

**Economic  
Reports**

**10 MAY 2018**



**المعهد المصري للدراسات**  
EGYPTIAN INSTITUTE FOR STUDIES

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## Foreign Investment in Egypt: Reality and Challenges

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Despite the economic measures taken by the Egyptian government to support the domestic and foreign investment climate – most notably the issuance of new laws to regulate investment, companies, capital market, and bankruptcy; as well as the adoption of monetary policies, such as floating the Egyptian pound, to guarantee the availability of foreign currency – yet figures of foreign investment have not yet reflected such reform measures.

Egypt attracted foreign direct investment of \$ 3.8 billion during the first half of the current fiscal year (July-December), compared to \$ 4.3 billion in the same period last year, a decline of 11.6 percent.

Investment flows achieved in the first half of this year are less than 40% of the Ministry of Investment's target (\$ 10 billion) by the end of the fiscal year ending June 30.

Foreign investment rates in the first six months of this fiscal year indicate the government's inability to reach its targets by the end of the year, especially since the first half of the last fiscal year saw a flow of about 55% of the total investment of the year. (55% of 7.9 billion dollars).

Also, a comparison with last year's estimates indicates that it is difficult to achieve these targets. In fact, the first half of the last fiscal year was much better than the same period of the current year with regard to the non-oil foreign investment flows, which fell to \$ 1.7 billion, compared with 2.5 billion in 2016-2017.

However, the foreign petroleum investments constituted a large part of the increase in direct investment rates, after rising to 2.1 billion dollars compared to 1.8 billion in the first half of the last fiscal year. The balance of payments showed that oil investments represented 55.3% of the total foreign direct flows, against 41.8% during

the same period last year; while non-oil investments declined to 44.7%, compared to 58.2% in the first half of 2016/2017.

Thus, we can say that foreign direct investment grew by 14 percent to record \$ 7.9 billion against \$ 6.9 billion in 2015/2016, although economic reforms were much lower than those achieved during the current period.

Despite all the facts presented by previous figures, the government still adheres to its FDI targets for the current fiscal year, despite the IMF cut of its forecast ceiling to \$ 8.4 billion, instead of the \$ 9.4 billion it foresaw during its first review of Egypt's economic reform program last September.

Many analysts expect that the government will exceed the \$ 8 billion barrier by the end of the current fiscal year, but their expectations are not in line with the government's low rates achieved during the first half of the current financial year. Also, they are not commensurate with the size of the procedures, resolutions, and laws introduced under the auspices of the IMF program.

There are many factors that have led to the poor return of the government program to attract foreign investment.

*Following are the most important factors that can improve the figures of foreign investment flowing into Egypt and the reality of the Egyptian situation:*

### **1- Government's ability to restore consumption growth**

Success of economic measures in attracting foreign non-oil investments depends on the government's ability to restore consumption growth, which is still low. For a foreign investor to decide to invest directly in a non-oil sector, he must rest assured that there is a recovery in consumption growth and that the growth opportunities in industry are real, not just promises.

Overall, the size of the market is not measured according to the number of population, but rather according to the average per capita income. In this concern, the Egyptian market is not attractive to many investors, especially as the government is still maintaining its economic reform plans, which have caused more decline in consumption rates.

## 2- Factors related to supply and demand

- 'Supply' is related to the ability to access production inputs, including intermediate goods and requirements, raw material, capital goods represented in machinery and production equipment, in addition to the availability of skilled and professionally trained labor force, as well as proper wages from the foreign investor's point of view. Unfortunately, the Egyptian labor force have been badly affected by the deterioration of the education system in general, which led to the local market's failure to attract foreign investment in this regard.

Although the new investment law recognized the shortage of trained workers by allowing foreigners to bring in 10 percent of the workers employed in their projects from abroad, 90 percent of the workforce is still untrained and the regime has not acted on this important issue yet.

- As for the 'demand' factors, they are related to the size and composition of markets. The local market depends on the "price" of the product than its "quality". Therefore, foreign investors are reluctant to involve their capital and technology in a market that looks at the price of commodities before their quality.

## 3- Reducing inflation and interest rates

The high inflation and interest rates are among the most important factors that directly affect the decisions of foreign investors. Under interest rates of about 20%, and



inflation rates exceeding the limit of 30%, it is difficult to improve foreign investment flows. Therefore, any future decline in inflation or interest rates can contribute to increasing investment significantly.

At the end of last March, the monetary policy committee of the Central Bank of Egypt (CBE) cut the interest rate by 1% (16.75% for depositing and 17.75% for lending) for the second time in less than two months. Also, the CBE has raised the interest rate by 7% since its decision to liberalize the exchange rate in November 2016, to meet price inflation, before lowering it by 1% in mid-February, after the decline of inflation.

Observers believe that a decline in the interest rate is likely to a large extent in light of the government control over the CBE decisions. According to many research centers, interest rates are expected to drop by 200 basis points until the end of 2018.

As for the inflation rate, it is very difficult to continue its decline. The increase in the prices of oil derivatives at the end of the current fiscal year, as well as the announcement of a package of economic measures aimed at reaching the world price rates, all these actions promise a continued rise in Inflation rates.

#### 4- Ease of doing business

This relates to the ease of doing business, as defined by the World Bank, in terms of easy access to projects, and the realization and transfer of profits, starting from obtaining approvals and licenses, through access to land and facilities, and ending with the provision of infrastructure, especially in the field of energy, transport, and modern communications. In fact, all this has already been stated in the Investment Law and its recent executive regulations.

The government also responded to the International Monetary Fund's request to issue a law to facilitate the issuance of industrial licenses, which shortened the licensing period for most industrial projects to weeks instead of about two years in the past.

Nevertheless, the security control, the proliferation of sovereign institutions, the intervention of the army in many projects, and the control of security men over local government administrations and licenses still give the impression that procedures and even laws are hostage to the actions and decisions of those 'related to the military', which threatens the investment flows or disrupt them at the very least.

## 5- Political stability

Achievement of political stability has been a major factor in influencing flows of foreign direct investment. Since 2013, the regime has shown a great deal of exaggeration in describing and intimidating terrorism; and promotion of the war on terrorism has taken up a large part of Egyptian political statements over the past period, whether internally or externally. Also, the media role in this regard helped to draw a mental image suggesting that there is political instability and lack of security in Egypt.

A series of measures have also been taken in this concern, including the continued extension of the state of emergency, which could be considered a negative indicator for the investor, in addition to the military operations in the Sinai, and the economic crisis that results in political freight which is met with severe repression by the regime, accumulating hostilities.

Egypt's internal political situation does not need much effort to demonstrate instability as an important factor in dismissing and discouraging foreign investment.

Global geopolitical tensions, particularly in the Middle East, along with the domestic political situation, play a major role in discouraging investment, and make it difficult to predict significant developments in investment flows.

## 6- High prices of lands

The government's trading in lands, especially in most of the new cities, contributed to raising prices so much, which is considered another discouraging factor to foreign investment.

## 7- Other factors

There are other factors, including: the low levels of transparency and flow of information, difficulty in customs clearance and spread of corruption in ports, high customs fees on some materials, management systems and difficulty in determining the functional responsibilities of some government agencies.

## Summary

It is difficult to achieve the figures officially announced by the Egyptian government in the field of attracting foreign investment. The foreign investor wants a stable business environment, clear tax policies that do not constantly change, and low interest rates. Foreign investments do not come massively to a particular country unless they ensure the existence of strong domestic investment through a business sector, public and private, capable of actively participating in productive activity - which is not available in Egypt so far.

The question is not about the issuance of laws. However, there are other important things such as respect for laws, a low interest rate on borrowing, clear tax policies and a stable political situation.