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Swiss economic development co-operation with Egypt

1. Economic context: an overview

■ The Arab Republic of Egypt is a major geopolitical player in the Middle East and an important economic actor in the Mediterranean region with a population of about 73.4 million (the largest in the Arab World), 33% thereof under the age of 15.

■ The country has made considerable progress in macroeconomic stabilization and structural reform since embarking on a structural adjustment process in 1991 aiming at deregulation, liberalization of trade and promotion of private initiative and investment. During most of the 1990s, very positive results were achieved and the GDP growth rate averaged 5 % per year. Tighter fiscal discipline, downsizing of the bureaucracy and increased liberalization modified the Egyptian economic environment, as well as the structure and pattern of growth. During this period, private investments increased substantially and eight new jobs out of ten were created by private enterprises (only five in the 1990s).

■ In parallel, some important human development indexes have significantly improved over the past ten years: life expectancy increased by 5 years, maternal mortality decreased from 174 to 84 per 1000 births, children mortality reduced from 85 to 44 per 1000 births, while the literacy rate improved from 50% to 56%.

■ In the late 1990s, however, economic performance weakened with a substantial fiscal deficit, a rapid credit growth and a slowing in structural reforms. The situation even deteriorated during the period 2000-03, following the difficulties related to September 11 and the war in Iraq. During this period real GDP growth (1.8 % in 2003) remained considerably below the minimum required to absorb labor force growth and reduce poverty.

■ Since mid-2003, the country is experiencing a gradual economic recovery (real GDP growth of 2.7 % in 2004), which should further be strengthened by the implementation of the reform program of the new Cabinet appointed in 2004. A series of decisive measures, including trade and tariff reform, foreign exchange market reform and adjustments in administered prices have already been adopted. The first multi-candidates presidential election to be hold in September 2005 will

represent an important political milestone but could also bring some turbulence with a possible negative impact on the pace of reforms.

■ Much remains to be done to push forward the necessary additional reforms to sustain growth and reduce poverty. Income per capita (USD 1'400) is in the lower range of the middle-income countries. Egypt is also confronted to persistent high vulnerability to external shocks. The country has still to face daunting challenges, including:

- The demographic growth rate is higher than in comparable countries (1.9% per year). Unemployment is increasing (currently 11%). About 600'000 to 800'000 new jobs must be created every year in order to absorb new entrants on the market. To control unemployment, Egypt will need to achieve a real GDP growth rate of 6%.
- 23% of the population still remain below the poverty line, with more than 12% of children under the age of 5 suffering from malnutrition.
- State control, overwhelming administration (about 6 million civil servants) and regulation of the economy remain heavy. With a share of 3, respectively 15 % in government revenues and expenditures, local governments are almost inexistent and Egypt remains one of the most highly centralized countries.
- Egypt's economy is confronted with a persistent high vulnerability to external shocks and a heavy dependence on the US support (2003: USD 1.3 billion in military aid and USD 615 million in social programmes). Its external debt is rising (2003: USD 32 billion; 2004: USD 33.8 billion).
- The current level of investment (about 23 % of GDP) is insufficient to secure sustained high growth. Moreover, the flows of Foreign Direct Investment (FDI) to Egypt dropped from USD 1 billion in 1998 (fuelled by the Asian crisis) to USD 237 million in 2003. The persistence of such a trend may become a serious problem..
- Public finances remain fragile (fiscal deficit 6.1 % in 2004). The Cabinet's decision to lower customs tariffs will most probably stimulate economic activity and raise consumption, investment and output, but may, in the short term, further widen the fiscal deficit.
- The reform of the financial sector is overdue, the financial intermediation is inefficient and State-led "pharaonic" projects such as the Egypt Southern Valley Development Project massively restrain the lending capacity to private entrepreneurs.
- Corruption remains pervasive.
- Regional and internal political developments (Islamic opposition, human rights, democratic process, etc.), as well as international prices fluctuations (oil, cotton, etc.) will continue to have a direct impact on the socio-economic progress of the country.

- Environmental degradation is severe, particularly in the densely settled areas of the Nile valley and the delta.

■ Egypt is a country with a big economic potential and represents an important emerging market (2004: imports USD 12.1 billion; exports USD 20.9 billion). The Government's current economic policy underlines the importance for the country to maintain a sound and prudent macroeconomic policy, to promote a more active role of the private sector in the development process and to better tap the potential of trade as an engine for sustainable growth. It is committed towards a market-based economic development and the achievement of the Millennium Development Goals. These efforts deserve to be supported by the international community.

■ With exports amounting to CHF 391.5 million (2004), Egypt is the second largest export market for Switzerland on the African continent. Imports are on the increase amounting to about CHF 32.6 million (2004). According to statistics, Swiss investments in Egypt amount to about CHF 413 million (2002) and rank third (just after South Africa and Botswana). Egypt plays the role of business hub for North Africa and the Middle East. Agreements on the Protection of Investment and Avoidance of Double Imposition have been signed respectively in 1973 and 1987. Negotiations for the conclusion of a free trade agreement with the EFTA-States are ongoing.

2. Past experiences and lessons learned

■ The co-operation programme of **seco** in Egypt has been developed over the past 20 years. The financing of basic infrastructure – through mixed financing lines amounting to a total of CHF 330 million – has been the main pillar of this co-operation. So far, priority has been given to rehabilitation projects and projects supporting the economic reform program. With the 4th mixed credit line, opened in 1997, conditions have further been adapted to the OECD rules and restricted to commercially non-viable projects.

■ In addition, a partial cancellation (CHF150 million) of the bilateral debt was granted in 1995 and, in parallel, the Egyptian-Swiss Development Fund (endowed with local counterpart funds equivalent to CHF 90 million) was established. After the Gulf War, additional bilateral assistance has been provided including the rescheduling and reduction of the bilateral debt with a contribution of CHF 30 million to the establishment of the Social Fund and targeted technical assistance.

■ The main experiences and lessons drawn from the economic development co-operation with Egypt during the past many years can be summarized as follows:

- good and constructive working relations with the Egyptian authorities and partners. Easy access at the decision-making level whenever necessary, thanks to the excellent contacts and network of the Swiss Embassy in Cairo;

- bureaucracy is pervasive and delays decisions or implementation. An active local involvement (through Swiss executing agency or Embassy) is essential to ensure a reasonably smooth process;
- the bilateral donors must remain humble and realistic as regards their capacity to influence “policy orientations” (for example the water tariff for irrigation). Networking and coordination with multilateral or multi-national partners is essential to ensure a coherent sector policy dialogue;
- despite its constraints (tied aid), mixed financing remains a relevant and useful instrument (soft loan) for financing basic infrastructure in Egypt, subject to the following key conditions: (i) focus on one or two priority sectors only; (ii) meet sound development criteria; (iii) target exclusively commercially non-viable projects; (iv) integrate adequate accompanying capacity building or technical assistance; (v) ensure transparent and efficient joint implementation mechanism (PIU);
- taking into account the changing economic environment, co-operation in Egypt must gradually disengage from the public sector in the medium-term and increasingly target partners and operations in the private sector;
- permanent efforts are required to increase the visibility of **seco**’s assistance to Egypt;
- many international donors are active in Egypt. In comparison, **seco**’s contribution is quantitatively small, making it necessary to enhance coordination with like-minded donors and/or focus on specific niches;
- excellent working relations with the Swiss Embassy in Cairo; there is however a need to formalize the actual delegation of tasks and responsibilities in the implementation of the **seco** development co-operation program, taking also into account the capacities and resources.

3. Future orientation

■ Egypt is a middle-income developing country, with an emerging economy. It represents an important market and offers substantial potential for growing business relations with Switzerland. Taking into consideration the progress achieved so far under the EU – Mediterranean Partnership, the early conclusion of the negotiation of an EFTA free-trade agreement with Egypt is important to ensure a non-discriminatory treatment of EFTA Members’ enterprises in their trade relations with Egypt. This dimension needs to be fully taken into account in **seco**’s future bilateral economic co-operation with this country.

■ The economic development co-operation of **seco** with Egypt should aim at supporting the country's continued efforts towards sustained and strong growth – in the frame of an increasingly market-based and open economy – and contribute thereby to the overarching goal of reducing poverty.

■ Nevertheless, it must also be recognized that the impact of **seco's** assistance program on growth and development are and will remain – despite substantial financial allocations – rather limited and localized, due to the size of the country and its needs and also due to the extensive activities of other donors.

■ Taking into account all these various factors, the future orientation of **seco's** program needs to be articulated along the following lines:

- build on the positive experience gained in the field of infrastructure development, **fully integrating the new seco policy on mixed financing** (sector concentration, commercially non-viable projects only, related technical assistance, joint project implementation unit, etc.);
- progressively shift the co-operation program from an exclusively “public-sector” approach towards **partnerships with stakeholders of the private sectors**, also exploring the possibilities of an involvement in a Public Private Partnership;
- privilege close co-operation with multilateral and like-minded bilateral donors to develop **targeted policy dialogue** with the Government;
- provide adequate attention to the requirements of **capacity building**;
- favour a **“niche” approach** focusing on projects or activities with strong innovation and high demonstration effect;
- create **synergies** between different **seco** programs;
- implement **results-based** project management and incorporate clearly defined performance indicators (including expected contribution to poverty reduction);
- reinforce the **visibility** of the **seco** co-operation program.



Thematic focus/domains of action

■ After due consideration of the priorities set by the Government in its Poverty Reduction Strategy, taking into account other donors' programs and their experiences in the country, and after assessing **seco's** capacities and resources, the main avenues for future co-operation have been identified – in close consultation with the Egyptian Government - as follows:

Basic infrastructure

■ The level of public investment in basic infrastructure is insufficient to face the demand of a fast-growing population and to contribute effectively towards a sustained and strong economic growth in the medium-term. Inadequate provision of infrastructure (lack of funds, deficient maintenance, inefficient management and tariff policy) has a negative impact on the level of private (national and foreign) investment in the country, which in turn affects economic growth. The fragile public finances and the Government's debt will continue to constrain public investments in the years to come. In this context, Egypt further requires access to foreign soft loans in order to mitigate this funding constraint. The Swiss Mixed Financing (MF) represents a valuable option – financing the delivery of Swiss goods and services for priority and commercially non-viable infrastructure projects in selected sectors – for the Egyptian Government.

Strategic Orientation:

- **seco** will consider making available a 5th Mixed Financing line (CHF 60 million, 50% grant element). This new MF line shall be used for a maximum of two sectors, possibly health and environment/water, for commercially non-viable projects meeting sound development criteria.
- The modalities of the MF should ensure a strong project management (for example in the form of a joint Project Implementation Unit) and adequate accompanying technical assistance. Whenever possible, **seco** will make special efforts to ensure that *gender concerns* are being addressed in specific projects or programs (in particular in the health sector);
- for the selected MF sectors, **seco** undertakes to coordinate more closely with multilateral or like-minded bilateral donors in order to contribute towards the sector policy dialogue with the Government.

SME development

■ To sustain the development of a dynamic private sector, Egypt must address the needs and requirements of Small and Medium-size Enterprises (SME). Their potential contribution to job creation, technology innovation, diversified exports or industrial decentralization – and the related

impact on poverty reduction – is enormous. With the liberalization of trade, State's divesture and deregulation of the economy, some substantial progress has already been made. But, many issues have still to be addressed to further improve the business environment and reduce persistent red-tape and administrative barriers hampering private entrepreneurship. Moreover, the access to long-term finance remains a major constraint for SME.

■ **seco** is aware of the huge needs and requirements to develop the SME sector in Egypt. Its approach is therefore to contribute in a selective and targeted manner in areas where innovative activities or instruments could have a strong demonstration effect, or where **seco** avails of a specific competence or capacity to address specific priority needs.

Strategic Orientation:

- **seco** will contribute to efforts aiming at improving the business environment and delivery of related technical assistance and capacity building, mainly through multilateral initiatives or programs;
- **seco** will support the establishment and development of innovative term-finance mechanisms for SME, which could include leasing, credit-guarantees schemes of private banks or SME-targeted venture capital funds;
- the **seco**-funded Swiss Organization for Facilitating Investments (SOFI) will play a pro-active role in Egypt, to stimulate the potential interest of Swiss or OECD enterprises to invest in Egypt (information on risks and potentials, efforts for matchmaking of enterprises, support to processes aiming at new investments);
- **seco** will contribute to efforts aiming at more eco-efficiency, by the establishment of a Cleaner Production Centre aiming at advising SME on how to optimize their production processes while adopting environmentally sound technologies.

Trade promotion

■ Egypt undertook significant reforms of its trade regime in the early 1990s (reduced tariffs, removal of many quantitative restrictions, efforts towards foreign trade agreements). However, the country's level of industrial protection remains high; substantial additional progress has still to be made for achieving a better integration into the world markets. Egypt's position in international markets has indeed been further marginalized over the past ten years and represents today only 0.08% of world exports and 0.3% of world imports. Export performance is particularly unsatisfactory (accounts for less than 1% of GDP), also because of limited progress in diversification (2/3 of merchandise exports are still petroleum-related), insufficient product adaptation and market identification (e.g. focus predominantly on industrialized countries, neglect

of sub-Saharan Africa). The potential of trade as an engine for growth is far from being fully tapped in Egypt.

Strategic Orientation:

- selective assistance (sector approach) by the Swiss Import Promotion Programme (SIPPO) to support Egyptian SME in the design and marketing of their products to fit European standards, and to facilitate contacts with potential Swiss or OECD buyers;
- targeted support – in close coordination with the Ministry of Trade – to improve the efficiency of trade operations and promote Egyptian exports, to be implemented by a multilateral partner (possibly the International Trade Centre, Geneva);
- bilateral targeted support in the following possible areas: (i) customs (selective training and capacity building); (ii) technical barriers to trade; and (iii) intellectual property rights;
- availability of **seco** to continue promoting regional trade and economic development.

Indicative financial disbursements

■ For the implementation of its programme during the period 2005-2008, **seco** plans – subject to continued progress of the country in the reform of its economy and timely completion of the negotiations with EFTA – the mobilization of an envelope of **about CHF 50 million** (total grant and loans). Efforts will be undertaken to smoothen the annual disbursements, but the nature of the main operations (in particular the mixed financing projects) will most probably lead to continued erratic annual flows.

4. Program management

■ In Berne, the directly involved **seco**-cooperation (WE) divisions are: (i) Infrastructure Financing (WEIN); (ii) Investment Promotion (WEIF); and (iii) Trade and Clean Technology Cooperation (WEHU). **Ms Claudia Taverna (tav/WEIN)** is the **WE country coordinator**.

■ The **Swiss Embassy** in Cairo is the direct Swiss partner of **seco** in Egypt. It ensures the local coordination and management of the WE program. To strengthen further this cooperation, a detailed arrangement will be formulated together with the Embassy and other concerned partners, to specify the respective expected tasks and responsibilities, and to address – if required - the related questions of capacities and resources.

Annex 1

Swiss development aid flows (million CHF)

		1998	1999	2000	2001	2002	2003	2004
seco	<i>grants</i>	9.4	15.8	10.8	4.2	4.7	2.45	1
	<i>MF/loan component</i>	8.8	14.7	10.5	3.9	3.2	2.0	-
	total	18.2	30.5	21.3	8.1	7.9	4.45	1
SDC		0.6	0.5	0.7	0.8	N/A	0.8	0.7
Swiss Total		18.8	31.0	22.0	8.9	7.9	5.25	1.7

Comments and remarks

- The above-mentioned figures refer exclusively to the bilateral annual net flows.
- The table does not take into account the benefits of Egypt from global or regional **seco** and SDC programmes such as SOFI, SIPPO, etc..

Annex 2

On-going projects and programs

Basic infrastructure

- *Mixed Financing Line IV*

Mixed Financing Line IV has been in force since 1999 and has been used extensively. Currently, two major projects are implemented: the Rehabilitation of the Blood Transfusion System and the Radiology Project Phase I with the Ministry of Health. Furthermore, **seco** supports the Rehabilitation of Irrigation Pumps in Upper Egypt with the Ministry of Water Resources and Irrigation.

Sector: Health, Irrigation
 Amount: CHF 80 million, an increase by another CHF 20 million has been ratified by the Egyptian parliament in 2004; (Swiss Government grant: 50%, Commercial bank loan: 50%)
 Duration: 1999-2007
 Partner: Ministry of International Co-operation
 Internet: For project details, please refer to www.seco-cooperation.ch

- *Public Private Infrastructure Advisory Facility (PPIAF)*

This facility aims at promoting private infrastructure development in developing and transition countries through national strategies, formulation of the necessary laws and regulations, preparation of pilot projects and capacity building in the public sector.

Sector: All infrastructures, multi country
 Amount: USD 6.23 million out of a total budget of USD 92.2 million (pledges)
 Duration: 1999-2005
 Partner: World Bank
 Internet: www.ppiaf.org

- *African Infrastructure Fund*

AIF operates all over Africa but concentrates at least 50% of its operations in selected countries, including Egypt. AIF invests in infrastructure projects in partnership with large private African enterprises.

Sector: Infrastructure (water, energy, telecommunications, transportation, sanitation and environment)
 Location: Washington D.C.
 Amount: USD 10 million from **seco**
 Duration: 1999-2009 +2
 Internet: www.empwdc.com

SME development

- *NAED – North Africa Enterprise Development / PEP-MENA*

This multidonor technical assistance programme managed by IFC started operation at the end of 2002. It assists Egypt, Algeria and Morocco in developing favourable conditions for SME development with a focus on: 1) improving access to finance, 2) supporting intermediary organisations / service providers, 3) developing linkages between SMEs and larger companies, 4) improving framework conditions (passing and implementation of laws and regulations) favourable to SMEs. Since 1.1.2005, the programme has been transformed into a PEP programme and extended to all the Middle-East (from Morocco to Pakistan and including some Gulf states) thus a change of name into PEP-MENA. NAED's original budget target was of USD 20 million and PEP-MENA target budget is of USD 100 million.

Sector: Business environment
 Location: HQ operations in Cairo
 Amount: CHF 4,9 million from **seco** (for Morocco, Algeria and Egypt)
 Duration: End 2009 (end 2005 for the Swiss contribution)
 Partner: IFC/Worldbank

- ***FIAS (Foreign Investment Advisory Services) - Africa***

Out of a dedicated Trust fund for Africa, FIAS, part of the World Bank group, offers advisory services to assist African countries in developing and implementing strategies and tools to attract foreign direct investment. Technical assistance is demand based from the concerned country. Since 2002, Egypt is eligible for assistance out of this Trust Fund.

Sector: Investment promotion
 Countries: Africa
 Location: Washington
 Amount: CHF 250'000 (non country specific)
 Duration: 1989 – 2007 (and potentially onwards)
 Partner: FIAS
 Internet: www.fias.net

- ***IFC Sustainable Financial Markets Facility (SFMF)***

The Sustainable Financial Markets Facility (SFMF) of the International Finance Corporation (IFC) has the objective to enhance the environmental and social development impact of funding via financial intermediaries (FIs) and to support the competitiveness of FIs, by improving their capacity to manage environmental risk and the continuously-evolving 'business and sustainability' agenda; It will also strategically support and influence the sustainability agenda of the broader financial community, with the objective of increasing the potential for environmentally and socially responsible investment in emerging markets. The Facility is structured around three outcome-led programs, delivered through a combination of sector-wide capacity building, institution-specific technical assistance, selected special projects, and strategic support but is non country-specific. Support from this facility is offered to developing and transition countries, including Egypt, on request.

Sector: Financial Sector
 Amount: CHF 2.3 million
 Period: 2003 – 2005
 Partner: IFC
 Internet: www.ifc.org

- ***SOFI***

Egypt is one of the 8 priority countries selected to benefit from **seco's** investment promotion mandate executed by the Swiss Organisation for Facilitating Investments (SOFI) and is therefore to benefit from proactive efforts for specific investment promotion.. Apart from information dissemination on investment conditions and opportunities (eg. trough internet, conferences, missions), SOFI provides advices to enterprises in the preparing and implementing their investment

projects and in identifying potential partners. Advisory services at a project level are paid for by the client.

Sector: Investment promotion
 Location: Zürich
 Amount: CHF 4.5 million per year for the mandate but not country-specific
 Duration: 2004-2007
 Partner: SOFI
 Internet: www.sofi.ch <<http://www.sofi.ch>>

- ***seco Start-up Fund***

To encourage and facilitate preparation and initial phases of new investment projects, **seco** provides loans to Swiss entrepreneurs up to 50% of the financing needs. A number of loans concern projects in Egypt. This financial window is being administered by SOFI.

Sector: Investment promotion
 Location: Zürich
 Amount: CHF 15 million for the revolving fund (all eligible countries)
 Duration: 1997 -
 Partner: SOFI (management agreement)
 Internet: www.sofi.ch <<http://www.sofi.ch>>

Trade promotion

- ***SIPPO***

Since 1999, the Swiss Import Promotion Program (SIPPO) has promoted import of products from developing and transition countries to Switzerland and OECD countries, through the support to local SME (e.g. product adaptation, participation in trade fairs, matchmaking) for improving their access to markets. In Egypt, the programme follows a sectoral approach.

Sector: Organic products, Fruit & vegetable, textile & fashion, trend forecasts (fashion, jewellery), general trade and market information CH/EU, workshops and seminars (export marketing)
 Location: Zurich
 Amount: CHF 6 million per year for the mandate, but not country specific
 Duration: ongoing
 Partner: SIPPO, Expolink (Egyptian Exporter's Association)
 Internet: www.sippo.ch info@sippo.ch

- *Assistance to the small-scale leather products industry, phase II*

This project, which was started in 1997 in cooperation with UNIDO and the Egyptian Social Fund For Development, has established in its first phase an information centre for the leather industry, called FLISC (Footwear and Leather Industry Service Centre). FLISC supports local industries in their efforts to improve the quality and the marketing of their products. In the second phase FLISC will further develop its financial sustainability in order to become independent from external financial resources. To enable cooperation and export of leather products, FLISC will furthermore assist the small-scale leather industry to form industrial clusters following the organizational structure as applied in Italy.

Sector: Footwear and Leather industry
Amount: CHF 970'000.-
Duration: 2003 –2005/6
Partner: UNIDO (United Nations Industrial Development Organisation), Social Fund for Development, (SFD)



Annex 3

Main Current Development Partners ¹

Type Domains	Public	Private	Multilateral/Bilateral
Basic infrastructure	Ministry of International Co-operation Ministry of Water Resources and Irrigation Ministry of Health	Emerging Markets Partnership	World Bank USAID
SME development	Industrial Business Association	Business Associations	IFC World Bank UNIDO
Trade promotion	Ministry of Foreign Trade Customs		

This Table refers only to local (national or international) partners. Swiss executing agencies or development partners are not included.



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