – between institutions and restoring confidence in the overall Egyptian financial sector.

² El-Bayoumi, 2010, Interview.

³ According to the Bank for International Settlements (BIS) a Payment System is “a set of instruments, banking procedures and, typically, interbank funds transfer systems that ensure the circulation of money.” (Farakallah, 2009)



Market Context

Egypt is fundamentally a cash-based economy⁴, where cash is used in 97% of all transactions in the Egyptian market. About 90% of Egyptian citizens are unbanked and manage their finances outside formal banking institutions. As one analyst summarizes “*while Egypt has a number of ambitious players operating in its market, it is worth noting that these banks only serve 10% of the 75 million residents. This is a figure that has remained unchanged for a few years. The remainder of the population is too poor to bank. This creates the need for private sector banks – to offer financing solutions for low-income individuals.*”⁵

Typical to emerging markets is the situation where the banking sector started by catering to the corporate segment and a small (usually up to 10%) segment of wealthy private individuals in society. “*It seems that banks are not interested in having low-income consumers as customers, because they think they cannot make any money out of them.*”⁶ Historically, the inertia stems from banks’ strategies to make mostly corporate sales, the ‘lower hanging fruit’ or easily accessible banking business. Many start to find that in order to grow, banks have to look to lower-income segments of the market. For this reason current products and processes of the banking sector are not flexible enough to develop more inclusive products and services at this time.

Meanwhile, demand for financial services from the majority of the population is unmet. For example, out of the formal salaried workforce of 23 million people, 97% of them get paid in cash.⁷ Only 4% (around 3.2 million people) have a debit card.⁸ A costly monthly challenge arises as millions of employees in large public sector companies and institutions turn into crowds of people spending time queuing to collect their salaries. It takes an Egyptian household on average, 35 hours or about one full working week, per month to run cash payment errands.⁹

A macro-economic consequence of excluding access to banking services for the large share of the population is the low rate of bank deposits¹⁰ and accounts, creating a challenge to Egypt’s rate of economic growth which “*is slowed and is well below attaining its potential.*”¹¹ As banks increase checkable deposits they also increase the number of loans they can give to those who need them, to start small businesses or for other investment opportunities. The use of cashless payment systems, such as electronic cards, effectively reduces the cash economy by encouraging people to pay money into bank account deposits. From the point of view of

⁴ 70% of the basic money aggregate money supply (M1) is cash (van Rijn, 2006, p.4)

⁵ Marroushi, 2008.

⁶ van Eersel, 2009, Interview.

⁷ Al-Ahram Weekly, 2004

⁸ Zawya, 2008, (figure is a 2007 estimate).

⁹ van Eersel, 2009, Interview

¹⁰ 29% deposits rate (vs. 71% in currency circulation) in Egypt (CBE, 2009)

¹¹ van Rijn, 2006



The World Bank, having an efficient payment system was recognized as “a prerequisite for realizing sustainable economic growth and social development in emerging countries.”¹²

There are payments systems established in Egypt, all owned and operated by the CBE¹³, developing themselves, over more than 10 years¹⁴, to satisfy key characteristics of international standards, in compliance with the core principles for systemically important payment systems (CPSIPS).¹⁵

Table 1- Payment Systems in Egypt Established or Under Construction – By Value of Payment

Payment Value	Type of Payment System	Types of Financial Products and Services
Large Value Payments	RTGS (Real Time Gross Settlement)	High value Direct Credit Transactions only
	CSD (Central Securities Depository)	Cross-system transfer of securities
Retail Payments	ATM/EFT POS Switches	Debit card, e.g. “123”, “Cirrus” ATM inter-networks
	ACH (Automated Clearing House)	Direct Credit Transactions: Payroll (private and government), Pensions (private and government), Government Supplier Payments, Social Security Payments, Dividends, Money transfers and Corporate-to-corporate payments. Direct Debit Transactions: Utility, Credit card bill, insurance, Mortgage installment loans and Corporate-to-corporate payments.
	CCH (Checks Clearing House)	Funds transfer, Corporate-to-corporate
	Remittance Systems	Money transfer
Micro-Payments	Mobile Payment	Money transfers through mobile phones
	Bill Payment	Bill payments through mobile phones

Source: Central Bank of Egypt, Payment Systems Department (2009), Faragallah (2009)

Among many functions distinguishing the ACH from the recently launched Real Time Gross Settlement (RTGS), is the ACH’s use of processing high volume-low value transactions (e.g. pensions, remittances, and utility bills) and its target to reach the unbanked in the market. Similar to a toll station on a motor highway that increases revenue as more cars use their

¹² Wolfensohn, James D. Previous President of the The World Bank.

¹³ Banking Law No 88 (2003) Article (6)

¹⁴ With the assistance of the World Bank, International Monetary Fund and the EU on various projects.

¹⁵ Drafted by The Bank for International Settlements (BIS), an international organization fostering international monetary and financial cooperation and serving as a bank for central banks.



transport infrastructure, the ACH payment highway thrives on the number of transactions processed by their system, which increases, as more of the un-banked population is included.

When time came for the CBE to implement the national ACH, it looked to the state-owned Egyptian Banks Company (EBC) as the appropriate entity to build the technical infrastructure, as well as to own and operate the system. The EBC was established in 1997, founded by 18 local banks, to supply technical development to banks, in third party processing services¹⁶. The company began its challenging search for vendors of ACH systems globally. ACH models need to be designed to the specifics of a country, through long-term partnerships and very few vendors exist on stand-by.

When presented with GiroNil's business model and their understanding of the local market, EBC had found the opportune technical partner. As EBC Managing Director Mr. Mohamed El Bayoumi recalls, "*GiroNil was already in the Egyptian market, with five years of experience, their work being very close to the ACH concept, and have an excellent source of know-how and value to offer...*"¹⁷

Since 2005, GiroNil has pioneered the concept of a nation-wide payment system and introducing their business model to banks. They invested in the piloting and successful launch of an electronic payment processing network linking their founding partners Banque Misr, the Commercial International Bank (CIB) and Egypt Post. However, efforts to get all banks onboard their network and license to be the national ACH in Egypt, limited GiroNil's capacity to be a fully functioning payment system. But with the turn of events in the last few months, GiroNil's prospects in the Egyptian market is taking a sudden up-turn, a benefit to their early and patient investment. As EBC's chosen supplier, GiroNil's vision, management approach and technical solutions underlying their business model is making returns.

GiroNil Business Model

GiroNil offers easy, convenient (right-around-the-corner) access to basic financial services to all members of society throughout Egypt. By using post office outlets as financial transaction centers, a familiar outlet (location, staff, close to home/work) is now a gateway to important financial services. Egyptians (especially in remote rural areas) can own bank accounts, pay regular utility bills, receive salaries and in the future make money transfers using Giro products and services. To provide banking services to the poor, GiroNil is building a common network among financial institutions to make it happen.

FORMING GIRONIL EGYPT

In the history of relationships behind GiroNil's establishment is the initial invitation extended by Banque Misr¹⁸ to Inclusion Group, in 2002. Inclusion Group¹⁹, a financial institution based

¹⁶ A gateway or middleman between two processing banks or vendors

¹⁷ El Bayoumi, 2010, Interview.

¹⁸ One of the largest Egyptian public sector banks.



in Hoofddorp, Netherlands, “initiates and develops projects that contribute to the sustainable development of the financial sector in emerging markets.”²⁰ Banque Misr had called upon Inclusion Group’s services to assess how to make better use of their ATM²¹ network, which was only accessed by a very small base of workers in private corporations, wealthy individuals, tourists and business-travelers. Apart from an infrastructure (distribution) challenge, a main reason for limited use of ATM was that only a small proportion of the Egyptian public had a bank account. Profitable investment from the ATM payment system required the bank to expand their current banked client base.

While consulting with Banque Misr, the idea to establish GiroNil came from ING, a Dutch financial institution working in the payment industry for more than 40 years in Europe. At the time, Mr. Frans van Eersel, present Managing Director of GiroNil Egypt recalls, ING had advised their Egyptian partners to build a mass payment infrastructure as “it was and still is believed that payments are crucial if you want to include the banked and un-banked into one model.” In addition, ING and Post Bank²² developed a model recognizing the potential of post office networks to get into payments and banking. They promoted their idea to countries like Brazil²³, Algeria and Egypt. Egypt’s Ministry of Communication and Information Technology (MCIT) was showing the right signs in ICT developments that would be the basis for the technology that ING’s model required.

Local partners signed a Management Agreement with Inclusion Group and a Shareholders Agreement for the incorporation of the joint venture.

Table 2- Founding Members of GiroNil Joint Venture and Their Roles

Name	Type of Institution	Role in GiroNil Venture
Banque Misr	Local Public Bank	30% founding shareholder and member Brings customer base
Commercial International Bank (CIB)	Local Private Bank	30% founding shareholder and member Brings customer base
Egypt Post	National Postal Network	30% founding shareholder and member Brings retail network and customer base
Inclusion Group	International Financial Institution	10% founding shareholder and investor Brings business model & management expertise
Interpay	International Payment Processor	Transfer application of technology & know-how
FMO	International Development Bank	Investor
Dutch Bank for	International Bank	Investor

¹⁹ Inclusion Group – “A bank account for everyone”

²⁰ Inclusion Group, <http://www.inclusiongroup.nl/index.php?m=98>

²¹ Automated teller machine

²² Postbank and ING Bank later merged into one brand called ING, launched in February 2009.

²³ Bradesco Bank won the bid to work with Brazil’s Postal Network and “is known as a show case example of the potential of the postal network.” (van Eersel, Interview, 2009).



Development		
MIBC Group	Local Financial Consultant	Financial Advisor

Source: GiroNil Interviews, Factsheet (2009)

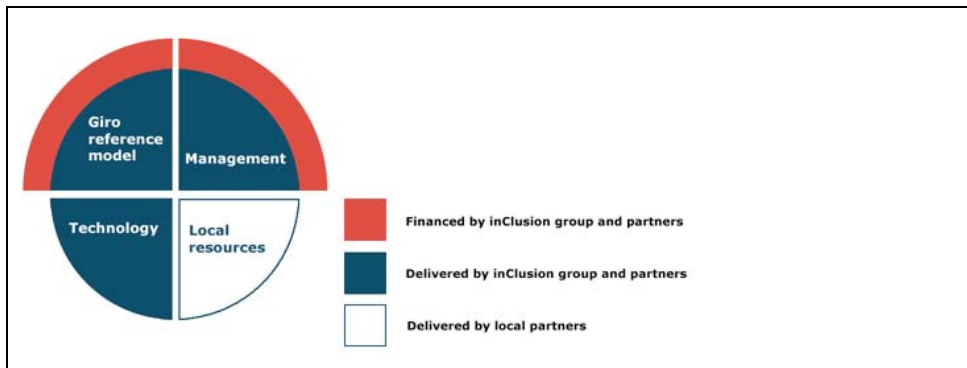
Banque Misr, Commercial International Bank (CIB)²⁴ and Egypt Post each hold a 30% stake in GiroNil Egypt. Inclusion Group invested a 10% stake and together with FMO a Dutch investment bank they jointly take a share in the joint venture. To bring an Egyptian payments system into operation a task force developed a business plan cooperatively, to establish an automated payments processing infrastructure. GiroNil Egypt is Inclusion Group’s first giro venture outside the Netherlands. By stipulating their shareholder status in the venture, Inclusion Group commits itself fully to the business. On the other hand, based on agreements with local partners, an exit may be exercised between the fourth and the sixth year of GiroNil’s operations.²⁵

According to their feasibility research, GiroNil planned to focus on three products in automated processing: Payroll, Remittances and Bill Payments.²⁶ By 2014 it was envisioned that 20 million Egyptian citizens would use the infrastructure they were planning to build.

STRUCTURE AND FEATURES OF THE BUSINESS MODEL

Inclusion Group structured the business model and invests in transferring knowledge and software to their local partners. Local partners may invest money and their customer base in the model. Inclusion Group’s management experience is meant to minimize the risk associated with implementing the new business initiative.

Diagram 1- Inclusion Group’s Business Model has Four Essentials



Source: Inclusion Group website, 2009 at <http://www.inclusiongroup.nl/index.php?m=31>

²⁴ CIB is one of the largest private sector banks in Egypt.

²⁵ Inclusion Group, 2006, p. 3.

²⁶ Full product range Annex-Table 3



The Giro Reference Model: Financial Inclusion and Giro Payments System

The blue-print for building a giro joint venture was supplied by Inclusion Group. They delivered what they call a reference model, which contains the concepts and methods to implement giro payments in the market.

Inclusion Group's corporate vision reflected in their strap-line 'A bank account for everyone' comes with a core belief that "*access to basic bank accounts [is] fundamental to daily life*", *providing identification, basic payment transactions, cost savings, access to loans and mortgages, and inclusion in the formal society.*"²⁷ A guiding ideology of their business model is that they also have a "*very profound ethical and social world view driving the company: building trust in the financial sector is a key ingredient for socio-economic development.*"²⁸ By building a network between banks, they are also trying to build trust between banks and ultimately in the Egyptian financial sector overall. Inclusion Group plays the role of an enabler and catalyst in projects that contribute to the sustainable development of the financial sector.

There are two types of payment methods: exchange and provision. Exchanging is to change cash based on a known fixed price. Provisioning is to transfer money from one account to another.²⁹ In provisioning, a third party must be involved. Giro or giro transfers are a method of payment that can be described as a 'credit transfer' (payment by transferring ownership of bank deposits) or as an electronic direct deposit payment. Giro is mainly used in banking for regular periodic payments like taxes or utility bills. With a giro payment, the payer hands the payment order directly to his own bank, which then makes payment to the recipients' bank. After the payment has been received, their bank notifies the payee. In GiroNil's model, they take on the role of the third party processor in provisioning payment.

Management

One of the critical success factors of the venture is the transfer of expertise to local management teams and employees. Inclusion Group delivers the key management staff and giro specialists from Holland to Egypt to grow their Giro joint venture. A Management Agreement is signed between Inclusion Group and local partners at cost plus for a period of three to four years.³⁰ Members of the founding organizations represent the GiroNil Egypt Board of Directors: Banque Misr, CIB, Egypt Post and Inclusion Group. In daily operations, having the right management teams is a key to building the venture.

Technology

²⁷ Inclusion Group website, accessed July 2009.

²⁸ Inclusion Group, 2006, p.1

²⁹ Debit cards, credit cards, money transfers, ACH (Automated Clearing House) are all electronic payments. Mobile phone payments would also fall into provisioning payment methods.

³⁰ Inclusion Group, 2006, p.3.



GiroNil processing center (Photo credit: Pascale Nader)

The technology behind the high volume transaction processor would come from Interpay Nederland, a processing company owned by Dutch banks.³¹ This includes software and processes for document and payment processing. The two main systems software for the GiroNil payments processing platform are delivered by Eqens - owned by leading German, Dutch and Belgian banks, which is one of the largest and most advanced automated Clearing Houses in Europe with over 10 billion transaction per annum.³²

Technology is offered by Interpay on a 'Pay-as-you-Grow' pricing structure to implement the system. This cost model means companies don't have to pay large capital upfront for IT capacity they may need in the future.

Operational since 2007, the infrastructure team at GiroNil's processing center collaborated closely with Inclusion Group's management team to implement the technology behind the payments system for Egypt. They fundamentally work step by step to adapt the Dutch payments model to the characteristics and operations of the Egyptian financial sector. Mr. Karim Fahim, Infrastructure Manager at GiroNil, explained a few aspects of the hybrid system: *"The Dutch model came with structures, for example in daily operations, and we learnt step by step that we have to change it to work according to the Egyptian model. You can say we have the Egyptian model beside the Dutch one both working on the same software now....Every implementation has its own characteristics to adapt to, it would be difficult to install something directly in another country and for it to work as is."*³³

GIRONIL INFRASTRUCTURE AND NETWORK

"Our model depends on post office outlets and banks that we are connecting and GiroNil is somewhat in the middle of the whole chain that works around us."

Frans van Eersel, Managing Director GiroNil Egypt

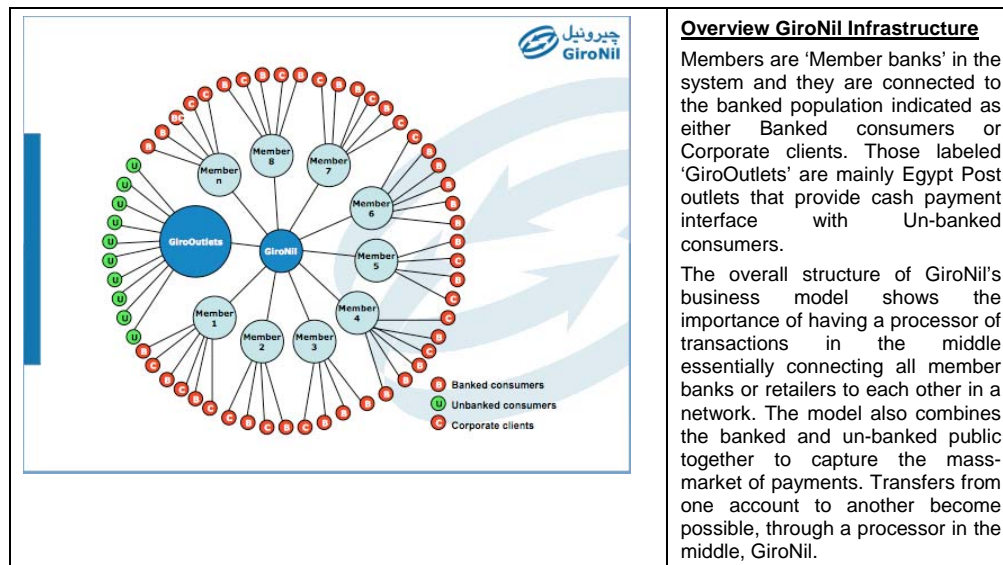
³¹ Inclusion Group, Press Release.

³² GiroNil, 2008, p. 2.

³³ van Eersel, 2009, Interview.



Diagram 2- Overview of GiroNil's Infrastructure: The Hub For Payments,

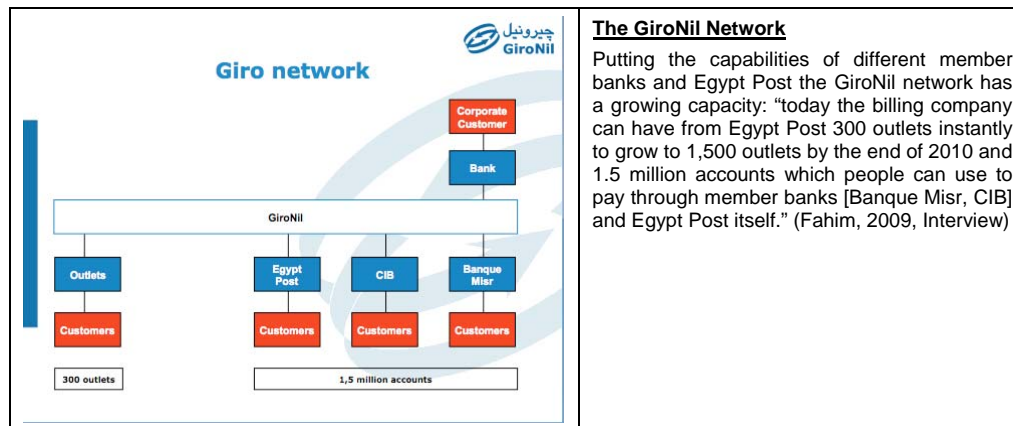


Whether the payments being exchanged are salaries, bills, pensions or money transfers, GiroNil's role is to collect cash payments and to start an electronic credit transfers (or giro) system between members of the network. GiroNil becomes the payments processing hub for all members of the network. With an identification card, a user can go to a giro post office outlet, and enquire about all his/her outstanding bills and invoices. Egypt Post now has the computer systems to go into the network and have that person's information available on-screen. This paperless, electronic capacity is made possible by GiroNil's server at its processing center where Egypt Post outlets are connected.

With the inclusion of the Post's outlets within the network, when Telecom Egypt (a billing company) signed onto the GiroNil network, they immediately increased their capacity of 100 cash collection outlets to 300 outlets (Giro Post office outlets). Egyptian citizens of all income levels in urban, rural and remote locations can increasingly access financial services that influence critical aspects of daily life, like having electricity and receiving pension payments.



Diagram 3- GiroNil's Network Size and Structure



GIRONIL PRODUCTS PORTFOLIO

GiroNil's infrastructural network links together the transaction capabilities of banks, postal outlets and companies by streamlining and standardizing their processes to form a common payment network. For each type of money transaction, or payment, such as a salary or telephone bill, a different network scenario and Giro-branded payment product is created.³⁴

Table 3- GiroNil Payment Products Portfolio

Payment Product Name	Product Type	Product Description
Operational		
GiroAccount	Current Account	The basic bank account issued by member banks of GiroNil.
AcceptGiro	Bill Payments	By signing the AcceptGiro paper form attached to the bill
BusinessGiro	Salary & Pension Payments	Salary and pension payments into GiroAccounts.
MCIT cash payments at Egypt Post	Bill Presentment	Business to Consumer; A company bills its customers and receives payment electronically through the internet.
DirectGiro	Fixed and Variable Payments	Fixed standing order for periodic transfers.
CorporateGiro	Corporate Payments	Business-to-Business transfers.
Available, not operational		
TransGiro	Remittances	Person-to-Person transfers between GiroAccounts.
CashGiro	Services	Withdrawals and deposits of cash from and to GiroAccounts.
Eurogiro	Remittances	International transfers via Eurogiro network (in Euro).
Under Development		
MobiGiro	Mobile Payments	Person-to-Person transfers between GiroAccounts.

³⁴ Annex: table 1: GiroNil payment products portfolio

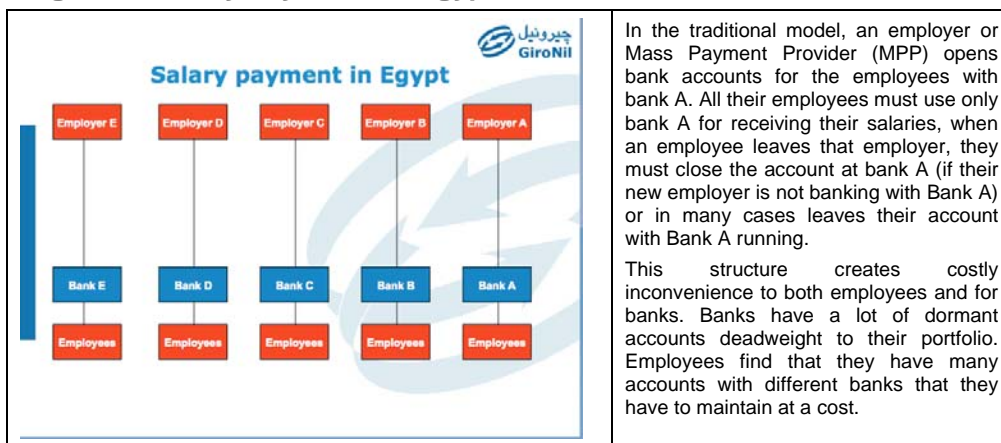


Source: GiroNil Presentation (2009), GiroNil Factsheet (2007)

The Example of Salary and Pension Payments: BusinessGiro

One example of large volume transfers occurs between large companies (or institutions) making mass payments to individuals, mainly employees on their payroll or pensioners. These companies are termed Mass Payment Providers (MPP) by GiroNil. In Egypt, MPPs typically pay the majority of their employees in cash, but even when electronic payment is used it usually takes place through ‘closed systems’ instead of through a payment system that works with many banks.

Diagram 4- Salary Payments in Egypt

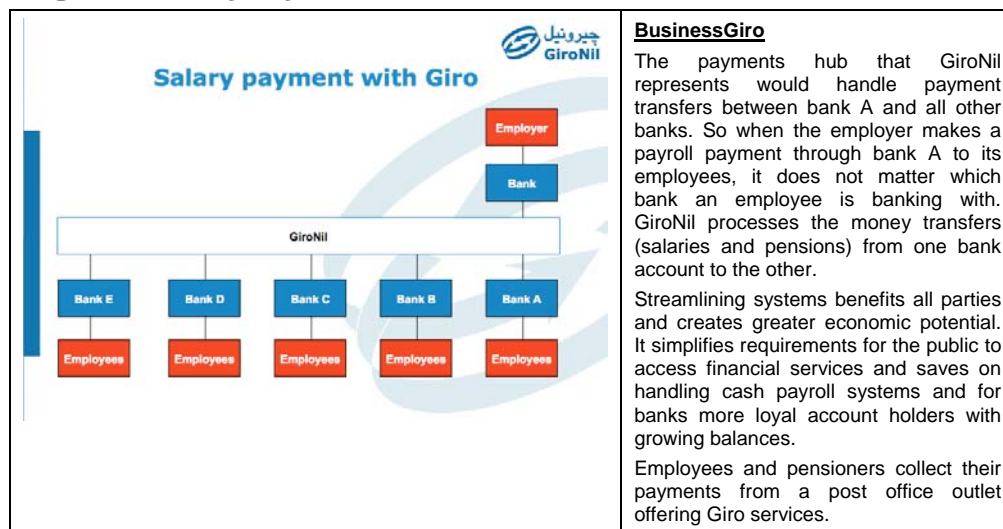


If all banks operating in Egypt join a shared network through a payments hub such as GiroNil, it allows for better handling of high volumes of salary transfers. Saving low-income individuals time, cost and offering them the convenience (and a saving mechanism) of an electronic bank account. Through their payroll payment product called BusinessGiro, salary and pension payments go into the GiroAccount where they are processed on their system server. The size of this segment is estimated at 20 million salaried customers and 4 million pension³⁵ recipients per month.

³⁵ Egypt's national pension plan covers 80% of the working population, the highest rate among developing countries. Government employees, military personnel, public and private enterprise employees and social assistance programs for special groups and in the informal sector are all included in the country's pension structure. At the start of 2009, total assets under the management of private pension schemes were at US\$4.3 Billion. (OECD, 2009, p. 1 - 4)



Diagram 5- Salary Payments with GiroNil with BusinessGiro



Tailored Products: Virtual Account for Syndicates

By the end of their first year of operations in 2007, GiroNil's Processing center discovered a specific product need in the Egyptian unbanked market. Public syndicates make payments to large numbers of members in the lowest income brackets and the poor in the market. Some syndicates needed an electronic payment product called a 'Virtual Account' held on GiroNil's network.³⁶ Out of their total payments in salaries to people over time, syndicates transfer part of these payments to the virtual account, while part of them continues to be paid to the employee in cash as normal. This gives greater convenience and access to financial services to employees. People can go to a bank or giro Egypt Post office, present identification, and receive payment from the syndicate's virtual account held on GiroNil's server.

THE FINANCIAL MODEL: A TRANSACTION-BASED PROFIT STRUCTURE

The business gains are considerable for investors who have both the vision and the patience to see through their investments in infrastructural phase of the network. The financial mechanics are based on processing large volumes of transactions on bills, salaries and remittances. For every bill payment, a transaction fee US\$0.09, is paid by the biller. Part of that fee goes to the credit bank and part of the fee goes to the debit bank (or the Post Office) and part of it goes to GiroNil. Processing payroll is more of a commercial deal. A bank may choose not to charge the transaction fee to the company to gain access to valuable new customers for retail products such as accounts, loans or credit cards, from a company's large employee base.

From 2005 to the time the enterprise achieves break even in the market, they would have invested approximately US\$18 million in network infrastructure.³⁷ Managing Director of GiroNil Egypt, Frans van Eersel, sees this investment in the context that "*this is the same*

³⁶ Fahim, 2009, Interview.

³⁷ van Eersel, 2009, Interview



amount it would cost to build 2 km of motor highway in Europe. So we are creating a payment highway for that amount of money...for a system that, according to our research studies, will have a stable impact on the economic growth of Egypt.”

Challenges and Solutions

THE REGULATORY ENVIRONMENT

It was always GiroNil’s objective to build what they call ‘the clearing house of Egypt,’ however, without a license to operate the national payment system; GiroNil’s growth to achieve its goal was limited. Egyptian laws and regulations related to payment systems³⁸ stipulate that the Central Bank of Egypt may exclusively perform the oversight of payment systems in Egypt. The CBE therefore awards licensing to banks or third parties payment system operators and the services they provide. These regulations led to the establishment of the Payment Systems Department (PSD) within the central bank placing more focus on the development of the national payment system starting with the ACH.

A series of other laws, such as the executive regulations of electronic clearing houses, and the proclamation of laws concerning digital signature, reflect the intentions of the CBE to take greater initiative in developing national payments systems. The most recent being that the Central Bank of Egypt issued a decree, mandating all banks operating in Egypt to connect to the ACH network by 1 June 2010.

In addition, in early 2009, the Central Bank and the Egyptian Ministry of Finance both took controlling share (27% each) of the EBC, the state-owned company developing payments systems locally, and designated the EBC as operator of the development of the ACH. EBC is now majority-owned by the national government and no longer has free hand to sell shares to private investors. EBC implements the policies of the CBE in building financial market infrastructures and does not play the third party processor role nor sell financial ACH products to banks to avoid a larger monopoly situation.

Engaging in Policy Dialogue

As a commercial entity, it was unlikely for GiroNil to be appointed the operator of the ACH payment system, as their management stated *“instead the CBE decided that it would be better for Egypt, and I think they are right, that they would step in behind [the development] and make it mandatory to all banks to become a part of an ACH.”*³⁹

GiroNil began concessions with EBC and the CBE, and the presentation of their work in Egypt led the Central Bank to support GiroNil’s initiative to add value to the local banking sector. Mainly due to their demonstration of their business model, early investment and

³⁸ Specifically Article(6) in The Banking Law No.88 of 2003

³⁹ van Eersel, 2010, Interview.



experience gained from five years of piloting and operating in the market. GiroNil has entered into an agreement with the EBC to co-develop the ACH infrastructure together. GiroNil was selected by the EBC to also play the role of the third party processor, developing and selling products to banks that would allow them to use the ACH system more rigorously.

INFRASTRUCTURE

While GiroNil had managed to successfully build an infrastructure connecting banks and post office outlets, the size of the network was still a limitation. Only the two founding banks, Banque Misr and CIB, out of 38 operating banks, were in the GiroNil network from 2005 to date. A fully functioning payment system requires more participating banks and greater momentum from the market towards using third party processors. While GiroNil tried to build the network with individual banks from the ‘bottom-up’ in Egypt, regardless of their technical tools and know-how, the environment still called for a unifying regulatory authority for strategic direction.

Investing in Process Development

In this case, the CBE governing body in the market became the leadership solution behind putting the infrastructure in place. Upon receiving the 1 June Central Bank decree, all 38 banks are now connected to an ACH system and participating in the national payment infrastructure. Together, the EBC and GiroNil will work to integrate and interface all the systems so that banks can send and receive files to the ACH, using a web service connected to the EBC in the interim. At a later stage, all systems will be connected by Straight Through Process (STP) technology.

Part of GiroNil’s agreements with EBC allows them to connect their platform (GiroNil’s existing network), which uses the same technology and language, to EBC and the ACH’s infrastructure. Therefore, benefiting from their piloting experience with GiroNil, founding members Banque Misr, CIB or Egypt Post hit the ground running in their use of the ACH and have first mover advantage compared to other banks. For example large companies can use payroll products from Banque Misr and CIB immediately with the ACH launch.

KNOWLEDGE AND SKILLS

GiroNil realized that as early entrants they would be educating the market about national payment systems. This development role would potentially lead to high business returns for the company. The more bank managers and executives understood the benefits of the network system, the more inclined they were to actually use it.

On the one hand, there’s the need to supply technical solutions in building the infrastructure, related to software solutions and programs. On the other, there was the transfer of management expertise and communicating the business value of innovating banking products to actually use the infrastructure itself. EBC and GiroNil seek to avoid the situation of *“providing banks with a live cable that never gets plugged in or utilized for the purpose for*



*which [the system] was built.*⁴⁰ To make a lasting impact in transferring both types of knowledge, beneficiaries needed to be motivated by an empowering learning experience with GiroNil.

Technical Co-Development of The ACH Infrastructure

As per GiroNil's business model, the features offered under transferring business expertise was of particular value to the EBC. Besides technical know-how, GiroNil encourages EBC to conduct visits to their operations and senior management at their headquarters in Holland and arranges regular events and workshops locally for all levels of managers and executives in the banking industry.

On the technical side, what convinced EBC to select GiroNil as co-developer of the ACH was their trusted commitment as on-ground partners as opposed to delivering a turnkey model, as El Bayoumi explained *“other vendors usually just give you software, install it and leave. GiroNil doesn't do that, not from day one, not today. We really appreciate this about their approach, the valuable exchange of knowledge between us.”*

For example, GiroNil agreed to give EBC a license to use the technology from Equens used to build the GiroNil network, since GiroNil owns the exclusive rights for the technology in Egypt. On top of that, GiroNil agreed with the company that owns the intellectual property to move the development of the platform partly to Egypt. So that currently, an international team of 15 to 20 system programmers from the Netherlands, India and Egypt, who sit at EBC's headquarters developing the ACH system together.

A long-term investment vision in knowledge and skills means GiroNil shows greater flexibility to control and make amendments to the system until it is a right fit for the market. GiroNil's model manages to instill confidence, as El Bayoumi points out, *“When it comes to technical transfer of knowledge, my programming support is right here, my people will be able to handle issues on the long term, or if a breakdown happens the country is not at a standstill awaiting a vendor to fix it. With other systems you cannot make any changes, but because my people are working with the GiroNil team right now, the transfer of knowledge is very high.”*

Product and Process Development with Banks

Working with GiroNil, banks gain competitive capacity to innovate and promote ACH-driven products such as bank payroll or Internet banking. Creating valuable customized IT solutions, adapting banking processes, computerizing systems and skills training are some examples of re-engineering services provided to GiroNil partners in the past.

⁴⁰ El Bayoumi, 2010, Interview.



GiroNil has previous record in committed investment in developing skills of Egyptian postal employees who deliver Giro products and services. Since 2007, GiroNil management teams visited 150 to 200 (of a total 300 giro) post office outlets, per week, to monitor quality. They use a methodology similar to ‘mystery shopping’⁴¹ to rate postal workers’ performance. Monitored results allow Egypt Post to improve its capacity to deliver services, by empowering their employees.

Business Incentives Behind Development: The Financial Model

EBC views GiroNil’s role of developing banks’ capacity for ACH use as worthy of a revenue-sharing incentive between them. As GiroNil routes more transaction traffic into the ACH, generating volumes, GiroNil will receive a nominal fee out of every transaction.

Actors

THE CENTRAL BANK OF EGYPT

In the Egyptian financial sector, it was necessary for leadership from the central bank to give greater momentum to the development and use of payment systems. When the CBE created their Payments Systems Department, banks had a focal point to begin dialogue and initiatives. The CBE plays several roles in Payment Systems, it is the: Operator (of RTGS, ACH, and Checks Clearing House), Policy Maker (defining objectives and strategies, and establishing regulations) and Overseer of systems and services (including licensing of operator services by banks and third party). In addition, the CBE takes on the function of being the ‘catalyst for change’ in the market by initiating the ACH payroll and pensions project as major shareholder in EBC.⁴²

THE EGYPTIAN BANKS COMPANY (EBC)

Starting in 2009, the central bank leverages and regulates the state-owned EBC to play a lead role in building financial infrastructures for the national ‘less cash society’ vision. EBC specializes in building the technical capacity of banks operating in Egypt.

Back in 1997, EBC had its own experience building a shared cash network commercially called ‘123’ which links more than 30 Egyptian banks’ 1,500 ATMs nationally using the ‘Switch’⁴³ payment system method. This project yielded similar learning, as a commercial enterprise, EBC could not get the ATM Switch network going without the ownership and enforcement of the central bank for banks participation in the project.

⁴¹ A market research tool used by companies to measure the quality of retail service or to gather specific information about products and services, where professionals pose as shopping customers.

⁴² Faragallah, 2009.

⁴³ ATMs are connected to interbank networks, enabling people to withdraw and deposit money from machines not belonging to the bank where they have their account or in the country where their accounts are held (enabling cash withdrawals in local currency) (wikipedia.org accessed Jan 2010)



In rolling out the ACH, alongside technical development of infrastructure with GiroNil, EBC conducts six major ongoing workshops with people working in different banking functions such as operations, administration, marketing, internal systems of procedures within the banking sector. The EBC handles the communication of the platform publishing educational articles in industry-related journals and newspapers to appreciate the business value of the initiatives.

BANKS

Banque Misr

With a 30% shareholder in GiroNil Egypt, Banque Misr is one of the first banks to adapt its internal processes and get aligned with Egypt Post outlets and other banks that accept cash payments. Banque Misr's has a large client base of 5.7 million clients in Egypt and a total paid-up capital amounting to US\$630 million (EGP 3.4 billion). By developing banking products together (virtual network, software), Banque Misr is in a more competitive position to cater to large volumes of low-cost transactions market potential.

Commercial International Bank (CIB)

CIB⁴⁴ is one of the largest private sector banks in Egypt, CIB holds the largest market capital in the Egyptian banking sector⁴⁵, amounting to approximately US\$3.3 billion (EGP 18 billion).⁴⁶ The bank brings a significant customer base and is also a 30% founding stakeholder in the GiroNil joint venture.

Other Banks: Banque du Caire and the case of Microfinance

The high cost of financial transactions is a challenge to microfinance banks and institutions whose main customers are from lower-income communities. Although it is not the most profitable segment of the population, it could potentially be by far the largest.⁴⁷ GiroNil has an agreement with Banque du Caire⁴⁸ to process their microloans. The bank targets their microcredit facilities to micro or SMEs in commercial, industrial, agricultural or services through their 217 branches nation-wide.⁴⁹ GiroNil's management sees the solution in offering the bill presentment system as a paperless (internet or other phone) payment solution, bill presentment can significantly cut microloan payments collection costs for banks.

⁴⁴ The bank itself was established in 1975 as a joint venture between the National Bank of Egypt and the Chase Manhattan Bank under its original name 'Chase National Bank of Egypt'.

⁴⁵ According to CIB's website, it is the fifth largest bank (assets held), the third largest bank in Egypt (net worth), and the Best Bank in Egypt according to Euromoney - 10 years in a row. (Arabianbusiness.com, 2009)

⁴⁶ CIB website. <http://www.cibeg.com/en/About/Pages/default.aspx> accessed Nov 01 2009.

⁴⁷ Marroushi, 2008.

⁴⁸ Banque du Caire – Bank of Cairo (translation)

⁴⁹ Banque du Caire website <http://www.bdc.com.eg/html/main.htm> accessed Oct 12 2009



OTHER KEY PARTICIPANTS

Egypt Post: Leveraging a Powerful Network

Overall, GiroNil's business proposition rests strategically on Egypt Post's partnership. As explained by van Eersel, "*we chose the post offices because people have a natural trust in [them], they know if they pay there they can rely on that. And that is what we see, very high uptakes on the post offices where if you compare it to the uptakes at the bank branches it is much lower.*"

Holding a 30% stake in GiroNil is Egypt Post. Egypt Post is a state-owned entity, considered the largest service-oriented organization in Egypt, in terms of assets, number of account holders and cash resources (US\$388 million in 2005).⁵⁰ Egypt Post brings a tremendous 3,700 branches, 2,600 outlets and 90 ATMs nationwide.⁵¹

Egypt Post was a strategic partner to the GiroNil payment system model in several dimensions. Their extensive branch reach provides a crucial platform for interface with end-consumers. In major urban and rural regions of the country, a total of 300 Giro-branded post office outlets are actively serving GiroNil's products and services today. In these post office outlets, postal workers collect the money paid for giro services (i.e. AcceptGiro and InstantGiro) and enter the payment data on the e-payment system developed by GiroNil in order to process the settlement electronically while it is being settled physically at their processing center. Egypt Post benefits from its role as a transaction center by gaining share of the value created by the giro model offering additional financial services to the general public. The Post gains additional revenue from charging fees for processing transactions on behalf of the banks.

Egypt Post enjoys a heritage of institutional trust with the Egyptian population. For decades, they have delivered pensions and other services⁵² to millions of people nationally. Egyptian citizens are largely aware of the special safeguard measures the government takes to ensure their deposits with Egypt Post who hold 17 million accounts (more than the combined holding of accounts at all banks in Egypt).⁵³ The opportunities exist for partnerships with the private sector to introduce new applications in postal banking.

As GiroNil's model gets transferred to developing the ACH, it is unclear what the role of Egypt Post will be. So far confirmed, the Post will be a member of the ACH like other banks, and "*GiroNil will help them to develop their system in order to work on the ACH system.*"⁵⁴

⁵⁰ National Telecommunication Regulatory Authority website, accessed October 3 2009.

⁵¹ The Daily News Egypt, Oct 2008

⁵² A World Bank survey reported that 90% of Cairo residents were primarily satisfied with the postal service's performance out of a list of infrastructure and municipal services (UNDP, 2007, p.6)

⁵³ El Bayoumi, 2010, Interview.

⁵⁴ El Bayoumi, 2010, Interview.



The EBC share GiroNil's appreciation for the postal network, as crucial to reaching the unbanked target population especially in remote and rural locations. It is still to be seen, whether the public sector's Principal Bank for Development and Agricultural Credit, which has a similarly extensive branch reach, can play this role more effectively as the EBC construes.

The Egyptian Ministry of Finance

From the perspective of payment systems, the largest corporate in Egypt's financial sector currently are government supplier payments. The government alone makes more than 45,000 payments per day to various suppliers and employees, in the form of cash or by issuing checks. The aim is to direct these transactions towards the ACH instead to be electronically processed to their beneficiaries. The Ministry of Finance, who handles government payments (specifically by the e-finance company), therefore invested capital, and holds a 27% share, in EBC for this initiative.

Results

A NATIONAL PAYMENT SYSTEM GOES LIVE

On 8 April 2010, almost immediately following the signing of the contract between GiroNil and EBC, a pilot run of the ACH system went live. The system included just four banks: Banque Misr, National Bank of Egypt, The Housing Development Bank and Banque du Caire as well as e-Finance Company. In April, the ACH processed its first 86,000 transactions alone.

With the 1 June mandate, today all 38 banks in the Egyptian market are connected to the ACH and begin their individual strategies to innovate their product offers to capture lower-income segments.

ACCESS TO FINANCIAL SERVICES

According to co-developers EBC and GiroNil, the ACH building phases are first to complete credit transactions currently under construction, followed by direct debit systems, to finally have a full service ACH payment highway by the end of 2010. This results in a variety of payment products for potential offer by banks with use of the ACH.⁵⁵

Today half a million pensions and salary payments are being processed in the system; The CBE's strategy to increase this level is through the use of electronic cards. Payment to government employees through six million debit cards, pension payments through four to six million specific cards and promoting pre-paid cards designed to pay for government services.

⁵⁵ See Appendix Table 1- Payment Systems in Egypt, Types of Financial Products and Services

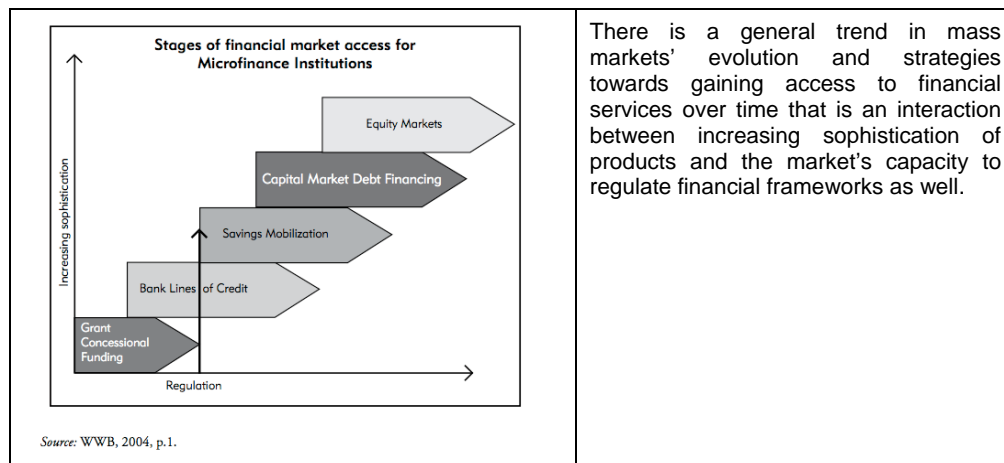


This will result in more than 15 million beneficiaries (7.5 million pensions, 7.5 million payrolls)⁵⁶ over the next three years, taking into account private sector payments as well.

Inclusion Group's underlying social mission to bring basic banking services to all segments of society influences their openness to including neglected low-income markets. GiroNil's experience with Banque du Caire's microfinance program is an example of developing banks' capacity to extend their line of credit to a mass population of poor individuals, micro-businesses and SMEs.

In research conducted on the early development of branchless banking with technology and microfinance to access mass markets, industry analysts⁵⁷ identified needs among which are "payment systems that can work with many providers, rather than in a closed system...and the creation of networks of third-party cash-handing agents (such as a post office) that can work with many providers..."

Chart 1- Access to Financial Services



From the end users' perspective, GiroNil has largely simplified access to financial services for the entire Egyptian population, as illustrated by the following testimonies about the use of AcceptGiro to pay phone bills⁵⁸:

"This service is very convenient for me because the post office is just beside my house; this is why I used it and I hope I can be able to pay all my other bills with this service".

Mr. Ahmed Shoeib, Port Said post office

"I like the service because it saved me the crowded queues at the centrals, in addition to the convenient working hours at the post office, which fits my work because there are some

⁵⁶ El Bayoumi, 2010, Interview.

⁵⁷ CGAP, "The Early Experience of Branchless Banking." (2008)

⁵⁸ Source: GiroNil Egypt, 2010.



offices that remain opened until 10 pm”.

Mr. Ahmed Al Arabi, Al Malahat post office

Future Outlook

INCLUSIVE BANKING PRODUCTS

“If we really succeed with the ACH it means we succeeded in targeting the lowest income segment most, either through post offices or through pre-paid cards, because we work on the basis of the number of transactions.”

Mohamed El Bayoumi, Managing Director, EBC

Looking directly to the unbanked population, and specifically to lower income segments including those under the poverty line, the EBC and the central bank will develop an additional tier of payment systems categorized as Micro Payments. The ACH system enables the lowering of the transaction costs and therefore makes micro payments financially viable.

As a new consumer market, the EBC studies how to position financial service offers that suits their lifestyle, habits and needs. GiroNil and EBC finding relevant payment tools to cover the widest range of people. As El Bayoumi differentiates *“The lower income and poor are the largest segments in Egypt, they don’t deal with banks and banks don’t approach them either, and cards are tied to banks. This is not the same with mobile phones though.”* For example, he explained how strategies at first included big plans to load debit cards for payroll with features such as co-branding with MasterCard so they could be used at A-class retail outlets. Given that a government employee earns on average about US\$75 (LE400) per month, it did not seem an appropriate financial service, when a local debit card would do.⁵⁹

GiroNil’s approach to banking the large number of lower income population is one of building relationships, in a rapidly advancing segment. Starting dialogue with customers as early as possible is the key to building a relationship with the consumer, understanding their needs to offer more advanced products (such as savings accounts, overdraft facilities or insurance).⁶⁰ GiroNil conducted pilot studies to understand how to position their products in the pipeline; where the consumer will react positively and based on those studies adapts financial innovations. The investment from the banks and new foreign investors goes to delivering new products for the retail market at the right time – mobile banking is a current example. *“The trend you see everywhere shows there is a lot of focus on mobile payments.”*⁶¹

⁵⁹ El Bayoumi, 2010, Interview.

⁶⁰ Ibid.

⁶¹ Ibid.



Remittances

Within the money transfer segment of the market, remittances⁶² from Egyptian migrant workers represent an important source of external funds for the Egyptian economy. Money transfers between parents and children are a significant driver in the payments market in Egypt. Inexpensive financial mechanisms are needed to attract cash transactions such as these through formal channels. In their 2003 feasibility study, GiroNil had identified the remittance payment⁶³ market in Egypt as one of their three main product focus areas. Mobile banking solutions is an area GiroNil is exploring as an example.

Mobile Banking

The capacity for branchless banking in Egypt would seem to have highest potential with mobile technology leverage. There are less than 10 million bank accounts in Egypt and at the same time there are more than 50 million mobile phones in use.⁶⁴ Van Eersel refers to an industry case of M-PESA in Kenya, which stands as model of success of mobile banking as a business opportunity in emerging markets similar to Egypt. *“We believe the mobile phone can become the payment platform where you have a bank account or do it through an outlet where you have a virtual account. The mobile phone could be the device to connect the unbanked and banked together.”*⁶⁵

Again, each market owning its own characteristics means that the story will be different in Egypt. For example, in Kenya, special circumstances, such as insecurity of having cash in hand due to war had an immense effect on the fast-paced adoption of new technology. EBC takes cues from the market, such as the observation that just one, of the three mobile phone operators in Egypt, Vodafone, has 45 million subscribers alone.⁶⁶ Another characteristic EBC identifies is the ease of use of mobile phone tools among the young generation, who are rapidly becoming their upcoming client base. Outside main cities, El Bayoumi envisions the many small shop owners interacting with customers he explains *“they won’t understand or maybe trust a card, or a bank outlet, but in both their pockets they have their mobile phones and you can physically see the transfer happen.”*

Other advantages considered are that the mobile phone as a tool for interfacing with the poor will require no additional investment, equipment or establishing branches from banks. EBC and GiroNil will focus on prioritizing periodic money transfer, where it will be a much cheaper, faster and convenient channel than available alternatives.

⁶² In 2007, Egypt was the top recipient of remittances in the Middle East and North Africa region with US\$5.9 billion. (World Bank, 2009)

⁶³ One of the Giro network’s products that is available but not operational is TransGiro, which handles money order transfers from one individual to another.

⁶⁴ The high level of mobile phone penetration can be misleading, as some analysts point out, “because not all mobile users can benefit from mobile banking services in Egypt. It is important to categorize mobile users because not all of them are bank accounts holders. (Abdel-Mageed, 2008)

⁶⁵ van Eersel, 2009, Interview.

⁶⁶ El Bayoumi, 2010, Interview.



Conclusion

In building a joint-venture payments processing infrastructure in Egypt, GiroNil and their partners have benefited from a development model that takes into account the necessary time and resources needed towards developing knowledge, management skill and insight to capitalize on substantial business opportunities. With leadership and regulation from the central bank, the initiative was given momentum to accomplish goals for a more cashless society.

On a sector level, the ACH payment system propels the banking industry towards providing retail products and services to the unbanked, giving them representation in the Egyptian financial market. Banks' growth and profitability will depend on institutions' strategies and vision in competing in the financial mass market. By building a cooperation network GiroNil and its customers build trust in the Egyptian economy, stimulating future growth.



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Growing Inclusive Markets

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January 2010

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Design: Suazion, Inc. (NJ, USA)

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