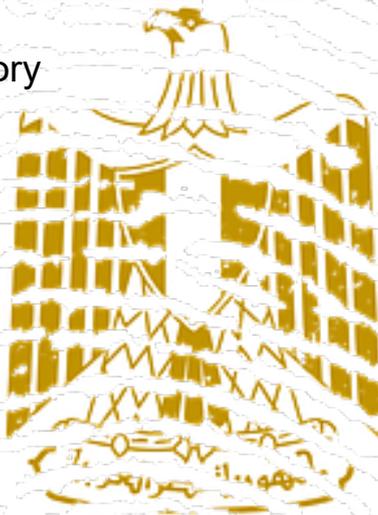




 KCS Country Risk & Threat Advisory

KCS Group Europe
Risk & Threat Advisory paper

Political Risk Advisory Briefing: Egypt
July 2019



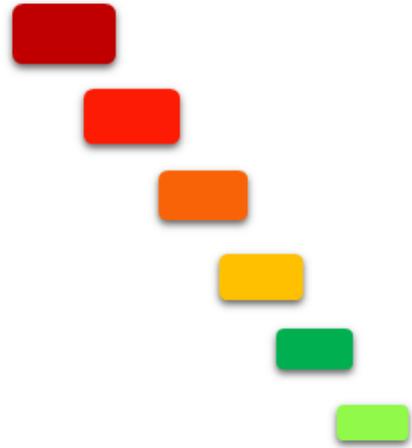


Political Risk Advisory Briefing: Egypt

GDP:	\$235.4bn USD
Population:	97.55 m
Source:	Trading Economics

Egypt has a Possible risk rating of 4

- | | |
|------------------------|--|
| 6 Very High | The assorted threats described in the report are almost certain to have a derogatory effect. |
| 5 High | The threats are extremely likely to negatively affect the business. |
| 4 Very Possible | There is a strong likelihood of problems arising in this country. |
| 3 Possible | There is a fair chance of problems arising in this country. |
| 2 Low | There is a low likelihood of any threats impacting business. |
| 1 Very Low | There are virtually no impediments to successful business in this country. |



Politics

Egypt is in need of an identity, both outward-looking and internal. Having suffered almost permanent political and social upheaval since the Arab Spring of 2011, terror attacks and ongoing instability mean that the country is struggling to consolidate a position, and a role, in regional and international affairs.

Successive coups and changes of government from 2011 onwards, after thirty years of one-man's strongman rule by Hosni Mubarak, have resulted in a Presidential, parliamentary system which last oversaw a Parliamentary election in 2015 and a Presidential one in 2018, both of which proved highly controversial: turnout in 2015 was in some regions as low as 10%, while multiple international observers considered the 2018 election to be farcical and unfair.

While President Sisi's administration and support comes with its own set of problems, there is also a religious angle to the strife. The Muslim Brotherhood took power in 2011 but were themselves forced out of power three years later by Sisi. It is now illegal for any political party in Egypt to have an explicitly religious dimension, and the Brotherhood itself - in a move supported by the USA - has been proscribed as a terror organisation. Worse, the death of Mohammad Morsi in June 2019 – ostensibly as the result of illness – has left the Brotherhood in even further opposition to the authorities.

While Sisi has drawn praise for some economic reforms and quality-of-life improvements, to say that he is a popular and democratic President would be severely overstating the case. Not only have the elections to date been shams, he has curtailed freedom of the press and deepened the crackdown on political dissent, won a referendum to allow him to stay in power until 2030, and enhanced the standing (and power) of the military on which he may, like so many strongmen, come to depend on. Sisi retains some measure of public support, and this – coupled with the loyalists that pack out the Senate under the influence of the military – should insulate him no matter what measures he puts forward.

There were also concerns dating back to 2014 that the Upper Region of Egypt wanted to secede, much like South Sudan did from Khartoum, which would not only imperil the country from a social and security perspective but severely impact its economy. As of 2019 nothing substantial has come of this but it is a sign that instability and contention still linger.

While Egypt avoided the outright civil war and dragged-out violence that were visited upon its neighbours, it is still fighting internal political conflict (not least from a resurgent Brotherhood), battling accusations of widespread human rights abuses and attempting to position itself as a destination for tourism and investment in the face of upheavals in the security and economic spheres.

Another revolution does not appear to be expected at present, but the number of issues bubbling under the surface mean that nothing can be definitively ruled out. Sisi's Constitutional changes, the proscribing of the Muslim Brotherhood and the continuing lack of social and infrastructural improvements are all fuelling resentment and could combine to push the general populace over the edge. As the opposition politicians are ignored and the media voices silenced, the dissatisfied must shout ever louder to be heard. This will undoubtedly bring attention – and it is how Egypt reacts in the eyes of her citizens and the world, that will ultimately dictate whether her future path is to be commended or condemned.

Economy

Sisi inherited an economic mess and, to his credit, steps have been taken to reform this. Despite having to seek a \$12bn USD loan from the IMF in 2016 after the Morsi-led crisis years, he has succeeded in lowering the deficit, decreasing the levels of subsidies and has arguably made Egypt an attractive investment and business destination from an economic standpoint.

The economy as a whole is expected to grow 5.6% by the end of June 2019. Investment since the Arab Spring has been more difficult to come by but with economic growth rising in the short-term, strengthening the conditions for business and seeing more money put back into infrastructure, services and so on should see a steady revival – although this is dependent on the continuing success of domestic policies. It is worth noting that this figure itself is lower than the government's own target.

The private sector is the one struggling the most, recently seeing its seventh straight month of contraction and with growth in only five of the last thirty-six months.

The exception to the above is the energy industry, with production of oil and natural gas flourishing despite the political travails. Indeed, Egypt is now entirely self-sufficient in the production of natural gas. It is actively encouraging international oil firms to the country, and with reserves of 3.3bn barrels can offer them work for years to come.

It has also signed a Memorandum of Understanding with the EU's European Energy Commission to look at becoming a 'hub' for production and export to the continent. The economic advantages of this, for all sides, should not be underestimated: it allows Egypt to receive significant investment and improvement, while giving it a wider range of clientele and options should relations with neighbouring Middle Eastern states sour. Egypt's downstream industry is the most advanced in Africa, and \$14bn USD has been promised by 2025. While accepting that it is a finite resource, the government is determined to extract as much value from oil as it can, and this means that the short-term investment climate is very buoyant indeed.

The state of Egypt's economy is arguably the strongest it has been since 2011, and perhaps even since the early days of Mubarak's emergency rule. However, this brings with it its own corollary – the stronger the economy becomes, the more Sisi will use this as justification for his reign to continue. A fine line must be trod between economic advancement and political capitulation.

Corruption

It is said that 'everything is connected' and regrettably this is the case in Egypt, with corruption prevalent across public and private sector businesses and at multiple sectors and walks of life. Firstly, and most notably is the degree to which Egypt has now become a military state in all but name, with Sisi (and Mubarak before him) being reliant on military backing to remain secure. It is now enshrined within the constitution, too: no longer is it the role of the military to *'preserve Egypt's security and territories'* but also to *'preserve the constitution and uphold the gains of the people'*. While on a political level this is intended to future-proof Sisi against any potential uprising or coup, in practical business terms it means that the hard- and soft-power of the army is significant and will have an even greater role to play in patronage and control. If it dominates the economy, then it dominates politics as well.

Clearly this does not bode well for anti-corruption as a whole in Egypt, and as Egypt further embraces authoritarianism it becomes harder to combat the corruption that is both a driver and a consequence of it.

As to specifics, Transparency International have raised their outlook for Egypt from 117th to 105th and registered its third best corruption perception score since the revolution.

But the spectre of Hisham Geneina, former head of the Central Auditing Organisation, looms large – he claimed that \$76bn had been embezzled and wasted by the authorities in just three years between 2012 and 2015, and although Geneina was sentenced to a year in prison for ‘disseminating false news’, no explanation was given by the government for the missing money. The bureaucracy is famously opaque, and bribes are commonplace at many governmental/authority levels.

Business Environment

As a destination able to straddle both the Middle East and Africa, Egypt understands both the advantages, and necessitates, of making itself attractive, particularly when its near neighbours are in ongoing civil war (Libya) or facing global censure (Saudi Arabia). In addition to the measures to improve the domestic economy and infrastructure, Egypt has been looking at ways to facilitate those coming from abroad, with the Minister for Investment claiming that Egypt is being positioned as *‘a global investment destination [with] comprehensive improvements in the business environment’*. In practice, this means a greater opening up to the private sector and a willingness to accept more Foreign Direct Investment. Egypt already receives more FDI than neighbouring countries (albeit declining by almost \$1bn so far in 2019) and has fixed on this as a means of creating jobs and enhancing the economy. Firms are also being buoyed by new laws regarding investment and tax designed to incentivise them to invest in Egypt for the long-term (very much the preferred outlook of the government).

But there are still gaps in the legislation and, indeed, the culture. Anti-corruption laws are, at best, arbitrarily applied and the lack of legal protection for whistle-blowers means that multiple cases of serious fraud may go completely unchallenged.

Foreign Affairs

Egypt has openly sided with the Saudi Arabia-led coalition against Qatar in the ongoing regional dispute. While at time of writing this has not led to actual violence, the sanctions and restrictions placed upon Qatar by almost all of its neighbours are seen as a proxy to put pressure on Iran – and it is here that the wider problems would occur. Iran is openly threatening to breach its imposed limit on enriched uranium supplies in the face of US troop deployments and it is difficult to see how Egypt could avoid getting involved in a regional conflict if it is to keep its promises to Saudi Arabia and the UAE.

Sisi's characterisation of the Middle East region is one of 'creative chaos' and as such he has sought to mitigate this by rarely participating in full-blown military action, preferring instead to support via air strikes and push the dialogue solution. Sisi himself announced "we do not want to be a leader; we want to be partners". It is to be hoped that this will be demonstrated not only in political actions, but in business and economic spheres as well – co-developing and funding projects that enhance the region as a whole, and improving the attractiveness of the business environment so that both domestic citizens and foreign companies can mutually benefit.

Criminality/Terrorism

Egypt continues to be riven by the occasional terror attack, whether on a grand scale (the exploding of Metrojet 9268 in 2015) or smaller attempts (a May 2019 attempt to kill tourists at the Pyramids of Giza). The situation is unlikely to get better anytime soon. Not only does Islamic State consider Egypt to be a major battleground in their territorial/political ambitions – sitting as it does right between the Maghreb and the Middle East in a tinderbox area – but the proscribing of the Muslim Brotherhood as a terror organisation and the ill feeling caused by this repression will destabilise the situation further. It will become easier for hardliners to claim suppression and the need for retaliation, which in turn will only foment further violence.

The tourist industry has been the hardest hit, although numbers in 2018 were notably higher than any year since the Revolution, business had been struggling as well with safety and surety in what remains a tinderbox environment. It is to be hoped that the recurrent tourist trade will spur a similar upswing in business interest, regardless of ongoing conflict in the Sinai and the ever-looming spectre of asymmetrical violence.

What Grey Area Dynamic threats is Egypt likely to pose?

Much of the issue base in Egypt is passive: matters that are always present behind-the-scenes either in law or expectation, and which must be remembered and dealt with during any deal. For instance, the bribery, corruption and vested interests which permeate business and government society, and the customs/traditions that can initially be off-putting to perceived Western actors. But there is also a strain of what is best termed active legality: issues over true ownership, the pace and scope of bureaucracy, and hostility that comes from a party-line press and rampant military control.

APPENDIX

GREY AREA DYNAMICS

Over the years, KCS has made it their business to find workable solutions to impossible problems. To do this, KCS has sought to establish clearly the intelligence gap between perception and reality.

In today's market where terrorism, organised crime, cybercrime and government sponsored cyber espionage and war appear to confront us daily, we need reliable tools to identify the risks well in advance. It was for these reasons that KCS created and developed the analysis of risk by Grey Area Dynamics or GAD's, as they are often referred.

GAD's are all the risks, weakness and threats that will, at one time or another, interfere, disrupt or at worst close down businesses. In the projects and work in which KCS have been involved in all over the world, it has been evident that the GAD's identified, can and do kill. This method of risk assessment and measurement goes well beyond standard due diligence and is a collective description of factors, which can be passive and non-passive, legal and illegal. Because GAD's are difficult to quantify or assess from a purely economic viewpoint, these considerations do not normally feature in most credit ratings, investment and banking reports, which focus only on sovereign risk.

The main categories of Grey Area Dynamics usually encountered are:

Passive/Legal

- Language & Dialects
- Local Customs & Traditions
- Local Staff – motivation and training
- Tribalism and Integration
- Cultural & Local sentiment
- Regulations, Taxes and Duties
- Currency & Capital exposure – payment methods and banking practice
- Environmental Hazards
- Pressure Groups
- Media Relations

Non-Passive/Legal

- Industrial & Labour Relations
- Absence or effectiveness of Legal Safeguards
- Government Policy and Nationalisation
- Overt and disguised/beneficial ownership
- Bureaucracy and Local Government
- Public or Media hostility

Passive/Illegal

- Bribery & Corruption
- Vested Interests and Cronyism
- Patronage
- Product diversion
- Parallel Trading
- Hidden Barriers to entry

Non-Passive/Illegal

- Counterfeit & Fraud
- Pilferage
- Unfair Market Competition
- Product Piracy
- Ethics and Corporate Espionage
- Organised Crime
- Threats to physical assets
- Kidnap & Extortion
- Religious Extremism
- Terrorism
- Civil Unrest
- Product Contamination

For a risk assessment to be thorough, it must encompass the potential for a broad array of economic, political and business situations that might affect a business venture. Evaluations limited just to political issues or financial factors may be completely misleading.

The degree of severity of a risk portfolio will also depend on the origin of the investing entity; for example, European companies often face different risk profiles to American corporations considering the same investment opportunity.

Grey Area Dynamics pose a challenge of diagnosis¹. The key to avoiding problems before they occur or solving them after they have begun to take a toll on performance, lies in their early identification and evaluation. Ignoring the impact of GAD's can be a costly business.

¹ KCS Group Europe won the European Service Provider of the Year, 1999-2000 at the European Risk Management Awards magazine International Risk Management for their work on GAD's. In 2004, the company won an award for Product of the Year from StrategicRisk.