China in the Middle East & Africa

Brief No. 1: China in Egypt

These briefs are informal notes for stakeholders on the implications of shifts in development and trade between China and various countries across the Middle East and Africa. They highlight emerging trends or topical issues, and are issued every quarter. Contributions are greatly welcome.

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Executive Summary

This report examines the state of Chinese trade and investment in Egypt in various sectors including stone material processing, textiles, manufacturing, infrastructure, and energy. The report draws on data collected from interviews with 20+ Chinese business leaders in the country in June 2017.

Egypt is a difficult business environment for Chinese enterprises. Top challenges reported by Chinese companies include business registration and licenses, access to finance, customs and trade control as well as access to land. However, despite currency shocks and political risk challenges that have driven away other investments, Egypt remains a promising new market for Chinese companies attempting to establish a foothold in the MENA/Sub-Saharan Africa region.

Chinese activity in the Egyptian economy first emerged through investments in the stone-processing sector during the 1990s. Today, the sector remains dominated by Chinese firms, which produce 70% of Egypt’s stone material exports and employ over 3,000 Egyptian workers. The China in Egypt Stone Material Association, launched by the Chinese embassy, now plays an instrumental role in unifying the business community, facilitating dispute resolution, and establishing industrial codes. Chinese companies in the stone material sector are well-integrated in the local labor market and procurement system, and work closely with the Bedouin community to ensure security.

Between 2000 and 2010, the number of Chinese companies investing in the Egyptian textile sector increased as demand for textile products from socks to shoes and clothes increased. However, due to the political turmoil of the Arab Spring in 2011, textile exports shrank and many Chinese-owned textile shuttered their operations. As the Egyptian state stabilizes today, several Chinese businesses have returned to the area or entered the market due to the reduction in competition.

Manufacturing companies such as Jushi, a leading supplier of fibreglass and reinforcements, and New Hope, an animal feed producer occupying a vast area of 29,000 square meters in Beheira province north of the Egyptian capital Cairo, have achieved remarkable growth in Egypt and introduced the “Made in Egypt” brand internationally.

The manufacturing industry has witnessed a flurry of interest from Chinese multinationals. China’s SAIC Motor Corporation Limited, a Chinese state-owned automotive design and manufacturing company headquartered in Shanghai, is now planning to construct a factory in Egypt in order to supply the Egyptian market as well as markets in the Middle East and Africa with active free trade agreements with Egypt.

Similarly, China’s Guangzhou Godessense Decorative Building Materials Co. Ltd. is constructing a new factory in a 16,000 square-metre area located in the Suez Governorate Ataqa industrial zone under a USD $100 million Egyptian-Saudi-Chinese joint venture.

While Egypt urgently needs more infrastructure projects, poor availability of foreign exchange renders such initiatives difficult. Several projects have been announced, but have experienced delays in negotiation and implementation. Nevertheless, some notable successes do exist. Sinopec, China’s second-largest oil group by market capitalisation, for example, has joined American company Apache as a junior partner in an oil and gas exploration project located in Egypt’s Western Desert. By spending $3.1bn on a 33 per cent stake in the project, Sinopec is deepening its commitments in Egypt having previously embarked on another joint venture there in concert with Tharwa Petroleum, an Egyptian company, in 2005.

The World Bank’s Doing Business Ranking places Egypt at 128th out of 190 countries in the 2018 edition of its annual report. Botho’s Sino-Africa Centre for Excellence has similarly found that Egypt presents a challenging opportunity for Chinese enterprises with the country’s 2016 Business Perception Index ranking at 7.1 out of 10.

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China is now the largest investor in the Suez Canal Economic Zone with a Tianjin-based state-owned company as the major developer of the Teda Industrial Zone in Ain Sokhna, which lies on the western shore of the Gulf of Suez. Teda currently hosts several successful companies in Egypt and is ready to launch its second phase of development.

As Egypt emerges as a promising production center, investments by Chinese companies are likely to continue to grow.

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Introduction

China and Egypt have strong economic, political and social ties. According to the Chinese Ministry of Foreign Affairs, China is currently Egypt’s largest trading partner as well as its largest importer. In 2017, bilateral trade volume between Egypt and China reached $USD 6 billion. During July of the same year, Chinese imports from Egypt rose to $102 million with an increase of 479.4% on an annual basis, as the volume of bilateral trade between China and Egypt recorded $921 million during the same month.

Both governments have championed the increase in trade and investment. Since Egyptian President Abdel Fattah al-Sisi’s inauguration in 2014, he has visited China annually. In return, Chinese President Xi Jinping paid a state visit to Egypt in January 2016 in order to consolidate strategic partnerships between the two countries. Egypt is also one of twenty-one African countries that are officially identified as a high-priority investment destination for Chinese enterprises.

Despite these warm diplomatic ties, Egypt has a relatively small Chinese immigrant population for a country of its size and strategic importance. Prior to 2010, approximately 25,000 Chinese nationals lived in Egypt. Following the Arab Spring, the Chinese population in Egypt dwindled to 10,000. Since 2013, the number has increased to 15,000 Chinese nationals, including 3,000-4,000 students studying in religious colleges in Egypt; however, the Chinese immigrant population has failed to reach pre-Arab Spring levels.

As more Chinese nationals immigrate to Egypt, the number of Chinese companies is on the rise.

This report examines the state of Chinese enterprises in Egypt and analyzes development trends and challenges in sectors including stone material processing, textile, manufacturing, infrastructure, and energy. It also identifies potential opportunities in the Egyptian market and provides suggestions on how to leverage growth opportunities.

The content of the following report draws data and insights from more than 20 business owners, professionals and officials. Names, titles and company information mentioned in the report are considered sensitive information and may not be re-published without express permission of the Sino-Africa Centre for Excellence at Botho Emerging Markets Group.

According to the Chinese Business Council in Egypt, there were around 20 Chinese companies in Egypt. By the early 2000s, the number increased to around 50 by 2012. As of early 2017, there are more than 100 Chinese enterprises in the country.
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Stone Material Processing
A Chinese-Dominated Sector

Egypt has abundant marble, granite, and greystone reserves. The country’s annual export volume of stone materials is worth approximately USD $1 billion, making Egypt one of the top four marble-exporting countries in the world alongside Turkey, Greece, and Italy. Prior to the 1990s, Europe was Egypt’s primary export destination for raw stone materials; however, rising Chinese interest in Egyptian stone rose in the 1990s as more Chinese firms attended Italian trade expositions. These firms first began operating in Egypt as exporters before expanding to process raw stone locally.

There are more than 50 Chinese-owned stone material processing companies that employ over 3,000 Egyptian workers. Around 35% of these products are now exported to China, but companies interviewed for this study also indicated interest in exporting to other Chinese companies operating in Africa.

Despite their contributions to the local economy, Chinese businesses in the stone sector have not escaped controversy. They regularly face opposition from the local Egyptian community, media, and civil society. As a result, Chinese businesses operating in the Egyptian stone sector are cautious about their labor and supplier relations. According to company representatives interviewed, firms often hire Egyptians as factory managers in order to mitigate these tensions.

China in Egypt Stone Material Association (CESMA)

China in Egypt Stone Material Association (CESMA) was established under the Chinese embassy following a kidnapping incident in March 2012 in which a Chinese national working in the stone sector was kidnapped for a ransom of half a million Egyptian pounds. Although the hostage was recovered, the incident created considerable media attention in China. In an effort to focus on proactive rather than reactive strategies in future, the embassy created CESMA in order to facilitate better communication between the embassy and private Chinese companies in the stone-processing sector in Egypt.

Since its founding, CESMA has played an instrumental role in unifying the stone-processing business community and resolving disputes. In 2016, for example, the association formed an alliance between stone material producers and export trading companies to adopt the U.S. dollar as their transaction currency in order to mitigate currency shocks amid the Egyptian pound crisis. Moreover, the association advocated on behalf of its member companies to the Egyptian Ministry of Labor in response to a series of disputes regarding work permit quotas for Chinese workers. The embassy also uses CESMA as a communication and control channel to reach private companies in the sector. Finally, CESMA has leveraged the collective resources of Chinese-owned stone processing companies for corporate social responsibility activities since 2012. During Ramadan 2017, the association worked with local non-profit organizations to distribute 4,000 Iftar meals to local communities. CESMA also organizes periodic charity dinner and donation events.

Bedouins and Security

Chinese companies in the stone processing and trading sector report higher rates of crime as compared to Chinese companies in other sectors. The high incidence of crime may be linked to a variety of factors including the remote location of most stone-processing factories, insufficient safety awareness and prevention measures, and reliance on low-income labor. Crime incidents range from theft and car robbery to kidnapping, in the most serious instances.

To secure factories and protect employees, many Chinese firms in the stone-processing industry hire Bedouins, a nomadic group of Arab-descended people who have historically resided in the desert. Today, most Bedouins live in the suburbs of Cairo and the Sinai Peninsula. Most stone-processing companies with production sites in industrial areas interviewed for this report stated that they pay Bedouins a monthly fee to exchange for protection.

While several companies surveyed acknowledged such payments might be constituted as bribery, managers described them as necessary facilitating payments in order to ensure business continuity. Companies in the stone-processing sector spoke highly of Bedouin security services, and noted their critical role in resolving past disputes. According to companies interviewed, Bedouins are effective in identifying and locating criminals by leveraging their networks.
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From Textiles to Manufacturing
Fall of the Textile Industry

In the 1990s, an increasing number of Chinese businessmen from Zhejiang, Fujian and northeastern China arrived in Egypt as traders and small-scale investors in the textile sector. Between 2000 and 2010, investments by Chinese companies in the textile industry peaked.

With low labor and land costs, these Chinese enterprises soon excelled. The Nile Textile Group, based in the Said Port Industrial Zone, exports over 100,000 garments made by 400 textile workers each year to China. Egypt-China Brothers Shoe Co Ltd. has witnessed similar success. Founded in 2002 by a businessman from Zhejiang, the company has six production lines worth nearly USD $3 million. With its more than 500 employees, the factory has produced more than 3 million pairs of shoes for domestic and overseas markets.

These successes, however, have shrunk considerably due to political turmoil stemming from the Arab Spring, which drove numerous Chinese-owned textile companies out of business. While Egypt is relatively advanced compared to other countries in the region, it cannot produce all required raw materials for textile production. Instead, it is forced to rely on imported inputs. Currency fluctuations stemming from recent political turmoil, therefore, lead to increased costs for textile companies, many of which were forced to close their doors.

Hanging on a Thread

As the market share of Chinese textile companies has shrunk, new opportunities are emerging for Chinese companies in the manufacturing sector. Jushi and New Hope are two such notable examples. Both are privately-owned companies that have recently entered the Egyptian market amid political uncertainty and have achieved remarkable success that have exceeded expectations.

Jushi Egypt For Fiberglass Industry S.A.E | Jushi Egypt is one of the best-known Chinese enterprises operating in Egypt. Founded in 2012 as a subsidiary of the world’s largest fiberglass producer, Jushi Group is located in the Suez Special Economic Zone. The company currently employs over 2,000 workers who work across three different shifts in order to maintain 24-hour production. More than 97% of its workforce are hired locally and the majority of its middle-level managers are Egyptians. It is the first company to produce fiberglass in Africa and has established Egypt as the third-largest producer of fiberglass in the world. Jushi Egypt exports 95% of its products to Europe, the Middle East and India, of which Europe accounts for 40-50% of its exports.
Hanging on a Thread (cont.)

During an interview, Jushi Egypt executives explained that the choice of Egypt as an investment destination was based on three primary factors: market access, low labor costs, and tax incentives. Companies in Egypt have easy access to the European, Middle Eastern, and Indian markets. Secondly, Egyptian labor costs are low, an attractive incentive in a labor-intensive industry like fiberglass. Lastly, the “made in Egypt” brand shields Jushi’s products from anti-dumping criticisms frequently lobbed against Chinese companies and provides Jushi Egypt with preferential tax treatments. The company plans four phases of investment with a value of more than USD $600 million. The first phase began in 2014 while the second phase launched in 2016. By mid-2018, the third phase will be ready for production, which will increase the company’s total production capacity to 200,000 tons of fiberglass per year.

Similarly, New Hope Egypt Co. Ltd (New Hope) is a wholly-owned subsidiary of New Hope Liuhe Co., Ltd, the largest animal feed producer in China. New Hope started operating in Egypt in 2013, three years after announcing its plans to launch in Egypt. Its first factory occupies nearly 230,000 square meters, and has a production capacity of 200,000-ton chicken feeds per year. The second factory was launched in May 2016 with a production capacity of an additional 200,000-ton chicken feeds per year. As of 2016, the company comprises 10-15% of Egypt’s feed market, and market share exceeds 50% in some regions.

New Hope is currently constructing another two factories in Egypt, which will employ 700 more local workers in addition to their current 300 employees. The company is projected to capture 20-30% of the feed market in Egypt by 2018.

Successful Chinese manufacturing enterprises in Egypt (as well as successful stone processing enterprises) share some features: a large percentage of their raw materials are sourced locally in Egypt, their main markets located in Europe and the Middle East, and they are low-skilled, labor-intensive businesses that source most of their workforce locally.
Rise of Public-Private Partnerships in the Manufacturing Industry

Due to Egyptian regulations, Chinese companies primarily enter the Egyptian market through joint ventures with local firms.

In 2008, for example, China XD Group, a major manufacturer of power transmission and distribution electrical equipment, formed a joint venture with the state-owned Egyptian German Electrical Manufacturing Co. (EGEMAC) to establish a high-voltage electric equipment factory in Egypt. Located in the Suez Special Economic Zone, China XD Group is one of the few Chinese-owned companies to successfully weather the political turmoil of 2011 and maintains a steady operation at the moment.

Similarly, CHINT-EGEMAC Co. Ltd is a joint venture between Egyptian German Electrical Manufacturing Co. (EGEMAC) and Chint Group, a leading Chinese private industrial electrical equipment production company. Located in the 6th of October, a city west of Cairo, CHINT-EGEMAC will offer multiple types of low-voltage switchgears that are tailor-made to meet the local demands.

The first phase of the project is a factory funded by Chint with 40 Egyptian employees that will serve as a trial investment before Chint expands its presence in the region. The two parties commenced negotiations in April 2016, moved swiftly to form a partnership, and launched operations in February 2017. Per the terms of the joint venture, Chint holds 51% of shared while EGEMAC owns the remaining 49%. While CHINT is seen as China's largest industrial electrical company in terms of sales and production volume, EGEMAC plays an important role in supplying trained workforce and manage sales channels.

Chinese companies' expansion in Egypt reflects the country’s growing potential as a MENA manufacturing hub. Since the 2011 revolution, the industrial and manufacturing sector have been a key element of the Egyptian government’s economic growth story, with industrial growth increasing by 30 percent in 2017.

The government has encouraged investment through the Industrial Licensing Act, the pound flotation, and restrictions placed on non-basic imports. According to the Industrial Development Authority (IDA), 2085 new factories have opened since 2016 with a total investment value of $3.3 billion.

With more comprehensive partnerships fostered between Chinese and Egyptian businesses, it is clear that China will be a key partner in Egypt's growth story.
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Government-led Cooperation
Infertile Ground for Infrastructure Projects

Egypt is a promising new market for Chinese-led infrastructure projects; however, large-scale projects often fail reach fruition. Chinese companies interviewed for this study attributed the failure of these projects to the challenges during the government negotiation process around project scale, pricing and partnership structure.

In 2015, for example, the Egyptian government announced plans to construct a new USD $4.5 billion administrative, financial and commercial capital between Cairo and Suez, but due to setbacks, the project has yet to start.

In 2016, China State Construction Engineering Corporation (CSCEC) was awarded a USD $3 billion contract for the first phase of construction, but disputes over pricing and design led to the project’s suspension of the project and endless re-negotiations. The following year, the China Fortune Land Development (CFLD) reached another agreement with the Egyptian government together with CSCEC for the construction and development of the second phase of the project with an estimated cost of $20 billion. No updates have been publicized, but it is reported that budget cuts led to the departure of Chinese contractors. CSCEC has refused to comment on the project, and CFLD has yet to set up an office in the country.

The Egyptian government similarly proposed an electric rail line in 2015 to connect Cairo and the proposed new capital. Following two years of negotiations, the Aviation Industry Corporation of China (AVIC) and China Railway Group Limited (CREC) were awarded the contract for the USD $1.2 billion project, financed by the Export–Import Bank of China and the Egyptian government in 2017. According to interviewees involved in negotiations, the decision-making process was prolonged due to the Egyptian government’s reservations regarding the cost of the project.

The sole China-Egypt infrastructure project to be recently realized is an upgrade of the national electricity transmission, which was contracted to the China State Grid Corporation in 2016. The USD $760 million electrical line, funded by the China Development Bank, Export–Import Bank of China and the Bank of China, marks the first successful project within the China-Egypt industrial capacity cooperation initiative. As these examples highlight, successful government-led projects between China and Egypt are few and far between due to poor negotiations.
Suez Canal Economic Zone and Teda Industrial Zone

Launched in 2015, the Suez Canal Economic Zone (SCZone) has been billed by the Egyptian government as the most important special economic zone in the country’s history. Located on the banks of the Suez Canal, the SCZone aims to promote trade and industrial development. With 8% of global trade flowing through the Canal, the SCZone is critical for Egyptian job creation and economic growth.

SCZone is situated on the banks of the new Suez Insofar, China is the biggest investor in both the SCZone and Suez Economic and Trade Cooperation Zone in Ain Sokhna, which is also known as Teda Industrial Zone (Teda).

Teda was the subject of national attention when Chinese President Xi Jinping and Egyptian President Abdel Fattah al-Sisi jointly attended the nameplate unveiling ceremony of the second phase project in 2016. However, China-Africa Teda Investment Co. Ltd faces numerous challenges in developing the second phase.

Firstly, attracting Chinese investors becomes more difficult due to a lack of policy support put in place by the Egyptian government, as a result of the unfamiliarity with PPP structures. Furthermore, companies entering Teda no longer enjoy preferential tax treatment. As a result, Teda no longer has unique advantages that differentiate it from other industrial areas such as 6th of October City and the Ramadan 8th City. Furthermore, Teda also faces challenges in attracting investments due to poor access to finance, policy and regulation uncertainty as well as poor water and electricity infrastructure.
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Impact of Political Uncertainty
Impact of Political Uncertainty

In recent years, Egypt’s political turmoil has been the subject of considerable international concern. As a crucible of the Arab Spring, former Egyptian President Hosni Mubarak lost power in 2011. After six months of chaos, an interim government headed by Prime Minister Kamal al-Ganzouri emerged. Six months later, Mohammed Morsi from the Muslim Brotherhood was elected as president in mid-2012. In the following months, President Morsi’s Islamist decrees and policies triggered an uptick in street violence and finally contributed to a military coup in mid-2013. By mid-2014, the U.S. government declared the Muslim Brotherhood a terrorist group and the former army chief Abdul Fattah al-Sisi was elected as President. Between 2014 and the present day, extremist groups such as the Islamic State in Egypt have launched dozens of attacks to undermine the current government.

Despite the ongoing perception that these political phenomena have disrupted foreign investment in Egypt, some interviewees voiced that political turbulence has actually attracted several Chinese companies to Egypt; while most foreign companies from nations such as Japan and Germany exited the Egyptian market during the two revolutions, which created a market vacuum. The political uncertainty further undermined investor confidence and led to a decline in the value of the Egyptian pound, land and raw materials, which greatly lowered the costs of doing business in Egypt. During the power transition, as the Egyptian government scrambled to attract more investors, “everything became possible” (according to one interviewee) from registering a wholly-owned company by foreigners in a certain industry (which was not allowed under the investment laws), to obtaining certificates and permits. Private construction, for example, gained additional momentum during the turmoil due to a lack of building regulations, which greatly benefited construction and building material companies.

According to multiple interviewees, the Egyptian government has adopted an attitude of flexibility, leniency and cooperation with foreign investors that was seldom present in the past.
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Emerging Opportunities in Egypt
Emerging Opportunities in Egypt

Manufacturing Industry Set to Expand

Based on the success of manufacturing companies such as Jushi and Chint-EGEMAC in Egypt, several large manufacturing Chinese firms are now considering expansion within Egypt. FAW Group Corporation, for example, recently began to distribute a range of products including cars, vans, and heavy-duty trucks in Egypt. During FAW Group’s opening ceremony in June 2017, the company indicated its interest in exploring the possibility of establishing an assembly factory in Egypt should local sales prove promising. Three other car manufacturers, BAIC Group, Geely Automobile, Changan Automobile, are reportedly considering similar plans.

The Growing Female Economy

Women now control over $20 trillion in annual consumer spending, a figure that is set to rise as women gain more autonomy and increase their purchasing power. In Egypt, the beauty industry is one such sector poised for growth as the country’s well-developed tourism industry and its growing middle class continue to expand. At present, Egypt has a population of 89 million people and is the third largest country by population in Africa. Hair salons, nail salons, and spas are now commonplace throughout major cities. While no large Chinese beauty companies currently operate in Egypt, there may soon be opportunities to collaborate through technical vocational education and training (TVET), franchising, and joint-ventures.
Conclusion

The arrival of Chinese enterprises in Egypt has been turbulent, but sectors such as manufacturing and textiles show a promising future for Chinese investors hungry for returns. While Chinese firms have struggled to navigate Egypt’s political uncertainty and currency crises in the past, those that have weathered political and economic storms have demonstrated considerable resilience. Long-standing businesses in the stone-material processing sector, for example, have come together to collectively navigate currency crises, while investments in textiles have shifted to pivoted by increasing exports to nearby lucrative markets in Europe and the Middle East. Despite setbacks and delays in infrastructure and engineering projects in government-led projects, Chinese enterprises are now experimenting with joint-ventures and industrial park development with the Egyptian private sector.

Challenges still abound in various aspects of business such as business registration and licenses, access to finance, customs and trade control and access to land. Yet the growing interest of Chinese companies in Egypt as a production center and investment destination make it one of the most promising hubs of activity in the emerging China-Middle East-Africa trade corridor.
About Botho Emerging Markets Group

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For over a decade, Botho Emerging Markets Group has been a leader in guiding Fortune 500 companies, governments, development institutions, small businesses, and nonprofits in navigating the world’s fastest growing markets.

We are entrepreneurs and investors, thought leaders and scholars. Creatives and innovators connecting capital, catalyzing conversations, and creating opportunities to implement solutions to complex global problems. We’re guided by a common set of values: curiosity, collaboration, and impact.

What we learn from collaborating closely with SMEs and multinational companies as well as government and international organisations, we share to advance a more sustainable, inclusive world.