

Summary Notes of the Seminar:

Making The Case for Formalization in Egypt

The Egyptian Center for Economic Studies and the Federation of Egyptian Industries organized the seminar: Making the Case for Formalization in Egypt on 11th May, 2014 at the Four Seasons Nile Plaza, Cairo.

Speaker: **Hernando de Soto**, President, ILD, Peru
Discussant: **Heba Handoussa**, Founder, ENID, Egypt
Moderator: **Sherif El-Diwany**, Executive Director, ECES, Egypt

On behalf of ECES and FEI, we are pleased to share with you the main takeaways from this seminar presented by the speaker and the discussant.

1. Informality should not be placed in the category of poverty. It is the richest sector of the economy.

4 out of 7 billions of the world's population live and work in the informal sector. Egyptians, Brazilians, Tunisians and others from the informal sector seek to move to Europe or North America looking for good laws that work for them. Once back in their countries they avoid the law, because the laws are bad. In Egypt, there are 8.2 million people employed extra-legally. Of those, 68 percent are engaged in extra-legal enterprises, 22 percent in legal enterprises, and 10 percent in street vending activities and the like. Estimates also indicate that 92 percent of Egyptians hold their property without registered titles, the replacement value of which is estimated to be US\$ 360 billion.

2. Informal economy is big business. If it is treated like small business it will mean more poverty. If formalized, this property can put an end to Egypt's credit crunch. Egyptians do not feel a real credit crunch because they are constantly living in it. The banking system is not able to offer credit to most of the population because there are no formal assets in the economy to secure it.

3. Informal entrepreneurs are already in business but with unlimited liability and with no or very expensive credit. Every time they invest, all their savings and assets are on the line; a very high risk and excessive cost.

4. Results of formalization in the Peruvian case: ILD implemented formalization in Peru in 1987. The economy is now the fastest growing in Latin America and the middle class grew by 4 times and continues to do so.

5. All modernized economies have undertaken formalization programs at one point or another. Example: Japan, 1946 after they lost the war, US Wolf Ladejinsky was able to formalize all the Japanese economy. He was able to organize the population in a process designed to obtain the information about who owns what from the farmers. In six years all the

Japanese economy became formal. Similar transformations happened in USA, Switzerland, France, Germany, Vietnam and South Korea.

6. Ten guidelines on how to best implement a formalization program:

- i. Recognize that formalization is a revolutionary transformation and it is not about finding a technical solution to license and to register. It is about political leadership and will.
- ii. Change the public perspective on what informality is: it is not about micro credit; it is big business.
- iii. Recognize that the poor want to move from small to big business but they are held back by laws that do not work for them. The new legal system has to be better than customs and rules that the informal sector functions by today.
- iv. The poor believe they have the right to buy and sell and they are doing today, but outside the law. The current laws are bad laws, they need to be reformed to change from being barriers to becoming facilitators of business.
- v. Formalization is not about land tenure, it is about information of who owns what, where; and who lives where. Information makes it possible for markets to function, for transaction cost to come down and for new wealth to be created.
- vi. Reform all the laws and regulations that govern business and property bearing in mind that all violations of past laws will have to be foregone.
- vii. Get in touch with the informal economy. Listen to and find out from the informals why they do not want to join the formal sector to learn what needs to be changed to encourage them to move voluntarily to the reformed legal system.
- viii. Find quick wins and start with them to provide proof of concept and convince the informals that moving to the new legal system will not dispossess them of their assets.
- ix. Communicate well to the population in the informal sector, explain the incentives and benefits of formalization under the new legal system, but do not raise expectations too high and build credibility of the formalization program.
- x. Create a new organization that has the leadership with a clear and sole mandate of moving informals to the new legal system. Do not leave implementation to the technocrats.

During the seminar participants were asked to vote on two questions. The results are shown in Figures 1 and 2.

Figure 1: Should the Egyptian extralegal economy be integrated into the formal sector?

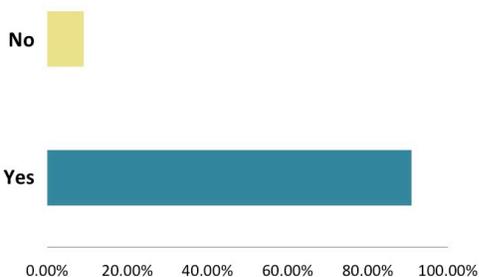


Figure 2: What are the most important risks facing the implementation of a formalization project in Egypt?

