

Global Value Chains Diagnostic – Country Deep Dive

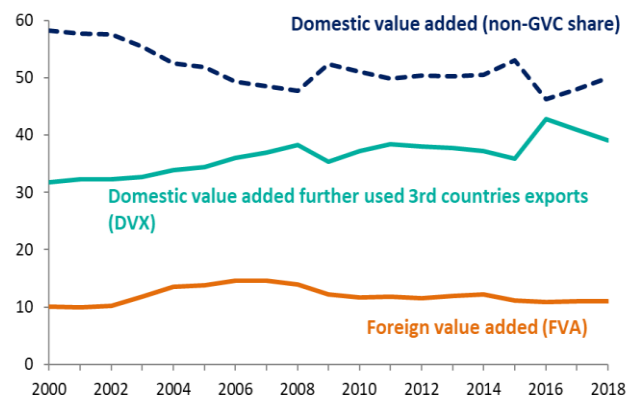
Egypt¹

- Egypt's integration in global value chains has increased but remains relatively subdued
- Strong forward linkages and weak backward linkages in value chains
- Main exports are (petro)-chemicals, horticulture, electrical machinery and textile products
- Egypt achieved to diversify its export basket and destination markets, but few firms participate in trade

Mapping the integration in GVCs

At the global level, global value chain (GVC) integration has stagnated in recent years, whereas most trade integration had happened before the financial crisis. Egypt followed the trend and increased its integration in GVCs in the 2000s, but experienced stagnation afterwards (Chart 1). In 2018, around half of Egypt's exports had value chain linkages, with 10 per cent being sourced as foreign inputs in exports (backward linkages) and 40 per cent being domestic value added that was sold to third countries via value chain linkages, where it was further processed in exports (forward linkages in GVCs).²

Chart 1: Decomposition of gross exports (as per cent of total gross exports)



Sources: UNCTAD-EORA (2018) and authors' calculations

Egypt's strong forward linkages indicate that the country is strong in exports of raw materials and intermediate goods which are needed for export production of firms in other countries. Such a high integration via forward linkages can be usually found among resource-rich countries. Weaker backward linkages highlight a low import intensity in the export production of Egyptian firms, which is rather common in large countries with higher domestic production capacities.

¹ This note was produced by Olivia Riera from SEP/EPG and Philipp Paetzold from OCE. The analysis was supported by the [Value Chain Competitiveness Programme](#), implemented by the European Bank for Reconstruction and Development and financed by the European Union. The views expressed in this note are those of the authors only and not necessarily those of the EBRD or the EU.

² Global value chain integration is the sum of foreign value added (FVA) & domestic value added embodied in 3rd countries' exports (DVX). The residual part of exports value consists of domestic value added with no GVC linkages.

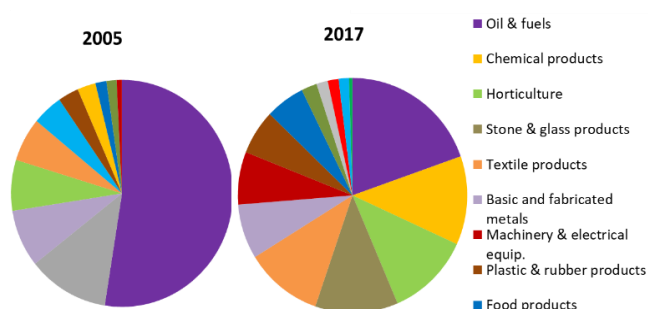
However, it is important to underline the advantage for domestic producers to have access to competitive and high quality inputs of foreign firms. Unfavourable trade regulations are often an underlying cause for a low backward integration of local firms in global value chains.

Overall, Egypt's economy relies to a small extent on exports, which only accounted for 9 per cent of GDP in 2018. Aforementioned GVC linkages made up around 4.5 per cent of GDP.

In terms of composition, the export basket has changed significantly over the last 15 years. In 2005, almost two thirds of total exports were consumer goods, exports of intermediate goods accounted for 17 per cent and raw materials for 12 per cent. Out of the US\$ 25 billion of exports volume in 2005, more than half of the value were exports of fuel, gas and oil. Not only has the export volume of goods almost doubled to US\$ 46 billion 2017, but nowadays, intermediate goods account for more than a third of the export basket, raw materials for 20 per cent of exports, while the share of consumer goods declined to 43 per cent.

A changing pattern can also be observed in the product groups between 2005 and 2017, with the export basket being significantly more diversified with chemicals, horticulture, textiles, metals and electrical machinery products gaining export shares and oil and fuels reducing export shares (Chart 2).

Chart 2: Export basket composition (as per cent of goods exports)



Sources: WITS (2018) and authors' calculations

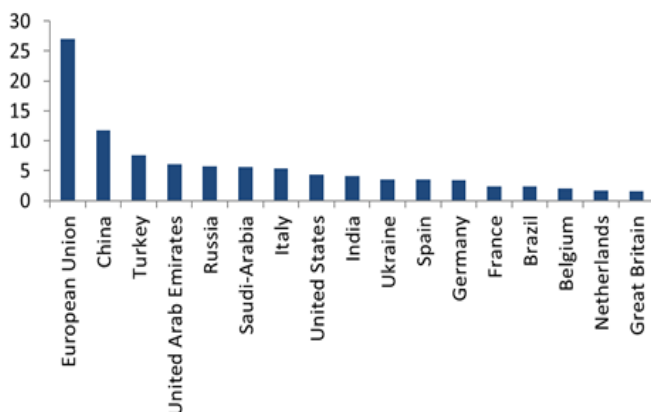
In the absence of input-output data, which is usually used to analyse global value chain linkages between countries, trade in intermediate goods acts as a proxy measure to observe Egypt's integration in global value chains. Generally, exports of industrial supply can either be used as input for final goods to be consumed in the export destination country or used as input in further production of exports (i.e. forward linkages in value chains).

Egypt's integration in global value chains has happened mainly via an increase in forward linkages. This can be observed in the stronger export growth of both intermediate goods and raw materials. Raw materials such as crude oil and gas, precious stones and metals, are among the most exported single product groups in Egypt. Industrial supply of chemical products as urea solutions and methanol, of plastics such as polypropylene, and of electrical equipment such as coaxial cables are also among the top export products of Egypt. In 2017, out of the ten most important product group exports, eight were industrial supply goods and only two consumer goods (oranges and TVs).³

Most of the trade in both intermediate and final goods has been done with the European Union, which is the major trading partner and has strong value chain linkages with Egypt. Around 27 per cent of total trade in intermediate goods (both exports and imports) was done with the EU in 2018. However, despite preferential access to the EU market via a free trade agreement, Egyptian export volumes to the EU have stagnated in the last decade, whereas trade with China, Turkey and other Arab countries in the region gained importance.

³ Based on six-digit Harmonised Classification product code level of goods exports.

**Chart 3: Trading partners in intermediate goods
(exports and imports as per cent of trade,
2018)**



Sources: WITS (2018) and authors' calculations

Trade and investment policies

Egypt is an active country in the multilateral trading system as a member of the World Trade Organisation. It has preferential market access to more than 2 billion consumers due to free trade agreements with the EU, Turkey, Mercosur, COMESA, Pan-Arab countries and soon to the entire African market with the recent ratification of the African Continental agreement.⁴

However, trade flows are hindered by severe trade regulations. Egypt has frequently made use of trade contingency measures (anti-dumping and safe guard measures). In addition, the applied Most-favoured nation tariff rate in average was higher in 2017 than in 2012 (from 16.5 to 19 per cent). The country also still raises taxes on exports on a number of products including sugar, fertilisers and marble. Furthermore, firms operating in Egypt face high non-tariff barriers in the form of import licencing and registering, import restrictions for economic,

health and religious reasons, and in form of sanitary and phytosanitary measures that are not aligned to international standards (such as the EU SPS standard).

In terms of trade and investment, Egypt relies on a complex system of designated free zones and a special economic zone to attract foreign investment and to promote exports. Free zones⁵ have the objective to benefit Egyptian firms by ensuring free flows of trade with a competitive advantage in exports and without cumbersome regulations. However, firms are only allowed to sell products on the Egyptian market after payment of custom duties, which effectively creates pure exporting firms and makes sales on the large domestic market unattractive.

The Suez Special Economic Zone has its own laws and legislation, special customs system, low taxation and relaxed labour regulations. The Suez Canal Zone⁶ is designed to attract foreign investors and firms, where 100 per cent foreign ownership and full control of exports/imports activities is granted.

The government also promotes the development of the local industry, particularly in the manufacturing sectors with the objective of exporting and integrating into global value chains through strategies and investment laws, In particular it has adopted an industry and trade development strategy (2016-2020) and implemented a new investment law in 2017 cutting red tape and offering financial incentives for investors and firms in designated economic or development zones. The newly established Suez Canal Zone plays a key role with the objective to attract foreign direct investment in targeted sectors (maritime services, pharmaceuticals, food processing, automotive, electronics, textiles, petrochemicals, ICT and renewable energy) and

⁴ The AfCFTA has been signed by 54 countries and ratified by 28 countries so far. However, the implementation has been postponed due to Covid-19.

⁵ Free zones offer firms full exemption from import tariffs, income taxes and customs duties. Firms are only subject to payments of an annual fee of the goods value entering and exiting the free zones.

⁶ In detail, a ten per cent tax rate is applied on profits and income, imports are exempted from customs duties and sales tax, a one-stop shop for investment and a dispute settlement centre are provided.

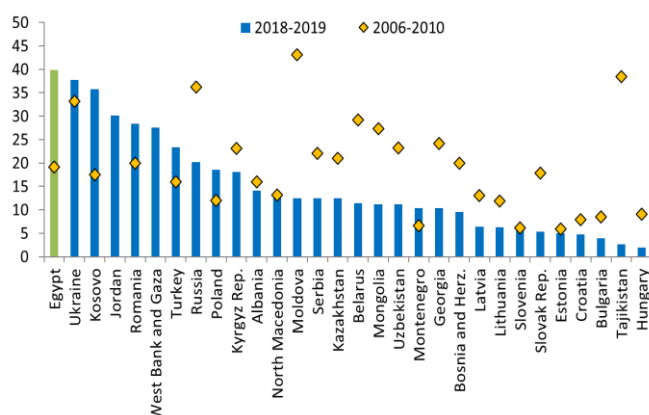
to become a major industrial and logistics hub between China, the EU and the African continent.

Obstacles and barriers

The Egyptian economy has recovered after the IMF programme approved in 2016, which supported the reduction of macroeconomic imbalances causing high inflation, unemployment and interest rates in the mid-2010s. After the adoption of a flexible exchange rate system and the currency devaluation, firms benefited from higher margins and competitiveness due to a decline in relative prices of export products, but also faced higher import costs in their production. Today, firms count on a stable macroeconomic environment, which is often a premise for GVC integration and attraction of foreign investments.

However, despite facing cheap production costs stemming from a large pool of labour, low energy costs and a good shipping infrastructure, firms suffer under a complex trade regime, high administrative barriers, scarce pool of qualified labour and a cumbersome business environment in the domestic market. Almost half of all actively trading firms perceive customs and trade regulations as major or severe obstacle for their business operations (Chart 4). Furthermore, the World Bank Doing Business ranks Egypt rather low at the category *Trading across Borders* (171 out of 190 countries). Trading firms face extremely high costs and lengthy procedures with customs and document compliances. Consequently, only ten per cent of Egyptian firms are active in both exporting and importing.

Chart 4: Firms reporting customs and trade regulations as major or severe obstacle (as per cent of total firms active in trading)



Sources: EBRD-BEEPS (2020) and authors' calculations

In order to strengthen GVC integration, firms need to have better access to foreign inputs and be able to export more efficiently. The complex different regulatory frameworks and the resulting dichotomy of economic systems split between exporting firms and firms operating in the large domestic market creates a complicated environment and results in different productivity levels among firms. This is reinforced by unfair competition, a heavy presence of state owned enterprises and a large informal sector in the economy. Furthermore, the scarcity of qualified labour due to few vocational training schools and skill mismatches, and a lack of alignment to international standards and poor quality controls reduce the opportunities for firms to enter new value chains, upgrade along existing value chains and to benefit from the vast preferential market access available to Egyptian products.

Further information is available to supplement this country factsheet:

- GVC diagnostic – The Southern and Eastern Mediterranean region
- GVC case study: Opportunities from diversification and promotion of resilience in GVCs