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Egypt gets a new electoral law that paves the way for legislative elections in early 2015. But the elections themselves are only likely to bring an illusion of stability unless major economic reforms are implemented soon. And, absent such reforms, the military government's headline investment summit – planned for March – could be a damp squib as investors wait for concrete evidence of reform plans and action on the underlying causes of Egypt's huge budget deficit (expected to stay around 10% of GDP), especially fuel and food subsidies. Islamist insurgents remain effective, especially in and around the Sinai Peninsula, and may benefit from heavy-handed army efforts to establish a security buffer in the area. Extremist attacks continue to focus overwhelmingly on Egyptian state targets rather than foreigners. The UK and Canadian diplomatic missions close temporarily to the public, most likely a precautionary move but also indicative of nervousness on their part about insecurity in Cairo.

Approval of a draft electoral districts law

Egypt's **Supreme Electoral Commission** approved the draft electoral districts law on 16 December.¹ This represents a key step towards holding legislative elections, expected in the first quarter of 2015. The significance of the electoral law is that it details the composition of the new parliament. Of the 567 seats, 420 members will be elected individually in single-member constituencies and 120 through electoral lists, while President **Abdel Fattah el-Sisi** (2014 – present) will have the power to appoint the remaining 27.²

The passage of the draft law has been drawn out, and reflects the broad range of social stakeholders that the government is trying to accommodate in its search for domestic legitimacy. The cabinet originally approved a proposal for 232 single-member electoral districts, before the **State Council** revised this to 237. The **Supreme Electoral Commission** assented to the new revised figure, sending the amended proposal back to the cabinet where it is awaiting final approval. Egypt has been governing without a lower legislative chamber since the supreme constitutional court declared the **Muslim Brotherhood**-led people's assembly unconstitutional in June 2012 and the armed forces, under Sisi, took power. This has led to concern about possible future legal challenges on the constitutionality of legislation passed during the past two years.

Despite government claims – and ambitions – the new parliament will be no guarantor of political stability. The dominant number of individually elected parliamentarians will encourage the development of fractious and fluid blocs in the new parliament, without the stability and predictability that party discipline requires. Egypt's new political landscape is already inchoate and chaotic. The political parties that are allowed to exist are mired in petty disagreements over coalition names and priority on the electoral lists ahead of the elections. The number of parties has expanded substantially since 2011: approximately 80 are registered, and dozens more are in formation.³

¹ Aswat Masriya, 16 Dec 2014.

² Aswat Masriya, 16 Dec 2014.

³ Source, MENA analyst

“Give it two to three years, and those Egyptians currently giving Sisi the benefit of the doubt will be as disgruntled as they were under [President Hosni] Mubarak [1981-2011].”⁴

Three electoral alliances have emerged thus far: the **Egyptian Wafd Alliance**, the **Democratic Current**, and the **Egyptian Front Alliance**. The first two are largely secular and support the stated democratic principles of the **January 25 (2011) revolution**, but the parties themselves differ in every other regard.⁵ The Egyptian Front Alliance is home to many former members of former Mubarak’s now-disbanded **National Democratic Party**. The heterogeneous composition of the blocs is indicative of Egypt’s struggle to progress beyond the divisions that followed the 2011 revolution.

Mubarak acquitted

On 29 November, a **Cairo** court dropped all charges against former president Mubarak, always likely since his former intelligence chief, Sisi, had seized power. The charges related to alleged state-inspired violence during the 2011 uprising that resulted in Mubarak’s ousting. For opponents of both Mubarak and the Sisi government, the acquittal marked a symbolic end to the liberal ideals of the **Arab Spring**. While Sisi has ensured at least some political and economic stability, the style and makeup of his administration is strongly reminiscent of Mubarak’s. After the divisiveness and instability of the Muslim Brotherhood administration that eventually succeeded Mubarak, most Egyptians have initially seemed willing to view this as an acceptable solution if it delivers greater stability and addresses Egypt’s profound economic problems in meaningful, concrete ways.

Fixing the economy, or not?

The government has been expending a great deal of political and financial capital in persuading international investors that the **Egypt Economic Summit** in March 2015 will deliver a new investor-friendly economic framework. Media have been reporting government’s plan to prioritise the power generation sector, and building expectations of far-reaching announcements on energy subsidies and tariffs before the summit.⁶ However, the pace of real measures and actual reform to date has been slow and piecemeal. A persistent problem facing the government is the decline in its foreign currency reserves (needed for imports of food, for example), as well as the long-standing power generation crisis, which directly impacts on industrial activity and inflicts outages on consumers.

*“Don’t hold your breath about the March summit. The government is sending up a lot of public relations balloons. I’m trying to keep an open mind, but there are too many vanity projects in the government’s infrastructure planning that don’t make economic sense. Take the idea to widen the **Suez Canal**. My shipping contacts tell me it’s not like widening a road: you won’t get more traffic or income as a result. The difference between the **Gulf** leaders and Egypt’s is that those in the Gulf know what they want to do and get outside advice on how to do it. The Egyptians think they can do it all themselves.”⁷*

*“The summit could succeed in persuading some investors to pile in. Interest in Egypt is high, partly driven by the strong recent performance of the stock market compared to **Tunisia**, for example. But I wouldn’t be one of them as things stand.”⁸*

The government claims to be accelerating reforms. In the oil and gas sector, it announced on 13 November its intention to repay \$4.9 billion owed to foreign oil and gas companies within six months. The announcement has had an immediate impact. **British Petroleum (BP) Egypt** chairman **Hesham Mekawi** announced on 9 December that BP would invest more than \$12 billion in Egypt over the

⁴ Source, north African political analyst

⁵ Source, MENA analyst

⁶ Source, energy sector careerist, Egypt.

⁷ Source, corporate lawyer

⁸ Source, published economist specialising in Egypt

coming five years, and the company also plans to double the amount of gas it supplies to the Egyptian domestic market over the next ten years.⁹

Several Gulf States have provided critical help to the Egyptian government to clear its debts to international oil companies, by providing bridging finance.¹⁰ The **United Arab Emirates (UAE)** and **Saudi Arabia** have given around \$12 billion to Sisi's government since 2012. Both also hope to turn direct aid into investment opportunities for their own companies. The Sisi government prefers to work with Gulf-based companies, supposedly because of their close government links and because they are known and trusted entities.¹¹ On 7 December the **Kuwait Fund for Arab Economic Development**, for example, agreed to loan Egypt \$102m to upgrade a power plant west of Cairo.¹² However, there is evidence of strain in relations:

"Sisi is misjudging how far he can rely on the Saudis and Gulf states to keep bailing him out. They are already getting fed up with the government's failure to make real progress on reform and fear that public demonstrations and violence will increase in 2015 as a result."¹³

The oil price crash

The sudden recent falls in oil prices could have severe implications for Egypt. The military government has created vast and costly domestic obligations (not least to itself), generous energy subsidies and social spending meant to prevent the kind of public discontent that simmered for years and boiled over in the Arab Spring. It has struggled to maintain these programmes in the face of persistently high budget deficits.

In December, the finance ministry (in draft budget note) said that it had targeted headline economic growth of 4.3% in the 2015–2016 financial year and a budget deficit of 9.5 – 10%. It said it would aim to close the revenue-spending gap by introducing new taxes and cuts to energy subsidies.¹⁴ The ministry has previously warned that, if left unchecked, government spending on energy subsidies in 2015 will be 10–12% percent higher than the 130 billion Egyptian pounds (\$18.6 billion) budgeted for this fiscal year. Subsidy reform in Egypt is politically contentious and deeply unpopular, making it unlikely that Sisi will embark upon it in any meaningful way until after the parliamentary elections.

"Egypt has a major debt problem and needs to get it under control. Its negotiations with the [International Monetary Fund] IMF have been unnecessarily tortuous at times. Lots of prospective investors are saying: 'until the IMF is happy, we'll keep a watching brief.' The government urgently needs to get a grip on subsidies and cut them back. With oil prices collapsing, now is the time to do it, as related commodity prices for consumers should be falling anyway. But subsidies in Egypt have a tendency to be 'upwardly sticky,' as one fellow economist calls it: once in place, the main beneficiaries (the urban middle class, not the poor) see them as a right."¹⁵

The armed forces as an economic stakeholder

There are certain obstacles to systematic economic reform in Egypt, notably the role of the military in economic matters. Sisi has so far not attempted to address the direct economic and commercial role of the armed forces, which own manufacturing and services companies in a range of sectors, including

⁹ www.dailynewsegypt.com

¹⁰ Source, energy sector consultant, Egypt.

¹¹ Source, energy sector careerist, Egypt.

¹² www.world.einnews.com

¹³ Source, Egyptian political analyst

¹⁴ MENA, 13 Dec 2014.

¹⁵ Source, published economist specialising in Egypt

energy-intensive ones. Military-owned and run companies are also major debtors to Egypt's energy companies and thereby distort natural supply and demand principles and relationships.

*"The military regime – itself a major player in the economy – doesn't appear to understand or appreciate the extent of reform that is needed. Remember: the generals grew up under Mubarak's system and protect their interests ruthlessly."*¹⁶

The formal energy bidding process appears to have become more transparent under Sisi and the government is no longer automatically awarding contracts to military-linked companies as they did previously. According to a senior executive in the Egyptian energy sector:

"Previously, we would not bother competing against state-owned companies or ones we knew had close links to the government or the military. It was a complete waste of time. Now we do, and we win open tenders even when we submit lower bids than state companies. It is definitely more transparent than previously and investors are increasingly confident in the credibility of the bidding process. Our one concern is [when] we win [seemingly] one-too-many contracts and the state-owned companies or the ministries begin to pay attention. If you raise your head above the parapet, there is still a very real risk that the government will force you into a partnership with a state-owned enterprise."

Security uncertainty

In November, an armed group calling itself the **Sinai Province of the Islamic State** claimed responsibility – in an online posting – for the car bomb attack that had killed 27 soldiers on 24 October.¹⁷ The group is named after the **Sinai Peninsula** in which it operates, and was formerly known as **Ansar Beit Al-Maqdis** (Supporters of the Holy House). Despite its apparent reference to the **Islamic State**, any links between it and the **Syria** and **Iraq**-based militant group are unproven. In November, Sinai Province also claimed responsibility for the August killing of **United States** national **William Henderson**, reportedly an employee of **Apache Corp** and **Qarun Petroleum**, in what had appeared to be a carjacking. However, insurgent group attacks specifically targeting foreigners remain infrequent in Egypt.

*"The army needs to be very careful in the Sinai. Its approach has been heavy-handed and – in places – indiscriminate. It is alienating neutral civilians and also creating a great deal of anger among [itinerant] **Bedouin** communities, many of whom have no interest in Islamism. The **Bedouin** will not submit to harassment and have a well-ingrained culture of revenge."*¹⁸

The army is also working to establish a buffer zone in the Sinai Peninsula to clear the area of underground tunnels leading to **Gaza** and it will also level any buildings and structures that could be used for cross-border smuggling.

The **United Kingdom (UK)** and **Canadian** embassies in Cairo temporarily suspended public operations in early December citing an unspecified security threat.¹⁹ It is unclear whether the suspension related to specific intelligence or a general threat. Sinai Peninsula-based Islamist terrorist groups **Ajnad Misr** and Sinai Province have carried out repeated attacks against Egyptian government security targets in the Sinai and Cairo but not, as yet, against foreign diplomatic targets.

Sources indicate that the Egyptian army may be playing a covert role in the conflict in **Libya** with the encouragement of its UAE allies:

¹⁶ Source, senior executive in energy sector, Egypt

¹⁷ Daily News Egypt, 16 Nov 2014.

¹⁸ Source, north African political-military analyst

¹⁹ Aswat Masriya, 16 Dec 2014.

"The Egyptians are interfering in Libya. The Emiratis want Libya go the same way as Egypt [back to a strongman regime]. The chaos of Libya is a poisoned chalice for Egypt, and they should stay out."²⁰

Implications

The new election law and the planned parliamentary elections will not end Egypt's political transition. They will create temporary stability as a wider range of social stakeholders gain a personal stake in the new system. But creating so many new political stakeholders always carries the risk of storing up irreconcilable disputes. Things already look messy and chaotic due to the fluid political blocs that are emerging. And with Islamists having few formal political means of representation, they will continue to be heard through other means, including continued protests (the moderates) and violence (the more radical elements).

The government says it will reassure investors before the March summit with a bundle of legislation offering greater reform, clarity, predictability and economic stability. But deeper structural reforms will take time to yield results even if they go far enough at the outset. It is questionable whether Sisi and his colleagues really understand what is needed or have the will to challenge vested economic interests, not least those of the Egyptian military itself.

Islamist terrorist attacks will continue, regardless of the army's progress with its 'Sinai buffer.' The Islamist groups appear well armed and organised, and could benefit locally from greater civilian support if the army continues its heavy-handed security approach. The Sinai is rich in government security and strategic economic targets: **Port Said**, **Suez** and **Ismailiya** are particularly at risk, as are softer official targets in major cities such as **Cairo** and **Alexandria**.

The UK and Canadian embassies' decisions to close temporarily appear, in this context, to have been largely precautionary: an attack against a heavily-guarded embassy in Cairo would indicate a shift in both Islamist target profiling and a so-far non-evident capacity to launch major attacks outside Sinai. But the embassies may not have complete faith in the authorities' ability to guarantee security in Cairo given recent attacks on soft targets there, and the Egyptian army's aggressive military operation in the Sinai amplifies the risk of insurgent retaliation in Cairo against hard and soft targets alike.

²⁰ Source, north African political-military analyst