LYNX STRATEGIC BUSINESS ADVISORS

LYNX Business Bulletin
Egypt's State Ownership Policy

January 2023

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Introduction

On December 29, 2022, President Abdel-Fattah ElSisi approved the final version of the State Ownership Policy document, which outlines the Government of Egypt's (GoE) vision on the future role of the state in the economy. The objective is to establish a clear framework that regulates the relationship between the state and the private sector across various economic activities.

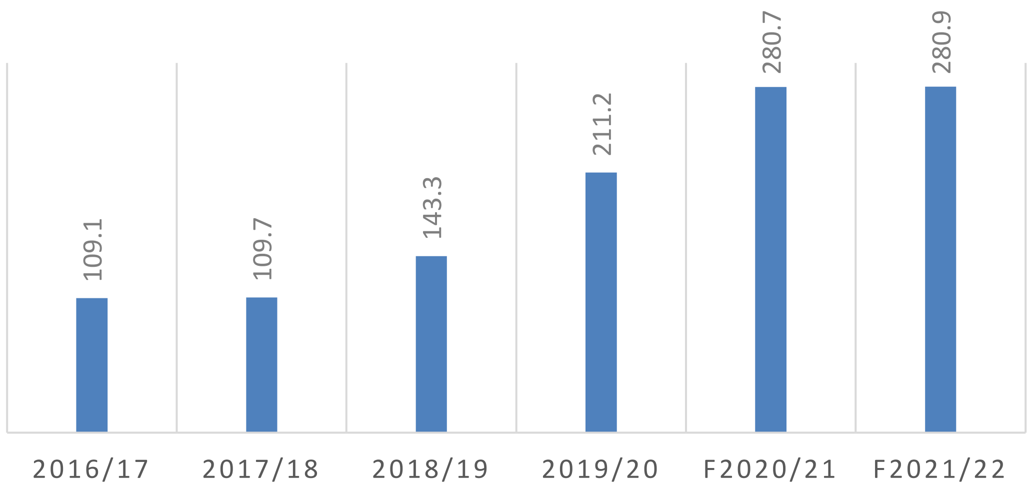
The policy's adoption followed a public debate, initiated May 2022 with the release of the policy document's first draft, on the rising role of state-owned enterprises (SOEs) in the local economy during the past few years, which impacted Egypt's business climate and added burdens on the state budget. Evolving structural weaknesses related to the private sector were not adequately addressed, creating business obstacles, especially for small and medium-sized enterprises. There have also been calls for the state to increase transparency, strengthen Egypt's public financial management and address other macroeconomic vulnerabilities to instill greater investor confidence in the GoE.

The newly adopted policy seeks to increase private investments in the economy by raising the participation of the private sector in public investments from 30% at present to 65% within 3-5 years. It also emphasizes the state's priorities of enhancing the participation of the private sector to achieve 7-9% annual growth rate, increase exports, and offer new employment opportunities.

Most notably, the policy determines the sectors that the state plans to fully withdraw, maintain, decrease and/or increase its role in. The role of key stakeholders in achieving the GoE's vision is also outlined.

Investors, Egypt's donor partners and economic experts have been encouraged by the increasing debate in Egypt about the role of the state in the economy. Under the recently approved 46-month Extended Fund Facility (EFF) agreement between Egypt and the International Monetary Fund (IMF), an emphasis was placed on the pursual of structural reforms such as reducing the state footprint, enhancing transparency and governance of SOEs, levelling the playing field for all economic players, strengthening competition policy, and improving trade related processes. The IMF stressed that the State Ownership policy is a critical first step down this reform path.

Following the presidential ratification of the policy, a Supreme Committee, headed by the Prime Minister, will oversee its implementation. The committee will be responsible for defining the state's exit mechanism from selected sectors, determining relevant timelines, and addressing evolving challenges.



GOVERNMENTAL INVESTMENTS, EGYPT

Source: LYNX Quarterly Macroeconomic Overview- October 2022

Future Role of the State in Economic Activities

In the GoE's view, the withdrawal of the state from designated economic activities depends on a variety of factors including:

- The nature of economic activities,
- The direction of economic developments on the local and global scales,
- The strategic nature or implications of the economic activity on Egypt's national security.

Accordingly, the State Ownership Policy highlights the intentions of the state to withdraw from 62 business activities (within 3-5 years), decrease its presence in 56 other activities, and increase its presence in 76 activities. Under the initial draft policy, which was released in May 2022 for public consultations, the GoE intended to exit from 79 sectors and reduce its footprint in 45 other sectors, within a maximum period of 3 years.

According to the policy, the state will ***withdraw*** from several sectors including:

- Crop and fish farming in the agricultural field,
- Passenger, cargo, and river transport,
- Food and beverages (with exceptions),
- Retail,
- Various financial brokerage activities such as commercial insurance.

The state further plans to retract from several construction activities. And compared to the first draft of the policy document, the state will be more involved in establishing dry ports, rather than completely exiting the sector.

Meanwhile, the GoE intends to ***maintain or decrease*** its footprint in several fields including:

- Wholesale trade,
- Several activities in the water and sanitation sector, such as drinking water lifting stations and water distribution networks,
- Several mining activities, such as coal mining, gold refining and others,
- Several agricultural activities such as fisheries, and various dairy products.
- Several activities in the transport sector, such as the establishment, operation and management of container terminals in marine ports, as well as the operation of various maintenance services in the local railways system,
- Several sports activities, including establishing and operating sport clubs/cities and youth development centers.

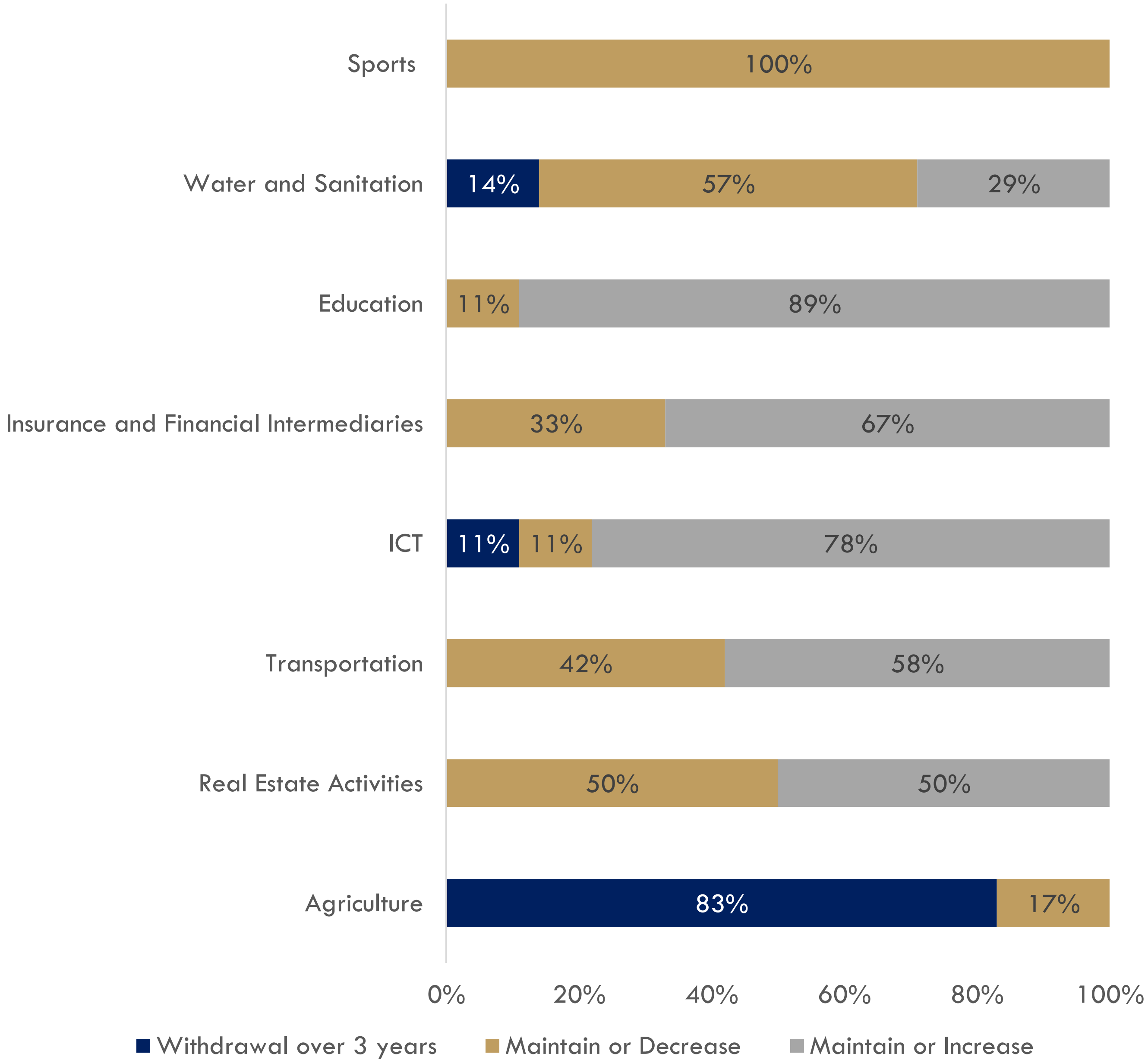
On the other hand, the state intends *to* ***maintain or increase*** its role in several sectors including:

- Pre-primary and higher education,
- Healthcare,
- Activities associated to the Suez Canal,
- Investments in oil/gas extraction and refining,
- Investments in electricity transmission networks,
- Several activities in the Information and Communications Technology (ICT) sector such as infrastructure for wireless and terrestrial communications, and units for modern postal services,
- Press and media activities, including video/ cinema films, radio and television broadcasts.

Future Role of the State in Economic Activities

According to the GoE, the implementation of the country's privatization plan is likely to materialize through the following alternatives:

- Offering state-owned assets in the Egyptian Stock Exchange (EGX) to expand the ownership base, whether in whole or in part,
- Injecting new private sector investments into a state-based ownership structure,
- Public Private Partnerships (PPPs),
- Concession Contracts,
- Build-Operate-Transfer Contracts (B.O.T),
- Build-Own-Operate-Transfer Contracts (B.O.O.T),
- Build-Own-Operate Contracts (B.O.O),
- Design-Build-Operate Contracts (D.B.O),
- Build-Finance-Operate-Transfer (B.F.O.T),
- Performance Contracts,
- Management Contracts.



GOE PLANS FOR A GRADUAL EXIT BY ECONOMIC ACTIVITY

Source: State Ownership Policy Document

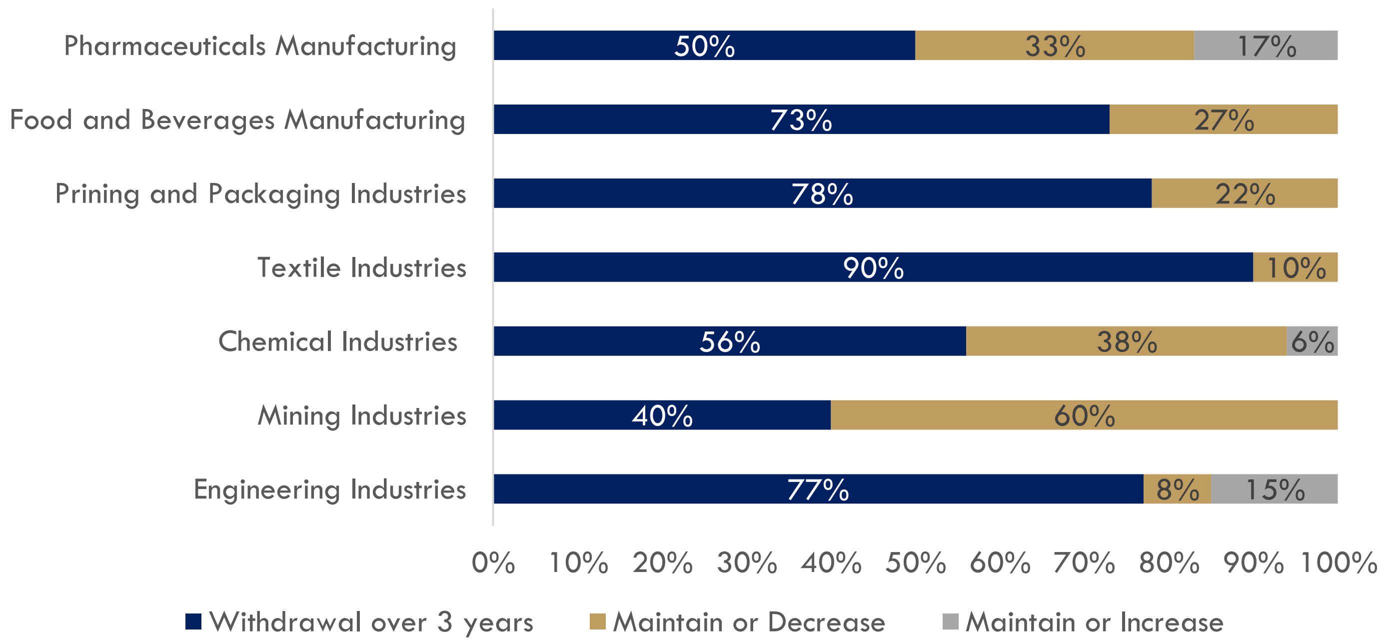
Future Role of the State in Economic Activities

In particular, the GoE's vision of the role of the state in **manufacturing** activities can be summarized as follows:

1. ***Withdrawal*** from leather industries (including shoe manufacturing), engineering industries (such as production of electronic devices), furniture manufacturing and wood activities, food and beverages manufacturing (such as fruits and vegetables, dairy and juices), chemical products manufacturing (including ink, paint, rubber, plastic, glue, foam, sponges,) as well as waste management). The GoE further intends to pursue the state's exit from various textile industries (including the manufacturing of ready-made garments and home textiles), packaging and printing, and pharmaceutical manufacturing (including the production of perfumes and beauty products.)

2. ***Maintain or decrease state role*** in the manufacturing of raw materials and production requirements for wooden and furniture, several activities in the food industry, (such as the production of meat, birds, fish, cigarettes and smoke), several metallurgical industries (including metal crafting and forming), chemical industries (including cleaning detergents and other liquid chemicals). The state further plans to decrease its footprint in several activities in the textile industry (such as cotton and wool weaving, manufacturing of fiber and industrial polyester yarn as well as dyeing and finishing industries,) as well as in the manufacturing of animal pharmaceuticals.

3. ***Maintain or increase state presence*** in various engineering industries (including boats and ships, machinery and equipment,) renewable energy, several food production activities (including oils and sugar), several mining activities (including production of copper, stainless steal and aluminum,) and some printing activities (including newspapers, magazines and printed ads). The GoE also plans to increase state investments in the medical and pharmaceutical industry (such as medical supplies, vaccines, medical raw materials, medical devices, surgical scalpels, medical syringe needles, catheters, kidney filters, and others), petroleum refining, and the manufacturing of fertilizers and pesticides.



FUTURE STATE ROLE IN MANUFACTURING ACTIVITIES

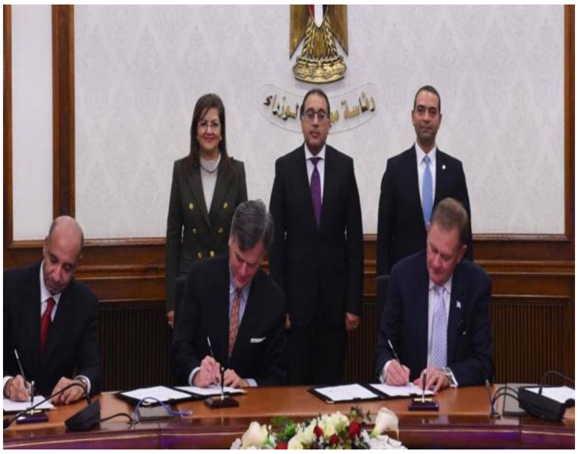
Source: State Ownership Policy Document

Role of Key Stakeholders

The State Ownership Policy seeks to emphasize and enhance the role of two key GoE-backed stakeholders in enhancing private investments and levelling the playing field between public and private economic players.

The Sovereign Fund of Egypt (SFE)

Since the Fund's establishment in 2018, the SFE has secured EGP 37 billion of foreign direct investments (FDIs), with a significant share from the Gulf Cooperation Council (GCC) countries such as the United Arab Emirates, Saudi Arabiam and Qatar.



Hence, the policy emphasizes the 'pivotal role' of the SFE in attracting private sector investments in sectors such as:

- Infrastructure (water, electricity plants, roads and telecommunication networks,)
- Agriculture,
- Logistical services,
- Transportation and storage,
- Waste management,
- Renewable energy,
- Banking and financial services,
- Education and healthcare.

The SFE will be directed to further ensure the optimal use of public assets within the framework of the State Ownership Policy.

The Egyptian Competition Authority (ECA)

The State Ownership Policy stresses the importance of creating a favorable legislative environment and ensuring competitive neutrality to stimulate private investment and boost economic activity. (The ECA was previously criticized for not exercising its regulatory role vis-à-vis SOEs.)

Accordingly, a strengthened ECA role is placed at the heart of the policy to create an enabling environment for free competition. In the GoE's view, this includes guaranteeing that the private sector is competing on a level playing field with SOEs. Thus, a **competitive neutrality** policy would materialize including through taxation, debt and regulatory neutrality measures that would be defined.

To achieve this objective, the Prime Minister will chair a Supreme Council to support competition neutrality. The ECA will create a special unit for this purpose, and the Authority's independence will be further strengthened to enforce competition neutrality.

The ECA will also be instructed to conduct periodic assessments of the impact of the State Ownership Policy on the economy through performance indicators, as well as publish periodic reviews on the status of sectors where the state is present to ensure transparency.

Conclusion

The adoption of the State Ownership Policy comes at a time of challenging and uncertain times for the Egyptian economy, as the GoE seeks to rebalance the country's external accounts following the shocks of 2022 through several movements in policy to address foreign currency shortages, high inflation rates and stimulate efforts to attract FDIs to Egypt.

The past period also witnessed noteworthy capital inflows from GCC countries to acquire stakes in key public and private sector assets, and (limited) steps- promoted by the SFE- to help transfer public economic assets to private investors. Announcements were made about including (economic) assets run by the military to private hands, though no public transactions have been made.

Through the State Ownership Policy, the GoE is signaling its intention to revisit some aspects of its policy direction in the wake of the recent economic, fiscal and social challenges. The policy should not be viewed as a new privatization program nor a plan that endorses a significant exit of the state from the economy, especially in sectors where the state's role is crucial (such as military production, infrastructure projects that don't attract private investors, and social activities and services that offer minimal profit for the private sector.)

In fact, the policy can be considered as an attempt to reposition the state's role in the economy through a mapping exercise of assets and activities that will be transferred by the GoE to private investors, while highlighting other activities where the state's role will continue or even be elevated, complemented by a general set of policy commitments to carry out its vision through a strengthened role of key stakeholders.

While the policy document, in defining the assets owned by the state that will be subject to some forms of privatization, references companies owned by the military that operate in the economic sector and the assets of other (non-civilian) entities, the document's reference to strategic or security considerations in shaping the market exist strategy may leave the door open for misperceptions over the state's intentions should these considerations not be clearly defined.

Enhanced transparency over the future role of the state in the economy and the creation of a fair level playing field are key to enhancing private investments in Egypt. However, reducing red tape and bureaucratic challenges, enhancing predictability of evolving economic and fiscal policies and regulations, facilitating land allocation, permits and licenses, and expediting the availability of raw materials are equally important in creating a conducive environment for sustainable investments in Egypt.

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