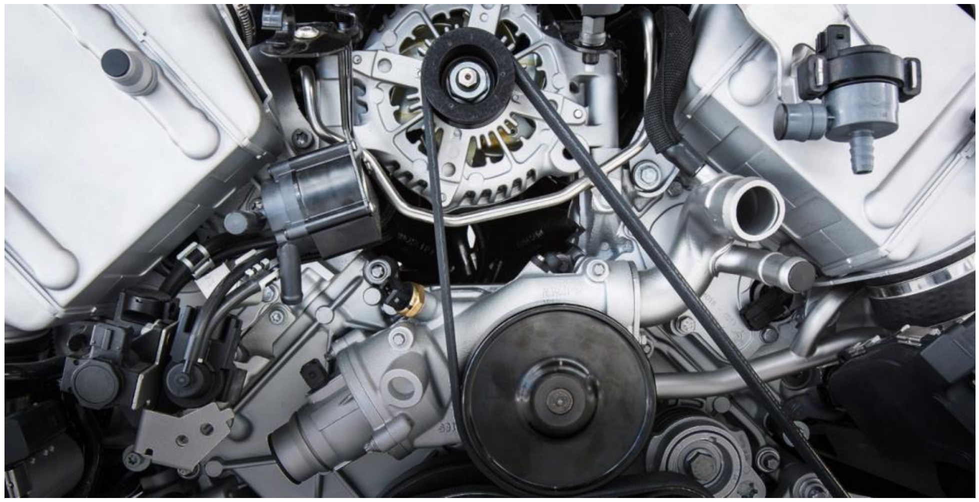
INDUSTRY NOTES

SEPTEMBER 2019



TAKING EGYPT'S AUTOMOTIVE INDUSTRY TO THE NEXT LEVEL

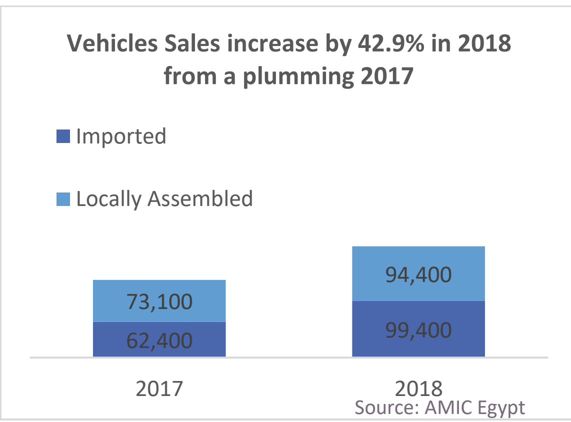
INSIDE THIS ISSUE

The return of Mercedes-Benz and other OEMs to Egypt's local assembly market has boosted confidence in the potential comeback of Egypt's automotive industry. To encourage further investments, the Government of Egypt is currently developing a package of incentives to promote the local production of vehicles and its feeding industries, thus paving the way for new OEMs and feeding companies to enhance their footprint in Egypt. Developing Egypt's R&D sector, through smart policies and regularly updated concrete incentives, should also be considered.

OVERVIEW

Egypt's automotive industry is dominated by assembly based supply chains and hundreds of automotive feeding companies. Relatively, Egypt's automotive market is currently small and has marginal tangible incentives to enable local assemblers to compete with imported vehicles. The industry has faced increasing business challenges, particularly following the events of the January 25th revolution and associated local economic hardship.

In fact, automotive sales in Egypt only began to (slightly) rebound as of January 2018 following a slump that was exacerbated by the devaluation of the Egyptian Pound in 2016. But the end of custom duties on imported European cars, as of 1/1/2019, renewed local assemblers' demands of the need to reconsider the existing unfair playing field within Egypt's automotive landscape.



The Government of Egypt (GoE) considers the development of Egypt's automotive industry a matter of high priority and is preparing to roll out a 'national program' to promote the local production of vehicles and its feeding industries. This renewed policy is intended to provide new incentives to boost domestic manufacturing and assembly, while enhancing local assemblers' ability to strengthen their market position and export their products to foreign markets. According to GoE statements, Egypt is targeting the manufacture of 500,000 cars annually by 2022, of which 100,000 will be exported.

With an improved economic standing, the GoE has signaled its interest in attracting additional Original Equipment Manufacturers (OEMs) and Tier 1 companies (companies that supply parts or systems directly to OEMs) to Egypt. But achieving this objective requires formulating a smart set of regularly updated incentives to attract such investments and thus enable Egypt to regain its standing as an automotive industry leader and compete with fierce regional players.

Looking towards the future, the GoE has also begun considering a national e-mobility strategy, including by taking initial step towards developing a regulatory and policy framework for electric vehicles in Egypt. A ministerial committee, headed by the Minister of Military Production, has been tasked with formulating a national policy with regards to the licensing, registration, importation, local assembling, manufacturing, electric charging, and other aspects of a viable electric vehicles sector in Egypt. This committee has yet to issue its recommendations.

HISTORY

The path to establishing a national automotive industry in Egypt began in 1959. Then, the GoE signed a contract with a German firm for the local manufacture of trucks and buses, which also called for the creation of a new Egyptian company in charge of assembling the vehicles in addition to manufacturing approximately half of the vehicle components. In 1961, El Nasr Automotive Manufacturing Company (NASCO) was established in Helwan, a district just south of Cairo. NASCO entered into agreements with various European companies to produce tractors (with Yugoslavia's IMR), trucks (with Germany's BLUMHARDT), and passenger cars (with Italy's FIAT).

Within ten years of its launch, NASCO claimed the production of approximately 3000 trucks and 1600 buses per year, with 70% local content. In a peak year in the 1960s the company announced its assembly of 21,000 passenger cars with 30% local content. NASCO was the first and, at that time, the only component's production company in Egypt, and the monopoly position it enjoyed enabled it to profit substantially.

Wars and economic hardships for Egypt in the 1960s and 1970s had a negative effect on NASCO's budget and expansion plans, and hampered the feeder industry's growth. Under extreme financial pressure, NASCO gave priority to the production of trucks and buses at the expense of the passenger car industry. A major downturn occurred in 1974 when the GoE adopted policies that ended the previous ban on the importation of foreign cars to Egypt. Furthermore, the GoE directed NASCO to focus its passenger car assembly operations on one model, the Fiat/Nasr 128. GoE price-fixing policies for public sector industrial products also continued despite rising costs.

In 1994, the GoE put up NASCO for sale under its famous privatization program, which in turn attracted bids from companies such as FIAT, DAEWOO, IVECO and others; all of which were considered too low.

Today, NASCO's operations are on a very limited scale, restricted to manufacturing some of the products of El Nasr Forging Company and the Eastern Company for a very small revenue. It remains a government-owned company in search of an investor to revive its years of glory. The GoE has and continues to engage a number of OEMs to upgrade the production lines of the company and resume its assembly of buses, trucks and passenger cars, in addition to vehicle components.

EGYPT'S VEHICLES MARKET TODAY

12 AUTOMOTIVE PRODUCERS WITH ASSEMBLY LINES

17 PERCENT LOCAL COMPONENTS IN THE FINAL PRODUCT

500 AUTOMOBILE FEEDING COMPANIES

3 BN USD INVESTED IN EGYPT'S AUTO FEEDING INDUSTRY/ YEAR

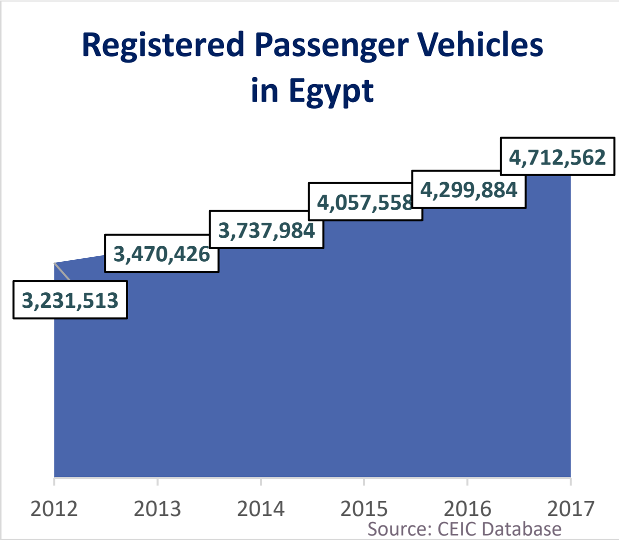
2nd BIGGEST EXPORTED ENGINEERING INDUSTRY CATEGORY IS AUTO FEEDING PRODUCTS (27%)

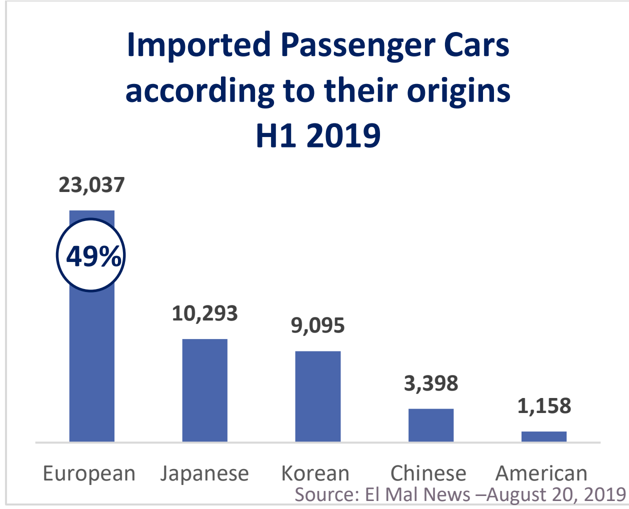
194 THOUSAND VEHICLES SOLD IN THE EGYPTIAN MARKET IN 2018

65 PERCENT OF CARS SOLD IN 2018 HAD EITHER A 1.6 LITRE ENGINE OR SMALLER

12.5 PERCENT DECLINE IN LOCALLY ASSEMBLED VEHICLES IN 2018

50 PERCENT OF PASSENGER CARS ARE 15 YEARS OR OLDER





VEHICLE SALES SUSTAIN DOWNWARD TREND DURING THE FIRST HALF OF THE YEAR

According to recently published figures from the Automotive Information Council (AMIC), total car sales in Egypt stood at 74,084 vehicles in 1H2019, down 6.8% y-o-y from 79,474 during the same period last year. Passenger car sales dropped 11% y-o-y to 51,311 units, while bus sales climbed 4% y-o-y to 7,053. The automotive industry had shown signs of recovery last year following a slump that was exacerbated by the EGP devaluation in 2016.

SIGNIFICANT RISE OF EUROPEAN PASSENGER CAR IMPORTS IN EGYPT

As the final phase of the EU-Egypt Association Agreement came into effect on January 1st, 2019, imported European passenger cars increased 37% during the first half of 2019.

Today, there are 20 European passenger car brands in Egypt. European cars attributed to 49% of the 47,026 imported cars in Egypt during the first half of 2019, with Renault standing as the highest imported passenger vehicle to Egypt. Imports of Peugeot cars have also greatly increased by 335%, in comparison with H1 2018, with the importation of 3,673 cars by H1 2019. Other imported European passenger cars to Egypt include Opel, SEAT, Mercedes, Fiat and Scoda respectively.

EGYPT'S AUTO EXPORTS INCREASE BY 45% IN 2019

According to the Central Agency for Public Mobilization and Statistics (CAPMAS), Egypt exports of locally assembled vehicles increased to USD 32.7 million during the first 5 months of 2019, compared to USD 22.5 million last year.

Congo and Rwanda were new added destinations for Egypt's auto exports markets. Currently, Egypt exports locally assembled vehicles and auto parts to 17 countries. They include the United Kingdom, which accounted for 53.4% for the vehicles after importing from Egypt 73 buses worth USD 17.3 million in 2018-2019. Additional export markets include, respectively, France (12.2% of Egypt's auto exports), Saudi Arabia (8.2%) and then the Philippines, Cameron, Ivory Senegal, Niger, Singapore, Mauritania, Hong Kong and UAE.

Most of Egypt's auto exports are in the form of buses despite the high local component requirement of 60%. One of the restrictions that is paralyzing Egypt's export capabilities lies within the exporters. Many assemblers lack the proper documentations needed – such as the VAT documents proving the local content percentage- therefore retrieve their exports incentives.

MAIN LOCAL ASSEMBLERS

GB Ghabbour Auto (GB Auto) is the largest player in the local passenger car market in terms of market share and production capacity. GB Auto's assembly operations include production of passenger cars, commercial vehicles, motorcycles and three-wheelers at plants in the Greater Cairo Area. Assembly largely refers to Completely-Knocked-Down (CKD) or Semi-Knocked-Down (SKD) vehicles imported as kits from leading international brands, including Hyundai (21% market share in 2018) and Geely (3.2% market share in 2018), that are then assembled with a legally mandated percentage of local content.

GB Auto's sales and distribution activities encompass the passenger cars line of business in Egypt, Iraq and Algeria, commercial vehicles and construction equipment in Egypt, and tires in Egypt, Iraq, Algeria, and Jordan.

GB Auto achieved EGP 25.8 billion in revenues in 2018.

Mansour Automotive is the biggest General Motor (GM) dealer in the world, selling around 100,000 vehicles a year around the world. It also owns franchises for Opel, Chevrolet (best-selling car brand in Egypt in 2018 with a 21% market share), Cadillac, Suzuki, and Isuzu. In a joint venture with GM it also manufactures cars, trucks and pickups for its various markets.

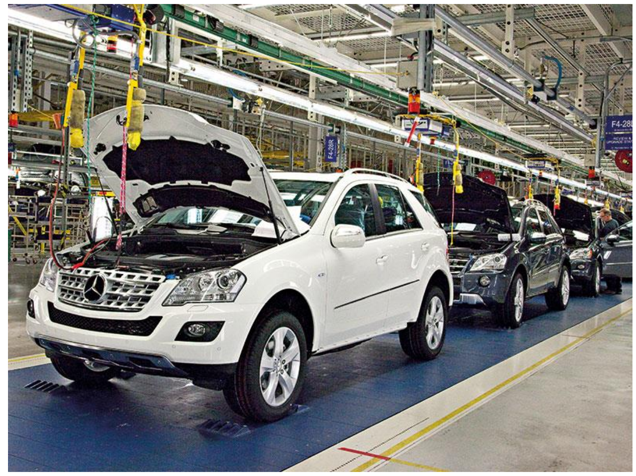
Mansour Automotive is GM's only licensed partner in Egypt, Ghana, Uganda, Iraq and Libya.

Nissan has the third largest market share in Egypt, standing at 11% in 2018. It produces an average of 22,000 units per year.

THE RETURN OF OEMS

In 2018-2019, a number of OEMs announced their intention to enhance their footprint in Egypt's auto market.

On June 24, 2019, the GoE and Mercedes-Benz signed a Memorandum of Understanding (MoU) for local assembly of Mercedes-Benz passenger cars in Egypt. This important development followed the inauguration of KIA's assembly line for its Sorento (SUV) in 6th of October city in December 2018 to produce 15,000 vehicles per year.)



The MoU describes a local Mercedes-Benz passenger car assembly and contains other potential fields of cooperation. The assembly will be set up by a local business partner (The Egyptian-German Automotive Company). At the same time, Mercedes-Benz Cars emphasized the involvement and know-how of Egyptian suppliers.

Mercedes-Benz had shut down its assembly line in mid-2015 due to foreign currency shortages and as completely built-up cars (CBUs) were made cheaper in light of falling tariffs on EU-assembled cars, which hit zero at the start of this year.

Mercedes-Benz passenger cars imports in Egypt increased by 82.4% during H1 2019. From January-June 2019, Egypt imported 2,646 Mercedes-Benz cars, versus 1,451 in H1 2018.

In its recent announcement, Mercedes-Benz stipulated that further future investments in Egypt are also conceivable, including the possible expansion of the dealer network, a logistical hub in the Suez Canal Special Economic Zone and a training center. Furthermore, the company has offered to make its specialist expertise with respect to modern mobility concepts, e-mobility and electric vehicles, as well as autonomous driving, available.

The German manufacturer is currently securing more than 1,000 direct and indirect jobs in Egypt with its own import and sales organization, a central spare parts warehouse and numerous authorized retailers and workshops in Cairo, Giza, Alexandria and Hurghada.

Mercedes-Benz Egypt S.A.E., a wholly-owned subsidiary of Daimler AG, is the exclusive sales partner of Mercedes-Benz Cars for Mercedes-Benz passenger cars and replacement parts in Egypt. The company has been in operation since 1999.

Brilliance Auto declared its intention to reassemble passenger cars in Egypt in Q1 2020, through a USD 120 million investment. Brilliance Egypt also announced plans to launch its first electric car by the end of 2019.

In March 2018, **Kia Motors** signed an agreement with Egyptian International Trading and Agencies to invest EGP 4.2 bn in a car assembly facility in Egypt over the following five years. The project, which included an investment of EGP 262 million in 2019, is expected to have a nameplate capacity of 15,000 cars per year. Kia Motors announced that this is the first auto assembly project developed by Kia in the Middle East.

FEEDING INDUSTRY

Egypt's automobile feeding industry is relatively young, started in the 1980s by General Motors Egypt. The industry thrived in 2006 and 2007 as the country's economic outlook was positive and customs and duties were high enough to entice investors to come to Egypt. This in turn encouraged OEMs, such as Jeep, BMW and Mercedes-Benz, to assemble cars in Egypt despite being required by law to secure at least 40% of parts from domestic suppliers, which did not exist. (The domestic content mandate later increased to 45%)

There are 500 automobile feeding companies in Egypt today, serving 16 assembly plants. They mainly produce exhaust components, air conditioning units, radiators, plastics for interiors, windshields, mirrors and seats, supplying international brands assembling their models locally or selling manufacturer-approved spare parts. However, the local components market is limited with only 80 auto feeders directly supplying local assembly plants.

The auto feeding industry is an important source of foreign currency for Egypt's economy. 60 auto feeders export their products to foreign markets, although 480 auto feeders are registered to do so. Auto feeders are the second biggest exporter in the engineering industries category, accounting for 27% of engineering exports in 2017. The main market for automotive feeders is Europe (80% of all Egyptian auto parts are exported). Arab countries account for 18% and the rest goes to Asia.

Total investment in automotive industry currently stands at USD 3 billion; USD 1.6 billion in the automotive industry and USD 1.4 billion in the feeding industries.

TIER 1 AUTOMOTIVE SUPPLIERS IN EGYPT

Two main tier 1 automotive suppliers are currently present in Egypt; Valeo and Brightskies Technologies.

Valeo, the French tier 1 software supplier's office in Egypt, is the Group's main software development center and the largest. Cairo-based Valeo engineers have developed various software enabling innovative technologies such as Valeo Park4U – automated parking, LED/Laser beam technologies and Stop-Start.

Brightskies Technologies provides services around high performance computing and code optimization, virtualization and cloud computing, big data, as well as embedded systems software development.

TIER 2 AND 3 AUTOMOTIVE SUPPLIERS

Tier 2 and Tier 3 components factories in Egypt manufacture a number of products including:

- Tires and inner tubes
- Glass and windshields
- Aluminum parts
- Electrical wires

- Batteries
- Leaf springs
- Oil filters
- Air filters
- Upholstery material
- Plastic parts and bumpers

Dr. Greiche Egypt is the leading glass manufacturer in the Middle East and Africa for OEMs and the replacement market. It produces complete glass sets for vehicles and provides vehicle glass replacement. Its main clients in Egypt are Ghabbour Auto, General Motors, Nissan and Toyota.

Established in 1976, **Mobica** supplies world class automotive furniture for OEMs such as BMW, Nissan, GM, Jeep, Toyota, Kia and Hyundai by utilizing advanced technologies and management systems.

Chloride Egypt is the leading manufacturer of automotive and industrial batteries with an annual production capacity of 2 million batteries. Chloride has 2 manufacturing plants in Egypt. It supplies brands such as Chevrolet, Nissan, Toyota, Suzuki, Kia and GM.

A NEW PAGE WITH OEMS?

In June 2019, two pending disputes between the GoE and major car manufacturers were resolved.

The first dispute, with Mercedes-Benz over the calculation of import duties, was resolved upon the Cabinet's dispute resolution committee ruling in favor of Mercedes-Benz in its dispute with Egypt's Customs Authority. As a result, an Egyptian importer of Mercedes-Benz vehicles won an EGP 700 million customs refund. The company was initially asked to pay an extra EGP 700 mn in a dispute over the basis of calculation for import duties. The sum was held in trust by the authority while the dispute committee took up the case.

The second resolved dispute, with **BMW**, witnessed an EGP 55 million settlement with the customs authority, ending a dispute over customs tariffs and valuations of imported cars.

However, other disputes remain unresolved. For example, **Toyota Motor Corporation (TMC)** has complained that the standard for custom duty imposed on Toyota service parts increased by approximately 3 times more than the amounts paid before September 2015, when the Minister of Finance's Decrees No. 70 dated 11/6/2015 and the Valuation Guidance No. 86 dated 22/6/2015 were issued.

TMC believes that a misunderstanding by the Egyptian Customs Authority exists regarding the method of calculating discounted prices of such services parts imported to Toyota Egypt (TE) in order to reduce import duty amount.

AUTOMOTIVE STRATEGY

The GoE considers the automotive industry an important pillar in Egypt's industrial development, but has, over the past few years, issued conflicting signals on the way forward in terms of its strategy on developing and enhancing Egypt's local production of automobiles.

In 2017, it was widely reported that the GoE was crafting an 'automotive directive' that would have provided incentives to local assemblers to move further up the value chain into manufacturing in return for a measure of protection against EU, Moroccan and Turkish imports.

In December 2018, the Minister of Trade and Industry, Amr Nassar, downplayed these reports, confirming that the GoE was working on a strategy to promote investments in the automotive sector but had no intention to announce an automotive directive. He added that the GoE would likely emulate the Moroccan and Slovakian models of concluding agreements with a number of OEMs to locally manufacture specific models in large numbers, and utilizing Egypt as an export hub for such models, in return for various tailor-made incentives that seek to enhance production and export capabilities.

Then in June 2019, the Prime Minister's office announced the GoE's plan to develop a 'national program' to promote the production of vehicles and its feeding industries in Egypt. This program is expected to provide new incentives to spur domestic manufacturing and assembly that would include notable custom discounts on automotive components. The objective is to enhance local car assemblers and manufacturers' ability to strengthen their market position and export their products to foreign markets.

In the build-up to the upcoming new policy, the Minister of Trade and Industry decided, on June 9th 2019, to cancel his predecessor's decree no. 371/2018. The repealed decree had regulated the method of determining the percentages of local component manufactured in the automotive industry and its feeding industries, stipulating that the percentage of domestic manufacturing in the automobile industry should not be less than 46% (with a 1% annual increase), and that the contribution of the assembly line in the local manufacturing rate of the car should stand at 28%.

Under the Minister of Trade and Industry's new decree, the locally manufactured components percentage is kept at 45%. The Ministry of Industry also decided to re-operationalize the decision of the Minister of Industry and Mineral Resources No. 136/1994, regarding the assessment of the contribution rate of assembly lines, as well as re-operationalize the Minister of Commerce's decision No. 907/2005.

CHALLENGES FACING LOCAL AUTOMOTIVE ASSEMBLERS

UNFAIR PLAYING FIELD

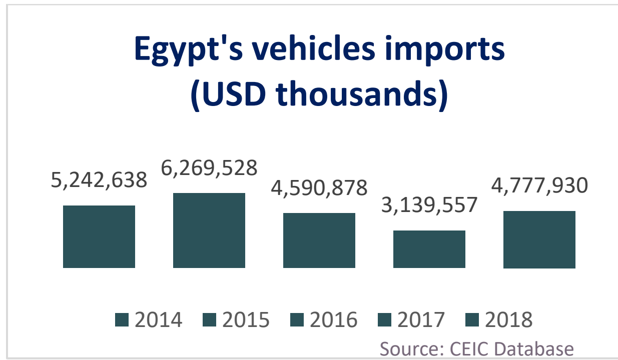
The final phase of the EU-Egypt Association Agreement (entered into force in 2004), which led to the gradual reduction of customs duties on imported European cars, was completed on January 1st, 2019, resulting in duties on imported cars from Europe falling to 0%.

Customs duties on cars with engines of 1,300 CC capacity imported from Europe were eliminated in 2016. For cars with engines of 1,600 CC and above, reductions took place annually at a rate of 4% annually until they reached 0% this year.

Imported cars are still subjected to a VAT at 14%, a 0.5% industrial and commercial profit tax, a 3% resources development fee, and a 1% additional tax. Following the tariff elimination, the market prices of cars of European origin have since gone down (ranging between 2.6% and 31.1%). Prices for non-luxury passenger vehicles from the EU dropped between EGP 20,000 and EGP 40,000. Luxury car prices by around EGP 100,000 to EGP 150,000.

As a result, local non-EU vehicles assemblers- which are subjected to various custom duties (on local components)- continue to complain of challenges faced in competing with customs-exempt European vehicles. Non-European auto parts are subjected to around 5% to 7% custom duties, 3% to 8.5% development fees.

Still, the tariff removal is unlikely to have a broader effect on market prices, as more than 65% of cars sold in Egypt have either a 1.6-litre engine or smaller.

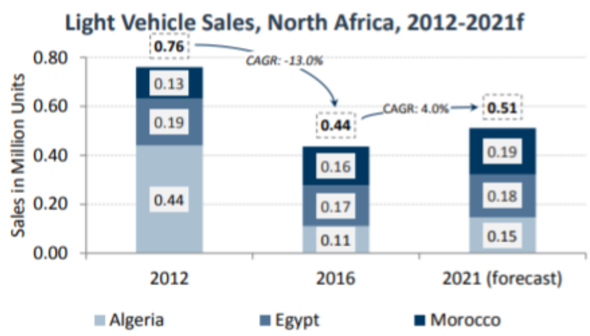


The impact of the Egypt-EU Association Agreement zero customs was notable by the end of H1 2019. Imports of passenger cars of European origin increased by 37% during the first 6 months of 2019, while American cars imports decreased by 56.2%. During the same period, Korean cars imports also decreased by 19.3% while imports of Japanese cars only increased by 15.3%. (Source: Al Mal News 20/8/2019)

Furthermore, the GoE's recent decision to float the customs exchange rate presents an additional challenge for local car assemblers and could lead to more price increases at a time when they are struggling to compete with no-customs imports.

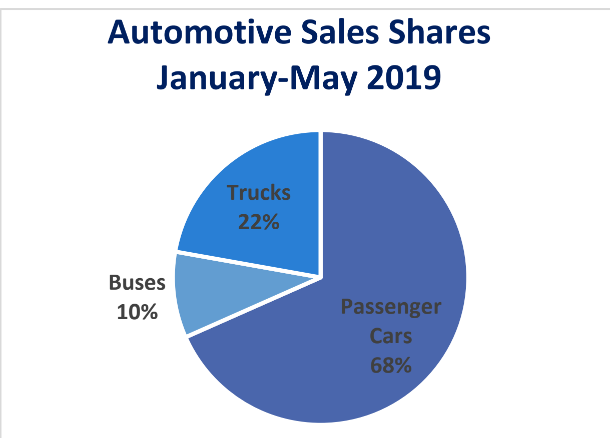
WEAK PURCHASING POWER

Car sales in Egypt were hit hard by the devaluation of the Egyptian Pound in November 2016, which slashed local incomes by 50% in some cases. Automotive sales in Egypt decreased by 40% in 2017, as consumers saw their purchasing power fall. Vehicle sales have since gradually rebounded.



Source: Frost & Sullivan 2017

According to AMIC, Egyptian passenger car sales declined by 6.7% by end of H1 2019, compared to H1 2018 (74,084 cars were sold from January to June 2019, compared to 79,474 cars in 2018). This decline has been attributed to a number of factors, including a viral social media campaign called 'Let It Rust', volatility of the car market, and the declining price of the US Dollar against the Egyptian Pound.



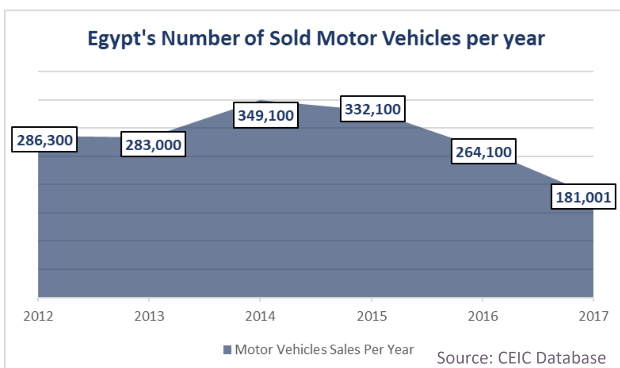
SOCIAL INFLUENCE – *LET IT RUST*

The sales decline has been somewhat attributed by some observers to the social-media campaign "Let it Rust". Let it Rust began in late 2018 and went viral in early 2019 in conjunction with the EU-zero customs mark. The social media led to boycotts by consumers in order to curb price rises. While the campaign has since garnered hundreds of thousands of supporters, measuring its precise impact on passenger cars market sales is quite difficult.

It was only months after the 'Let It Rust' campaign that the Egyptian Prime Minister, Mustafa Madbouly, issued a decision- in August 2019- to form a committee to control Egypt's passenger vehicles prices. The Committee, headed by the Chairman of the Consumer Protection Agency and includes members of the tax and customs authorities, is not mandated to impose mandatory pricing. Its mandate is to monitor the market and the random increase in prices of imported cars, including customs and other fees, with the aim of rebuilding consumer trust in automotive suppliers.

The Minister of Supply, Ali El Moselhy explained during a press conference in August 2019 that the Committee will inspect the papers and documents with dealers and importers of cars, review the intentional import invoices for the agent, and review the invoice of customs release and fees paid.

SMALL, UNDERUTILIZED MARKET



Source: CEIC Database

Egypt's small- but growing- domestic cars market, compared to other global markets, has made the country a less attractive destination for a number of major car manufacturers. This in turn has contributed to the underutilization of existing factory capacity and a very slow growth rate of research and development (R&D) investments in Egypt's automotive industry.

Egypt's small domestic market and limited R&D investments has, in some cases, contributed to the production of low tech, less expensive and lower quality automotive components by the feeding industry- rather than higher tech components such as engines and gearboxes- which has to tight revenue margins. This had restrained auto feeders' ability to expand and multiply their production due to insufficient financial resources and small market demand for such products.

FLOATING THE CUSTOMS EXCHANGE RATE

In September 2019, the GoE decided to revert back to setting the customs exchange rate on daily basis according to FX rates by the CBE, after two years of setting it monthly.

With no exemption scheme for local automotive manufacturers, experts have warned of possible implications, including the increase of prices in an already troubled auto market. Local manufacturers could be forced to increase the prices of their vehicles at a time when they are faced with fierce competition with the custom-exempted imported European cars.

REGIONAL COMPETITORS

MORROCO

- Morocco attracted renowned automotive firms, such as Renault and Peugeot, to open local plants.
- The automotive industry is Morocco's leading export sector and has made the Kingdom the leading car manufacturer in Africa, surpassing South Africa's 331,000 manufactured passenger vehicles with 345,000 passenger vehicles in 2017. Morocco is also positioning itself as a key supplier for European auto factories, taking into consideration that most manufactured vehicles in Morocco are exported.
- Recently, Morocco attracted feeding industry pioneer companies such as Nexteer, Gestamp, Ficosa and Fiat subsidiary Magneti Marelli to open plants in the Kingdom.
- Government incentives for automotive investments: 5-year corporate tax exemptions (extendable to promote export of production), VAT exemptions, modern infrastructure, skilled workforce, and free trade agreements with the US and EU.

TURKEY

- Turkey is the 15th largest automotive manufacturer in the world, the 5th largest in Europe and 2nd largest producer of commercial vehicles (CVs) in Europe.
- Turkey produces nearly 1.5 million cars annually (1.55 million in 2018). Domestic sales have exceeded 1 million cars, while annual exports reach $32 billion dollars' worth of automobiles.
- In 2018, Turkey exported 1.3 million cars, with 85% of vehicle production in Turkey being destined for foreign markets during that year.
- Turkey attracted car manufacturers such as Ford, Fiat, Honda, Hyundai, Renault and Toyota, Mercedes-Benz and M.A.N and has become a center of excellence, particularly with respect to the production of commercial vehicles.
- 1,100 auto-parts manufacturers, TIER 1 and TIER 2 supporting the production of OEMs are present in Turkey. Localization rate of OEMs varies between 50-70%.
- More than 250 global automotive feeding suppliers use Turkey as a production base; 28 of them rank among the 50 largest global suppliers.
- 175 R&D and design centers belonging to automotive manufacturers and suppliers are operational in Turkey. Proven as a production hub of excellence, the Turkish automotive industry aims to enhance its R&D, design and branding capabilities.

ALGERIA

- The Algerian Government seeks to enhance Algeria's position as a local automotive manufacturing base, with a particular focus on enhancing the local auto-feeding industry.
- Steps taken include introducing a quota system on automotive importers to "force" investments into local assembly. The government reduced car imports from 600,000 units in 2014 to 300,000 units in 2015. Vehicle imports were capped at 79,000 units for 2016, 55,000 in 2017, and at 50,000 cars in 2018.
- The Government recently announced that 40 foreign car and other vehicle manufacturers requested permits to join major car manufacturers Renault, Peugeot and Volkswagen in opening assembly plants in Algeria.
- **Government incentives**: Algeria will grant manufacturing operators exemption from VAT, customs duties and taxes on profits. It will also grant free land and ensure subsidized energy costs.
- The incentives should help Algeria reach an integration rate of 15% in the first 3 years of business activity and 40% in the 5th year to aid development and the use of locally produced components.
- Automotive policy review expected in 2019 with higher emphasis on local content and nationals' employment.

OPPORTUNITY IN EGYPT

MAJOR IMPROVEMENTS IN MACROECONOMIC INDICATORS

In 2016, the GoE began implementing a bold economic reform program to stabilize the economy and restore confidence in the face of macroeconomic imbalances and microeconomic distortions.

Program flagship reforms included:

- The liberalization of the exchange rate by eliminating currency overvaluation and foreign exchange shortages
- A fiscal consolidation program that introduced a VAT and a gradual reduction in energy subsidies and wage bill
- Major energy sector reforms by addressing the power outages and reestablishing Egypt's potential as an oil and gas producer by reducing pricing distortions and arrears

These reforms were complemented by efforts to improve the business climate and attract private investment, starting with legislative reforms and the introduction of new laws on industrial licensing, investment and bankruptcy.

Macroeconomic indicators have reacted positively to these reforms, with economic growth accelerating (5.6% GDP growth in FY 2018/2019), a parallel foreign currency exchange rate market contained, narrowed external deficits and increase in international reserves (over $44 billion).

The success of Egypt's economic reform program should have a positive impact on the local passenger vehicles market as the country's GDP growth and consumers' purchasing power gradually increase.

SIGNATORY TO PREFERENTIAL TRADE AGREEMENTS

Egypt has the potential to become a regional/global services, production and re-export hub. In addition to its central geographic location, Egypt has access to large key markets through various multilateral and bilateral trade agreements with the US, EU (zero customs on automotive imports and exports), Middle Eastern and African countries. Egypt is a signatory to the COMESA, the new Pan-African FTA, GAFTA, AGADIR. Egypt has also signed FTAs with Turkey and the Mercosur bloc.

Source: GAFI

INCENTIVES

The GoE is preparing to roll out new incentives to promote local manufacturing and assembly of vehicles and its feeding industries in Egypt. Such incentives will include notable custom discounts on automotive components, with a view to enhance local car assemblers and manufacturers' ability to strengthen their market position and export their products to foreign markets by utilizing Egypt's FTAs. TIER 1 automotive suppliers will be targeted with smart policies and competitive incentives to enhance Egypt's R&D investments.

THE SUEZ CANAL ECONOMIC ZONE

Spreading on 461 km2, the Suez Canal Economic Zone (SCZone) is a thriving free zone and trade hub along the banks of the Suez Canal. Strategically located on a major business global trade passage, the SCZone offers investors the following privileges:

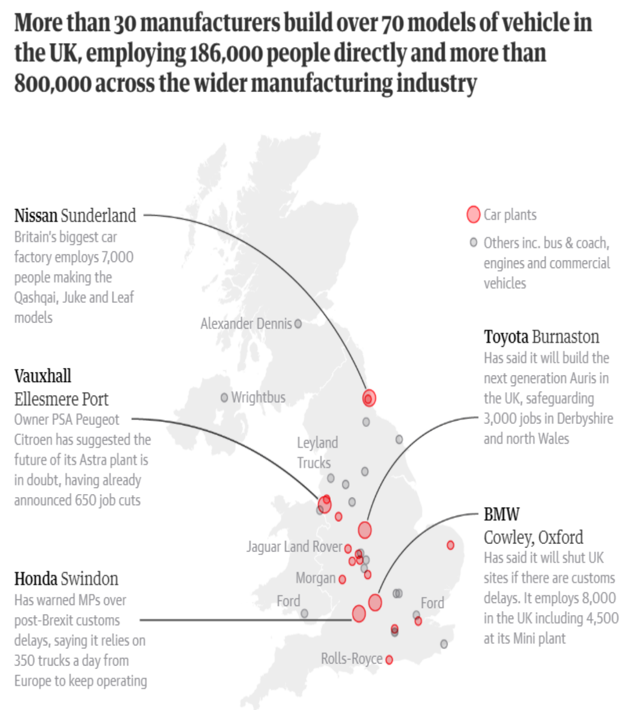
- 100% foreign ownership of companies in the zone
- 100% foreign control of import/export activities
- Imports exempt from customs duties and sales tax
- Customs duties on exports to Egypt imposed on imported components only, not the final product
- Fast-track visa services

COMPETITIVE COST

Egypt's cost is one of the most competitive in the world. The fully loaded operating cost is substantially lower than Eastern Europe and comparable to some of the lowest cost countries in the Far East

GLOBAL CHALLENGES FACING THE AUTOMOTIVE INDUSTRY

I. Brexit



Guardian graphic. Source: SMMT Motor Industry Facts 2017

Uncertainty rising in the European Union over how the United Kingdom is going to exit; elevated the risk of staying in the UK and made a lot of investors retreat their expansion plans. More than 275 companies are in the process of moving or have already moved business from Britain to other countries in Europe. The impact of a no-deal Brexit on the automobile industry would be potentially catastrophic as 8 out 10 passenger cars made in UK are exported. Jaguar Land Rover, Rolls-Royce Motor Cars, Toyota, Honda, and Nissan are among the OEMs that have voiced concerns over Brexit.

II. New emission control regulations

The EU's introduction of the worldwide harmonized light-duty test procedure for emissions controls has been considered, by many, to be a major setback to the car industry. The procedure's implementation has slowed car production.

III. Labor calls to increase wages

Labor strikes are fueling in car manufacturing plants in Eastern Europe demanding high wages. Audi (Volkswagen), Bosch, Westcast and Suzuki are some of the companies that have faced such strikes in countries such as Hungary, the Czech Republic, Poland, Slovakia, Belgium, Romania, and Serbia.

POLICY RECOMMENDATIONS

The automotive sector has become increasingly globalized as OEMs outsource a large portion of their manufacturing processes. Countries such as India, China, Thailand, Turkey, Iran, South Africa, Brazil, Poland, Romania and others have emerged as major players in the international automotive sector as cheap locations to assemble 'Completely Knocked Down' (CKD) and 'Semi-Knocked Down' (SKD) vehicle kits, and as producers of specific components and spare parts that are shipped internationally to assembly sites in other countries.

OEMs have become increasingly vertically integrated across multiple countries and continents demanding their Tier 1.

Egypt stands the chance to grow as a regional influential automotive player if it upgrades it game. There are key blocks of factors to influence future landscape of automotive in Egypt.

RECOMMENDATION # 1

Signal strong political support for local manufacturers, resume the dialogue with key industry players to develop an automotive policy that ensures a fair level playing field with custom-exempted vehicles moving forward and pave the way for additional OEMs and feeding companies to open units of their supply chain in Egypt.

This policy may include the following incentives, which should be reviewed and updated every 5 years:

CUSTOMS INCENTIVES

Introducing amendments to the Customs Act, providing customs discounts to car manufacturers in return for increasing their use of local components. Custom breaks can be split into different tiers according to the percentage of local content used in the vehicle's production.

TAX BREAKS

Providing tax exemptions or reduction for OEMs and feeding companies: VAT exemptions, income tax exemptions and/or corporate tax reduction.

For example, Moroccan incentives to OEMs have included a tax exemption in the first five years of operation, followed by an 8.75% tax for 20 years and 17.5% tax afterwards

EXPORT INCENTIVES

Providing further export-based incentives proportionate to local component input. This may include direct subsidies, direct pay backs, low-cost loans, tax exemption on profits made from exports and government financed international advertising.

INFRASTRUCTURE PREFERENTIAL PRICES

Offering competitive costs and facilitated procedures for land and infrastructure allocated for automotive factories and research and development (R&D) facilities.

EXPEDITE APPROVAL PROCESS

Reviewing- with the goal of simplifying and shortening- FDI approval procedures, on land allocation, registration and licensing, customs and taxes. Export support and subsidies are available in Egypt but further export support could be for automotive manufacturers.

RECOMMENDATION # 2

Attract automotive R&D investments. Developing an incentives program for R&D centers in Egypt, including automotive R&D, is likely to increase investments from OEMs and feeding industries. To achieve this, an incentives package, carefully crafted for the R&D industry, may include:

PATENT RELATED INCENTIVES

Providing incentives for researchers to register their patent in Egypt and/or import their patent from abroad for registration in Egypt.

FISCAL STIMULUS

Providing a tax break for companies developing technology related products and/or having R&D projects, product development, production or commercialization of technology oriented products.

A TECHNOLOGICAL FOUNDATION FUND

Creating a technological foundation fund to provide financial support to innovative projects, proposed by individual firms or groups of enterprises in the R&D sector. Selection is geared towards projects involving the development of new products, services or processes.

SCHOLARSHIPS

Supporting scholarships for researchers to work on R&D in relevant firms and thus stimulate linkages between the private sector and academia. The goal is to strengthen firm's capacity to innovate by placing R&D personnel in firms and provide professional development opportunities for scholars.

R&D EQUIPMENT IMPORTS

Providing custom duties exemption for imported equipment used in R&D related activities.

RECOMMENDATION # 3

Develop a comprehensive, well thought out e-mobility strategy, that takes into account the following:

- Egypt's market potential
- National readiness and policy framework
- A critical assessment of relevant technical aspects (proposed size, electricity requirements, costs, configuration, etc.)
- Project risks, ownership and actors involved
- Potential economic benefits (including reduced energy use and environmental benefits on air quality and emissions)
- Identifying additional investment needs and benefits (in terms of reduced energy use and reduced environmental impacts)
- Assessing the overall impact of the strategy and take up of electric vehicles on energy demand should also be carefully considered.

  The strategy should also seek to set out alternative charging infrastructure business models, based on an analysis of successful business models in other countries (such as the Netherlands and Norway)

RECOMMENDATION # 4

Consider a curb - in the new motor traffic law- on licensing passenger vehicles that are 30-years old or longer after thoroughly studying the implications of such a decision.

This decision will also have a notable environmental and health impact, taking into consideration that over 50% of passenger vehicles on Egypt's streets are more than 15-years old, which leads to higher consumption of gasoline.

RECOMMENDATION # 5

Seek to ensure market stability and growth by enhancing the predictability of policies and regulations associated with the automotive sectors and feeding industries.

ABOUT LYNX STRATEGIC BUSINESS ADVISORS

LYNX Strategic Business Advisors is an Egypt-based government relations, public policy and investment advisory consultancy firm. With a combined service of over 150 years in government and public policy, LYNX partners offer a government relations practice that combines both a strategic perspective together with a carefully planned execution in support of its clients.

LYNX leverages its principals' wealth of experience to provide high-value research-skilled government relations services combining timely, relevant and rigorous assessment, with innovative targeted solutions based on sound judgement designed to address our clients' strategic requirements. The firm's services are tailored to the client's needs and priorities but are fundamentally structured around delivering strategic insights and assessments that clients need to seize opportunities through in-depth understanding of the policies, politics and players at the heart of the relevant business opportunity or challenge.

LYNX advises clients on means of positioning their companies as a trusted partner to Egypt by supporting clients' efforts to develop constructive relationships with unrivaled access to expertise and invaluable connections with key policymakers and influencers, including government, parliament, industry associations, civil society. The firm enhances the client's ability to refine its business and political message and conveyance to suit the local culture and business objectives. It also tracks and identifies economic, policy and regulatory developments in the client's sector of interest through up to date analysis of new laws and regulations and potential issues of concern.

LYNX has published public policy notes on emerging topics as a contribution to the relevant ongoing public debates. They include two 'Industry Notes' on the opportunities and challenges pertaining to the electric vehicles sector in Egypt and Egypt's emerging status as a regional gas hub. LYNX also published a Business Bulletin on Egypt's new export rebates program. The three documents can be found on LYNX's website.

LYNX is a partner firm to Thebes Consultancy, an Egyptian Limited Liability Company established in 2012 and exclusively specialized in the provision of legal information, regulatory updates, legal compliance, training and regulatory advice in the area of commercial, financial and business law in Egypt and the Arab World.

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