

AFRICA RISK CONSULTING Egypt Briefing March 2015

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A supreme constitutional court ruling delays parliamentary elections originally scheduled for 21 March. The delay triggers a cabinet reshuffle, with President Abdel Fattah Al-Sisi (2014-present) replacing interior minister Mohamed Ibrahim with former national security adviser Magdy Abdel Ghaffar. The Egypt Economic Development Conference in Sharm El-Sheikh results in \$36 billion worth of deals in the energy and oil and gas sectors. The government announces a new administrative capital and development of the Suez Development Zone. In an effort to improve the business climate, the government reduces corporate tax to 22.5% from 30% and restructures the civil service.

Constitutional court delays election, triggers government reshuffle

A supreme constitutional court ruling¹ on 1 March that the December 2014 **Electoral Law** is unconstitutional will delay the parliamentary elections previously scheduled to begin on 21 March. The delay will undermine Egypt's political transition to a nominally democratic government, but will have no impact on government stability or the position of President **Abdel Fattah Al-Sisi** (2014-present). The ruling specifically challenged the article that divided up Egypt's electoral districts. Constitutional court rulings are binding with no avenue for appeal. Prime minister **Ibrahim Mehleb** on 2 March formed a committee to redraft the electoral law.² It is possible that the parliamentary elections will now take place in the third quarter of 2015, with Ramadan in June precluding an earlier date.³

Tensions have increased between the judiciary and the government. In recent months courts have overturned a number of rulings, notably against President **Hosni Mubarak** (1981-2011) era officials and **Muslim Brotherhood** supporters. The upper echelons of the judiciary blame political pressure for the original rulings.

The delay has prolonged Egypt's political transition, with Sisi preparing to govern without a parliament. In a surprise move, Sisi reshuffled his cabinet on 5 March.⁴ He was not expected to change his government – formed in June 2014 – until a new parliament was in place.

With the reshuffle, Sisi also sought to shore up investor confidence before the **Egypt Economic Development Conference** (see below). He replaced interior minister **Mohamed Ibrahim** with former national security adviser **Magdy Abdel Ghaffar**.⁵ Ibrahim was an unpopular figure. Leaked reports in local media in February claimed he had approved the use of live ammunition in policing protests. Ibrahim was a key ally of Sisi and was interior minister under former president **Mohammed Morsi** (2012-2013). Ibrahim helped to orchestrate the July 2013 coup that ousted Morsi. He was influential both in the security sector and within Sisi's government. Removing him will involve a rebalancing of political power around Sisi and suggests that the president is confident that he faces no serious political challenges.

Sisi's removal of Ibrahim appears to be a move to appease both international and domestic constituencies. Foreign investors remain wary of Sisi's failure to deliver concrete progress towards economic and political reform. The government cannot afford a poor human rights record that deters risk-averse investors:

¹ MENA, 1 Mar 2015.

² Aswat Masriya, 2 Mar 2015.

³ MENA, 1 Mar 2015.

⁴ MENA, 5 Mar 2015.

⁵ MENA, 5 Mar 2015.

“This is more than a cabinet reshuffle. With a major economic investment conference planned, Sisi need[ed] to appear concerned over human rights so Western investors [weren't] put off.”⁶

Domestically, Sisi will hope that Ibrahim’s removal will please the liberal secularists who are increasingly angry at continued human rights violations by security forces as well as their failure to stop terrorist attacks. There was an increase in violence in **Cairo** in February and March. The **Revolutionary Punishment** and the **Popular Resistance Movement** terrorist groups carried out most of the attacks.⁷ The security situation remains unstable: a suicide bomber killed two and injured 42 soldiers in an attack on a military camp in the **Sinai Peninsula** on 9 March.⁸

Sisi’s choice of successor may do little to reassure liberals that security forces will improve their conduct. Ghaffar was the head of Mubarak’s **State Security Investigation Service** and then Morsi’s **National Security Agency (NSA)**. He was briefly interior minister under Morsi but was quickly replaced. He has held an advisory position in Sisi’s government since June 2014 and is considered highly influential.

Sisi also replaced the ministers of culture, tourism, agriculture, communications, vocational education and training, higher education, and housing.⁹

Investment conference results in \$36 billion deals...

The Egypt Economic Development Conference in **Sharm El-Sheikh** resulted in \$36 billion worth of deals, indicating increased investor confidence in Egypt. Notable investments include:

- **Germany**-based **Siemens** will invest \$10.5 billion in a 4.4GW gas fired power plant in southern Egypt and 2GW of wind power, increasing Egypt’s electricity production by approximately one-third.¹⁰
- **United States (US)**-based **General Electric (GE)** will invest \$1.9 billion in power plant turbines;
- **PepsiCo** will invest \$500m in supply chain and capacity infrastructure;
- **United Kingdom (UK)**-based **British Petroleum (BP)** and **Russia**-based **DEA** will invest \$12 billion in developing gas fields in the **West Nile Delta (WND)**, with gas extracted offshore at two wells, **North Alexandria** and **West Mediterranean Deepwater**. BP aims to develop five trillion cubic feet (tcf) of gas and 55 million barrels of condensates, with production expected to start in 2017.¹¹ The project envisages peak production of 1.2 billion cubic feet of gas a day, equating to a quarter of Egypt’s current gas production. BP – keen to diversify its global operations – is a significant partner for the government which is keen to develop its indigenous hydrocarbon resources.

“The growth of investments in Egypt, notably the WND, is a welcome note in a sector beginning to feel the impact of lower prices – investment into the base of the projects will be essential in future proofing them. There have been many examples of such projects falling victim to market jitters. Cairo, by ensuring a welcoming investment environment and doing all it practically can to ensure safety and security, is making the right moves.”¹²

- **Italy**-based oil and gas company **Eni** will invest \$5 billion in its Egypt operation before 2018;
- **United Arab Emirates (UAE)**-based **Dana Gas PJSC** will invest \$350m in Egypt over the next two and a half years in addition to its normal operating costs. Dana Gas produced an average of 68,900 barrels of oil equivalent per day in 2014, up 6% from a year earlier. The investment comes after senior management agreed to pay the Egyptian government any overdue debts. Dana stated that it would use the investment to develop new wells and topside facilities as well as export

⁶ Source, MENA political analyst, Cairo

⁷ New York Times, 2 Mar 2015.

⁸ Al-Ahram, 9 Mar 2015.

⁹ Al-Jazeera, 5 Mar 2015.

¹⁰ D4, 14 Mar 2015.

¹¹ AFP, 6 Mar 2015.

¹² Source, senior petroleum economist

infrastructure. The additional investment is aimed at significantly boosting production in order to overcome domestic shortages, namely in liquefied petroleum gas (LPG) production and bottling;

- Supply minister **Khaled Hanafy** confirmed two investment agreements worth \$6 billion to launch a **Global Logistics Centre for Grain Handling in Damietta** and a **City of Commerce and Shopping** project as part of the **Suez Canal Corridor Development** project. With an already well established import-export infrastructure the projects will allow, upon completion, far greater access to domestic and international markets;
- The government also signed an agreement with **Carbon Holdings Ltd Co** to bear 26% of the cost of building the **Liberation Petrochemical Company** project with a total cost of \$7.3 billion. The project aims to build the largest oil-cracking base in Africa to serve global demand.

The government proposed a number of energy projects during the summit. The **El-Wady Phosphate Project** will see the development of a major phosphate fertilisers complex in **Abu Tartur District**. Through the **Assiut Hydrocracker Project**, the **Egyptian General Petroleum Corp** intends to install a full conversion hydrocracker complex adjacent to the existing **Assiut Oil Refinery**. A third project is the 110-km **Assiut-Sohag LPG 10" pipeline** between Assiut and Sohag. The conference is expected to encourage future investment in Egypt's downstream oil and gas sector, reducing its dependence on imports.

*"Capital investments of this sort into the energy sector and infrastructure are one thing – it is the investor confidence which we find the most comforting. We can see continued economic and investment growth into the sector. By also boosting the downstream and midstream infrastructure there is also a strong indication of further expansion of projects."*¹³

International financial institutions also committed to strengthening the Egyptian economy. The **African Development Bank (AfDB)** said it would offer Cairo a preferential lending programme of between \$300 and \$450 million.

*"The move by the AfDB and support from the **World Bank** etc. allows Egypt not only to access capital but also expertise – both organisations bring a wealth of experience in working in such transitional economies. Expertise and guidance are [paramount] here. Whilst the funds will help, the advice will be essential in helping Cairo move ahead."*¹⁴

The AfDB expects the benefits of its funds to be twofold. On the one hand, the funds will help Egypt's economic reform programme and on the other, they will develop trade and investment between Egypt and **sub-Saharan Africa**. The **Islamic Development Bank (IDB)** also signed a \$4 billion agreement with the government, with the participation of the **International Islamic Trade Finance Corporation**, to import petroleum products.

Bilaterally, **Saudi Arabia, Kuwait** and the UAE pledged a total of \$12 billion in investment aid, \$3 billion of which will go directly to the **Central Bank of Egypt** and the rest towards investment projects. Egypt also raised \$5.2 billion in loans from international institutions, and committed to \$18.6 billion of financed development projects.¹⁵

...as government announces mega projects

The government also announced two 'mega-development' projects at the conference. The first is the building of a new city east of Cairo, closer to the **Red Sea**. The city will become the country's administrative capital. It is planned to cover 150 square miles and house up to seven million people. It will also house government ministries and other organs of state, as well as major commercial development and residential properties.¹⁶ The government has signed a memorandum of understanding (MoU) with a UAE company to build the city.¹⁷

¹³ Source, senior economist

¹⁴ Source, economic analyst

¹⁵ AFP, 15 Mar 2015.

¹⁶ Al-Ahram, 13 Mar 2015.

¹⁷ AFP, 15 Mar 2015.

The second project is the development of the **Suez Canal** into a major shipping and manufacturing hub through the **Suez Development Zone**. The **Suez Canal Authority** will oversee 18 major development projects worth an estimated \$50 billion. These projects aim to turn the canal from a transit route into a loading and industrial destination in its own right. This will involve three major shipping ports and licences for 1,000 factories in the Suez area. A widening of the canal itself began in August 2014, with 90% of the dry digging and 40% of the wet digging already complete. Major international companies have already signed up to the development project. GE announced a \$200m project to build a manufacturing and training facility in the **Suez City** area of the development zone during the conference.¹⁸

“Sisi knows that unless Egyptians, who have developed a taste for public disruption, see the effects of development, further costly disruption could take place.”¹⁹

Government moves to improve business environment

The government moved to reassure investors that it is committed to improving the business environment with a number of announcements timed to coincide with the investment summit. In order to make Egypt a more attractive investment destination, Sisi signed into law a package of amendments to investment legislation on 12 March. The new legislation reduces corporate tax to 22.5% from 30%, makes the process of settling investment disputes through arbitration less complex, reduces sales tax from 10% to 5%, and sets customs duties on equipment used for production at 2%. The government also ratified tax incentives for investments in labour-intensive industries. Critics have argued that the reforms were rushed through the legislative process, but a number of factors including increased Islamist attacks and an ongoing power crisis have put pressure on Sisi to address development issues quickly.²⁰

The government has also moved to improve the notoriously inefficient bureaucracy. In a second presidential decree, Sisi outlined a new law implementing new regulation of the civil service. The law centralises the process of recruiting public servants, provides a faster system of promotion, and sets out new categories of civil service posts. The government recognises the need for greater transparency within state agencies and state-owned enterprises.

A presidential decree issued on 12 March amended three Criminal Code articles dealing with the recovery of stolen and misappropriated assets.²¹ The decree indicates the government’s desire to improve transparency and promote a safer investment environment. The cabinet is yet to fully ratify the decree; however, little opposition is expected. Once enacted and ratified, the law will allow for the **Illicit Gains Committee** to fully recover historic crimes and assets for a period up to 10 years from the date of the alleged crime.

A US court on 23 March sentenced a former **Bechtel Corp** vice president to 42 months imprisonment for money laundering and corruption charges after he pleaded guilty to receiving \$5.2m in bribes when manager of **Power Generation Engineering and Services Co** between 1996 and 2011.²² Power Generation Engineering and Services was a joint venture with the state-owned **Egyptian Electricity Holding Co**. The federal court also ordered dual US/ Egyptian national **Asem Elgawhary** to forfeit the \$5.2m. One of the power companies that bribed **Elgawhary** was **France-based Alstom S.A.**²³

Implications

The delayed elections will not affect Sisi’s authority as he faces little credible political threat. The raft of business legislation that Sisi passed around the economic summit suggests that the lack of parliament will

¹⁸ Reuters, 13 Mar 2015.

¹⁹ Source, Egypt analyst, Dubai

²⁰ AP, 12 Mar 2015.

²¹ Daily News Egypt, 12 Mar 2015.

²² www.fcablog.com

²³ www.fcablog.com

not slow governance. Ibrahim's dismissal suggests that Sisi will use the delay to broaden his support base before the elections and hinder the emergence of a meaningful political opposition.

The economic summit will encourage both new and returning investors. By drawing in long-term investment with its major international partners, Cairo is slowly building a sound economic base from which to move ahead, should the investment materialise and projects run unhindered.

Without structural reform of Egypt's bureaucracy and civil service, it is uncertain how long it will take for the economic benefits to be realised. Similar presidential decrees during the next six months or so will continue to improve the business environment, boosting both investor and popular confidence.

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