Comparison of foreign direct investment in Turkey and Egypt: motivations and obstacles

dumludag, devrim

Marmara University, FEAS, Department of Economics

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A Comparison of Foreign Direct Investment in Turkey and Egypt: Motivations and Obstacles

Devrim Dumludağ[1]

Abstract

This paper compares the political economy of foreign direct investment (FDI) in relation to economic development strategies and legal framework for foreign firms in Egypt and Turkey. The paper briefly examines the FDI performances of these countries starting from the end of the nineteenth century to the first decades of the twenty first century. In addition, in this paper, the legal framework for FDI is analyzed. Finally the paper put emphasis on the similarities between the FDI performances and the obstacles that foreign investors face in these countries.

Keywords: *Egypt, Turkey, Economic Conditions, Foreign Direct Investment, Legal Framework*

1. Introduction

Since 1980, with the liberalization of developing economies, the volume of FDI has grown significantly. With the increasing globalization, changes in government policies in trade and investment environment facilitate FDI into developing countries. Turkey and Egypt are not exceptions. These countries have made considerable progress over the past decade in liberalizing their business environment and encouraging foreign direct investment. They have involved simplified procedures, enhanced incentives, reduced taxes and greater openness to foreign investors.

However, neither Turkey nor Egypt succeeded at attracting FDI as they expected. Some could expect that due to their growth performances and market sizes, these economies should become attractive for many MNCs. However, in these countries FDI inflow had been below the expected level until the first decade of 21st century. Amount of FDI inflow had been roughly similar annually in two countries. The difference is Turkey started to encourage FDI inflow (1950) before the Egyptian efforts of 1974. Plus, Turkish encouragement Law of FDI No. 6224 was very liberal from the 1954. However, in Egypt, in this sense, a liberal law was enacted in 1998 after many encouragement laws were enacted.

Table1. Country rankings by Inward FDI performance Index and Inward FDI Potential Index, 2007–2009

	Inward FDI Performance	Inward FDI Potential Index

[1] Marmara University, Department of Economics, dumludag@marmara.edu.tr

Economy	2007	2008	2009	2007	2008	2009
Turkey	91	95	109	73	76	-
Egypt	34	51	52	85	93	

Source: UNCTAD, Handbook of Statistics, UNCTAD: Geneva, 2010

There are several ways to view Egypt and Turkey's relative FDI performance as host countries. There are two indices developed by UNCTAD: The FDI Performance Index and The FDI Potential Index.

The Inward FDI Performance Index ranks countries by the FDI they receive relative to their economic size. It is the ratio of a country's share in global FDI inflows to its share in global GDP.[2]

The Performance Index is shown for three-year periods to offset annual fluctuations in the data. The indices cover 141 economies for as much of the period as the data permit.

According to the inward performance index, Turkey ranks at 95 with a score of 0.917 in 2008 and 109 in 2009. This low score indicates that Turkey receives less FDI than its relative economic size. The position of Egypt is much better in comparison to Turkey with a rank of 52 in 2009.

The Inward Performance Index, alone, does not give sufficient information about the performance of a country because it assumes non-market related other factors such as the business climate, economic and political stability, the presence of natural resources, infrastructure, skills and technologies, to opportunities for participating in privatization or the effectiveness of FDI promotion as equal.

A more complex index, the Inward FDI Potential Index, captures several factors (apart from market size) expected to affect an economy's attractiveness to foreign investors. It is an average of the values of 12 variables.[3] Here, Turkey has a better position than Inward FDI performance index, however, with Egypt still standing behind other emerging markets.

[2] The index captures the influence on FDI of factors other than market size, assuming that, other things being equal, size is the "base line" for attracting investment. These other factors can be diverse, ranging from the business climate, economic and political stability, the presence of natural resources, infrastructure, skills and technologies, to opportunities for participating in privatization or the effectiveness of FDI promotion. A value greater than one indicates that the country receives more FDI than its relative economic size, a value below one that it receives less (a negative value means that foreign investors disinvest in that period).

[3] GDP per capita, GDP growth, share of exports in GDP, average number of telephone lines per 1,000 inhabitants and mobile telephones per 1,000 inhabitants, Commercial energy use per capita, share of R&D spending in GDP, and country risk

The figures of UNCTAD above reveal that Turkey and Egypt receive low level of FDI inflows in regard to their market potential. Hence, in this paper I investigate whether the reasons for unexpected level of FDI inflows, economic policies and strategies for FDI in these countries are similar or not?

2. Egypt and Turkey – Comparison for FDI inflows

Egypt and Turkey are secular, “modern”, Islamic countries. Egypt and Turkey are countries of approximately equal population size at the lower, middle level of income and development. They share a common historical background. They were both part of the Ottoman Empire. Around World War One they had similar levels of population and income. After independence, both followed an Etatist development strategy (relying on import substitution industrialization, expanding public sectors). The two countries both adopted inward oriented economic policies between 1920 and 1980.[4]

In Both countries efforts of secularization and modernization were parallel. In the Ottoman Empire these efforts started in the first half of the 19th century. In Egypt these attempts took place in the second half of the 19th century. Ownership rights to land were also introduced in the 19th century in both countries. Infrastructures were built up, cities Europeanized, and trade developed, largely financed by foreign capital. Apart from some processing of agricultural products, industrialization was almost absent. Central government played an important role in the modernization process in both countries.

In the nineteenth century, with the arrangements signed between the Ottoman Empire and several European countries, there was a climate encouraging the operations of foreign companies. These companies established enterprises in various sectors such as service (banking, finance), transportation (railways), and energy (electricity). Especially foreign companies built up monopolies dominating the basic services.

Before 1914, most of the FDI was placed in infrastructure such as railroads and ports rather than in production activities such as agriculture or industry. More than 80 joint stock companies were controlled by foreign capital, operating in the Ottoman Empire in 1910.[5] It is interesting that the number of firms containing foreign capital only reached this number in the 1960s.

Between 1888 and 1914 the rate of growth of FDI was higher than the rate of growth of foreign lending to the Ottoman government. FDI in the Ottoman Empire was concentrated two sub-periods; between 1888 and 1896 FDI exceeded 30 million pounds. Most of this capital inflow was directed towards railroad construction. FDI remained limited before 1875, particularly during 1876 and 1887. Between 1905 and 1913 more than 17 million pounds of FDI

[4] Although Etatism was abandoned in Turkey in 1980, it continued in Egypt with a growing bureaucracy blocking reform.

[5] Şevket Pamuk, **The Ottoman Empire and European Capitalism. 1820-1913: Trade, Investment and Production** (Cambridge: New York: Cambridge University Press, 1987), p.63.

was invested and again the largest share of these funds went to railroad construction.[6]

The distribution of foreign capital stock according to country of origin in the Ottoman Empire at the end of 1913 demonstrates the French domination with 50.4 percent, followed by Germany with 27.5 percent, and Britain with 15.3 percent.

As it was in Ottoman Empire, Foreign investment in Egypt dated from the nineteenth century. Relatively large amounts were invested in the 1890s, with investment peaking in 1907. Between 1903 and 1907, for example, the cumulative private direct investment may have amounted to £E8.6 million. At the turn of 20th century Egypt was a totally open economy. Trade, finance and industry were overwhelmingly concentrated in foreign hands, with more than 90 per cent of the paid-up capital of joint stock companies in Egypt in 1914 held by French, British and Belgian interests.[7]

However, the two world wars and the depression interrupted the process. During the 1930s, new FDI flows into Turkey decreased to very low levels and some foreign firms stopped production.[8] FDI flows also stagnated throughout the world during the depression years. As it was in Turkey, during the two world wars and the depression FDI flows stagnated and little foreign direct investment occurred during the nationalist economic phase under Nasser.[9]

3. Post-war period

After the Second World War, in Egypt, private sector activity has dominated investment and growth, and except for the brief socialist spell of the 1960s, foreign capital has been welcome in almost all sectors.[10]

The situation was somewhat similar in Turkey. After the end of the Second World War, major political and economic changes took place between in Turkey. Turkish governments, due to both international conjuncture and

[6] Profit transfers arising from FDI only exceed 1896 new capital inflows. Especially operations railroads were profitable plus, the timing of this major wave can be explained to some extent by international forces and reducing the cost of transportation.

[7] UNCTAD **Investment Policy Review, Egypt**. Geneva, 1999, p.1.

[8] A. Gündüz. Ökçün **1920-1930 yılları arasında kurulan Türk Anonim Şirketlerinde Yabancı Sermaye** (Ankara : Sermaye Piyasası Kurulu , 1997).

[9] For detailed study on political economy of foreign direct investment see D. Dumludag

An Analysis of the Determinants of Foreign Direct Investment in Turkey: The Role of the Institutional Context, **Journal of Business Economics and Management**, 1/2009. , for detailed study on economic conditions and economic development strategies in Egypt see: Bent Hansen **The Political Economy of Poverty, Equity, and Growth Egypt and Turkey**. World Bank:1991.

[10] Ashok Kapoor **Foreign Investments and the New Middle East A Survey of Prospects, Problems and Planning Strategies**, New Jersey: Princeton Press, 1975, p.25.

domestic pressure, turned towards an open economic model.[11] The new economic policies gave signals for encouraging FDI flows by changing or improving the laws.[12]

In Egypt, the wave of nationalization of the sixties did not touch private ownership in agriculture, distribution, real estate and housing, as well as small scale manufacturing, construction and service activities. Foreign investors were also successfully attracted in the socialist era to promote the tourism, pharmaceuticals and petroleum industries. Starting with Law 65 of 1971, foreign capital was invited to establish operations in Egypt's industrial free zones, and Arab capital was attracted to undertake inland projects.[13]

President Sadat officially inaugurated Egypt's Open Door policy (Infitah) in 1973, shifting back the country's orientation to a market economy. The domestic private sector was restored, and Law 43 of 1974 was specifically designed to attract Arab and foreign capital and technology and to promote exports.[14] Liberalization measures covered the investment, trade and exchange rate regimes, and the government monopoly of finance and foreign trade was abolished. Both Arab governments and private investors responded quickly. They initiated separate joint venture projects with Egypt, both in the military and civilian, especially banking, sectors. Arab and other foreign business concerns were located in the free zones near Alexandria, Cairo, Port Said, and Suez.

The Investment Law made no discrimination between the nationality of investors and both private and public capital, were encouraged to enter into joint ventures with transnational companies. The law gave priority to projects that promised to generate foreign exchange and had advanced technology components. A special body, the General Authority for Investment and Free Zones, was founded to supervise foreign investment.

The cumulative number of projects approved had by 1978 reached 591 (83 percent of which partly foreign owned). Investments in the petroleum sector also started in the mid 1970s - under a separate law - and gathered momentum to reach a cumulative figure of about $6 billion over the 1975 to 1985 decade. The

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[11] For the development policies about the period see İ. Tekeli and S. İlkin, **Savaş Sonrası Ortamında 1947 Türkiye İktisadi Kalkınma Planı** (Ankara : Orta Doğu Teknik Üniversitesi, 1974) pp.6-10.

[12] For instance, in by-law No.13, arranged in 1947, a new regulation was made for the "protection of the Value of Turkish Currency" which brought encouragement of foreign investment by mentioning FDI could operate and invest in the specific sectors which were important for the economic development of the country. Plus, foreigners that invest in these specific sectors gained the advantage to transfer profit and capital without having to apply for permission from the Ministry of Finance.

[13] Nemat Shafik "Private Investment and Public Policy: The Egyptian Case" in **Reviving Private Investment in Developing Countries Empirical Studies and Policy Lessons** ed. by A Chibber, M. Dailami and N. Shafik, Elsevier Science & Technology Books, 1992, p.69.

[14] Robert Springborg "Egypt" in **Economic and Political Liberalization in the Middle East** ed. by Tim Niblock and Emma Murphy London: I B Tauris & Co Ltd,1993, p.148.

bulk of tourism investment was also undertaken under special legislation -Law 1 of 1973.[15]

In this period, in Turkey the amount of realized FDI did not exceed $15 million annually. In spite of the subsequently enacted FDI laws, the inflow of FDI was below $5 million annually in the 1950s. The obvious increase in FDI inflows took place in the 1960s, yet again; the realized investment was below $15 annually. In the 1960s both authorized and realized foreign investments continued to be statistically insignificant, in spite of significant growth of domestic market.[16] In this period, called the golden age of Import Substitution Industrialization Strategy (ISI), the economic growth rate was seven percent and the manufacturing sector's growth rate was between 11 and 12 percent.[17]

In the 1960s, in both countries import substitution was chosen. However, in the mid 1970s there were some efforts to open economy in Egypt. With adopting the "open door" policy in Egypt in 1974 government aim was to reduce state control over the economy that was largely dominated by the public sector. In this period 8.5 percent growth rate was realized and the economy was boosted by sizeable amounts of foreign assistance, worker's remittances, and foreign direct investment. However, the rapid growth era ended in 1986 given that the economy was still inward looking.[18]

In the 1970s Turkey actually lacked the political and economic stability to provide an attractive investment environment for investors. In the 1960s and 1970s, several coalition governments and two military coups showed Turkey to be politically unstable in its second experiment with democracy. The period 1974-1979 also witnessed rising political instability and widespread violence between political factions and ideologies, which drastically worsened the environment for FDI.

4. Post-1980 Period

The contribution of foreign direct investment (FDI) in the process of capital accumulation in Egypt had been impressive since the first decade of the Open Door policy. Over the 1975 to 1985 decade, Egypt's aggregate imports of capital goods amounted to $25.4 billion, and the distribution of the total reflects the importance of investment activity undertaken by various players in the economy. While 46 percent, of total imports of capital goods, is accounted for by

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[15] Nemat Shafik "Private Investment……" p.70.

[16] This fact can be strengthened by reference to the proposed first five-year development plan about foreign direct investment. The five-year development plan forecasted the need of $50 million annually FDI inflow since the beginning of the plan in 1963. However, not only realized investment but also authorized investment had not reached the $50 million level since 1951. See Devlet Planlama Teşkilatı, **First Five-Year Development Plan, 1963-1967 (Ankara: Turkish Republic Prime Ministry, 1963)** pp.237-239.

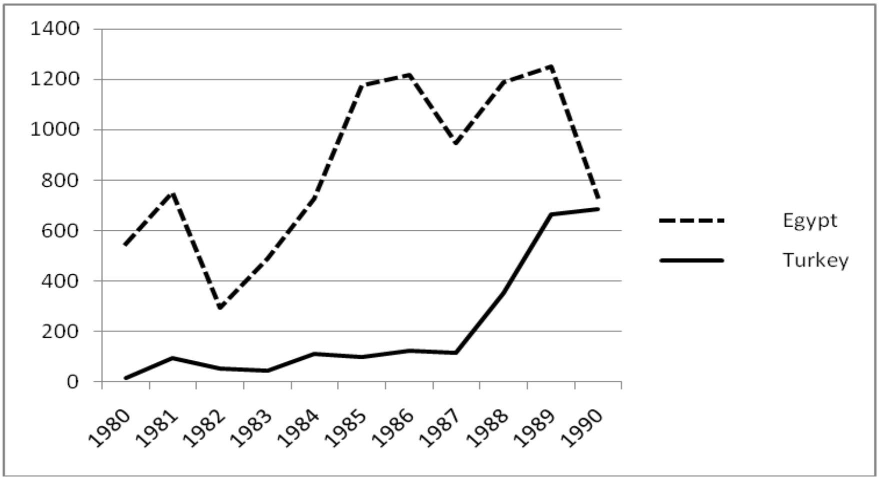
[17] Z.Y. Herschlag, **Turkey the Challenge of Growth** (Leiden: E. J. Brill, 1968).

[18] H. Handoussa, and M. Louis "Brownfield Investment in Emerging Markets The Case of Egypt" in *DRC* **Working Papers Foreign Direct Investment in Emerging Markets** London: London Business School, 2003, p.4.

the public sector, mostly spent on rehabilitating the infrastructure, 22 percent was spent by foreign petroleum companies, 19 percent by private domestic enterprise and 13 percent by Law 43 (now Law 230) projects.[19]

Turkey, under pressure from international organizations oriented toward private enterprise, free trade, and market forces, shifted in 1980 to a strategy of export led growth with structural reforms. On the other hand the Etatist ideology which influenced by List's infant industry philosophy under the label of Arab socialism and with extensive nationalizations and confiscations were imposed on Egypt by Nasser and continued, with modifications, under Sadat and Mubarak.

Figure1. Foreign Direct Investment Inflows (million dollars - current)



Source: UNCTAD, Handbook of Statistics, 2010

In Turkey, although significant measures were taken in order to attract FDI inflows in the 1980s, the amount of FDI increased annually but not as expected. The graph in figure 1 demonstrates FDI inflows in Turkey, which after a period of stagnation began to increase considerably after 1987. The average of FDI inflows was $170 million during the 1980s. On the other hand, in this period levels of FDI inflows to Egypt had been much higher than Turkey until the end of 1980s.

In this period, oil and banking absorbed the bulk of investments in Egypt. In the late 1980s, however, tourism attracted a number of foreign investment groups, and in 1989 a few major joint venture projects were under way with foreign firms, including a digital telephone exchange plant with Siemens, West Germany, a tire factory with Pirelli, Italy, and a baby-food processing plant with Nestle, Switzerland. According to some estimates, the average annual foreign direct investment amounted to about US$255 million between 1981 and 1988; according to others, it was considerably higher. The difference in estimates resulted from frequent lack of distinction in Egyptian official statistics between Egyptian and Arab investment.[20]

[19] Robert Springborg "Egypt…….", p.156.
[20] UNCTAD. **Report by the Secretariet of the UNCTAD**. Geneva: UNCTAD, 2002.

Actually Egypt turned to open economy in 1991 under the supervision of IMF and World Bank. After 1990 governments in Egypt, as in the Turkish case in the 1980s, opened Egypt economy and liberalized the financial system. The Government of Egypt recognized the importance of private investment for economic growth and endeavored to orient economic policies towards an open free market and these efforts were remarkable in the 1990s. Due to the rapidly increasing macro-instability of the economy, the government launched a comprehensive economic reform and structural adjustment program (ERSAP) under the support of the IMF and the World Bank in 1991. The main objectives of the program were to generate a higher and more sustainable growth rate and reduce unemployment and inflation. Egypt was placed on the map of emerging markets and on the IFC list of successful stock markets. As part of the reform the government started to privatize 314 public sector enterprises worth 4 billion and FDI reached 2.9 billion in 1999.[21]

Figure 2. FDI Inflows to Egypt and Turkey (million dollars - current)

Source: UNCTAD, Handbook of Statistics, 2010.

However, the policy implications did not bring a success to the FDI performance of Egypt in the 1990s.

As it can be seen from the figure 2, in the 1990s FDI inflow was fluctuated. In order to make a periodization for FDI in Egypt case; it can be argued that from 1975 to 1990 FDI inflow significantly increased, however, 1990s were the hard years for Egypt regarding FDI. The effect of the Asian and Latin American financial crises 1997 and 1998 was reflected on the economy by end of 1998.

As it was in Turkey the central bank was keeping a fixed exchange rate against the dollar by putting pressures on the international reserves. Foreign investors were discouraged by the instability of the exchange rate, the trade deficit and the overall decreasing macroeconomic performance. The privatization

[21] H. Handoussa, and M. Louis "Brownfield…..", p.4

process slowed and growth rate decreased from 6 % to 3.2 % (but it did not become negative as it did in Turkey).[22] In this case, Egypt is close to Turkish case.

On the other hand, Turkey's FDI performance in this period also failed. In the 1990s inflow of FDI was insignificant due to severe economic crises and inconsistent macroeconomic policies. This can be explained by several economic and non-economic factors: The 1990s called the lost decade in Turkey due to severe, subsequent economic crises. The political and economic instability obstructed higher amounts of inflow of FDI. While in the 1970s executives of foreign firms typically complained about the negative attitude of governments, in the 1990s they mostly complained about the macroeconomic and political instability.[23] In this period, Turkey had 9 coalition governments in 10 years. By this way there was no chance for government's ability to carry out its declared programs, and its ability to stay in office.

Economic growth was increasingly infrequent, with sharp rises and falls, including a financial crisis in 1994, followed by a severe recession. Inflation accelerated and exceeded 100 percent in 1994. [24]

The level of FDI inflows with current prices as US dollars, continued to remain low in the 1990s. In the 1990s average annual FDI inflow of $770 million fluctuated between $680 and $980 million. In the 1990s the inflow of FDI to Turkey reached 1 billion annually. However, when we compare Turkey with other developing countries such as Brazil and Mexico we see that Turkey was not successful at attracting FDI in relative terms. For instance, Brazil attracted two times greater FDI than Turkey in 1990; in 2000, the ratio reached 1:40. The ratio between Mexico and Turkey was 1:1.5 in 1990; however, the ratio reached 1:15 to the disadvantage of Turkey.

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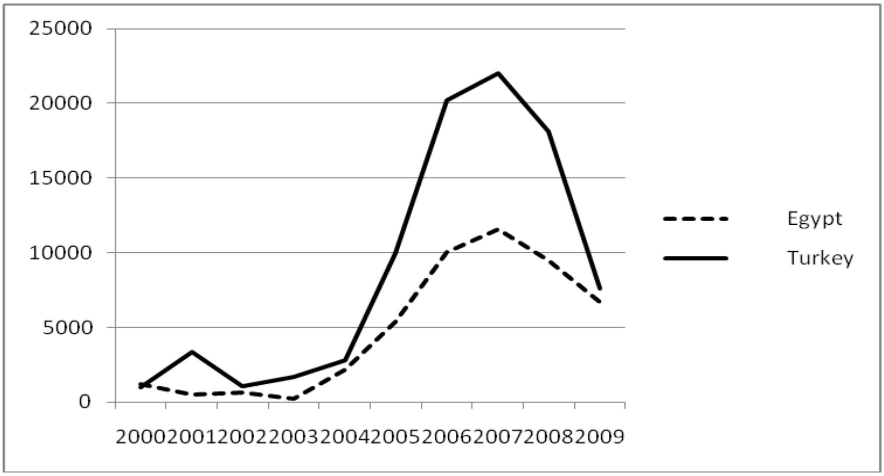
[22] Maryse Louis, and Alia El Mahdy, H. Handoussa "Foreign Direct Investment in Egypt" in **Investment Strategies in Emerging Markets**, London:2003, p.54.

[23] D. Erden, **A Survey of Foreign Direct Investment Firms in Turkey** (İstanbul:Boğaziçi Üniversity, 1996).

[24] On the other hand, inflation may not be a serious problem in some cases. For instance, Brazil, Mexico and Argentina attracted significant FDI inflows although high inflation took place in these countries in the 1980s.

Figure 3. FDI Inflows to Egypt and Turkey (million dollars - current)



Source: UNCTAD, Handbook of Statistics, 2010.

In Egypt, inflow of FDI decreased sharply in 2000 and stagnated until 2003. This was because of foreign investors' expectations about an economic crisis to happen increased. Egypt adopted a tight budget policy. The government's attempts to limit the rate of Egypt Pounds depreciation by selling US dollars made the economy fall into a liquidity crises and high interest rates. By 2001 there was a series of devaluations of the pound. By the end of 2002 the devaluation reached 35.3% of the fixed exchange rates of 1998/99. Despite these measures the economy was falling into recession as growth rate decreased to 2.5% inflation stated to rise.[25] In the end foreign investors were suspicious about macro economic stability and preferred not to invest under uncertainty.

According to available data on cross-border M&As and greenfield FDI projects, most West Asian FDI in Africa is concentrated in North Africa, with Egypt as the main destination (tables 15 and 16). About 40 per cent of total FDI in Egypt is estimated to have come from Gulf investors in 2006–2007. The latter have used the Egyptian Government's privatization scheme to move into the financial sector, and have also been encouraged by the simplification of property registration procedures to increase their activity in the construction and real estate market. In addition, Gulf investors in Egypt have been active in tourism, energy, insurance, manufacturing, fertilizers and telecommunications.

[25] H. Handoussa, and M. Louis "Brownfield…..", p.24

Table 2. Foreign Direct Investment (FDI) selected years (millions of dollars)

FDI inflows	1995-2005 (Annual Average)	2006	2007	2008	2009
Turkey	2,184	20,223	22,023	18,148	7,611
Egypt	1,311	10,043	11,578	9,495	6,712
FDI Stocks					
Turkey	14,933		153,124	70,118	77,729
Egypt	14,690		50,503	59,988	66,790

Source: UNCTAD, Handbook of Statistics, Geneva, 2010.

In Turkish case, the situation was similar at the beginning of the first decade of the 21st century. At the end of 1999, Turkey adopted a three-year economic stabilization and structural reform program with the support of the International Monetary Fund (IMF). However, after the subsequent crises of November 2000 and February 2001, the program collapsed. The support of the IMF and the World Bank continued and structural reform and economic stabilization programs continued. Turkish governments decisively adopted administrative reforms and the Turkish Parliament approved a sweeping revision of the country's codes to bring them closer to European Union norms.

Significant reforms were approved especially in the financial sector. In order to strengthen the quality of economic institutions, new measures were adopted. At the end of the period the rate of inflation decreased to fewer than 10 percent. The economy experienced high growth rates while there was no progress in diminishing the unemployment level.

The coalition government and succeeding AKP government paid special attention to inward FDI and approved legislative revisions concerning FDI. A new FDI encouragement law was enacted in 2003, the complicated entrance procedures were simplified, and for the first time, the state accepted to work in accordance with non-governmental organizations and the private sector in order to improve the investment environment for foreign investor.

Plus, in support of these efforts, Foreign Investment Advisory Service of the World Bank has been asked to analyze the business climate in Turkey and prepare this report which indicates the government willingness to attract more FDI inflows to Turkey. For this purpose Foreign Investment Advisory Service (FIAS) prepared a report, based on extensive field work consisting of surveys and interviews that declared that administrative barriers hinder more FDI flows into Turkey.

The FDI inflow was $982 million in 2000; it reached $3.2 billion in 2001. However, the increase of FDI inflow did not continue, rather, it fluctuated. The inflow was $1 billion in 2002, $575 million in 2003 and $2.7 billion in 2004.[26] Finally the expected levels were achieved in 2006 with $20,223 million, $22,023 and $18,148 for 2007 and 2008 respectively.

4. Position and Contribution of FDI

In Egypt as in Turkey, foreign firms concentrated especially in manufacturing and service sectors. Firms' main investment motive is market potential in both countries. Sectors like chemicals, building materials, engineering, food, metals and textiles benefited the most from the FDI inflows. The service sector also benefited, especially tourism. In addition, tThe privatization program in Egypt unlike Turkey was considered one of the most successful in the world, and, privatization process increased the level of inflow of FDI to Egypt.[27]

As in Turkey, European firms dominate overall foreign direct investment companies. European firms are mainly concentrated in producing intermediate products; infrastructure and construction; trade and tourism; and pharmaceuticals. This concentration, especially in the case of the first, second and last sectors are consistent with their fields of specialization whereas the investment in tourist companies is more related to the competitive advantage of Egypt. Arab FDI has an important share and is more evenly distributed among economic activities, minor concentration in the financial sector, machinery and equipment and infrastructure and construction. Asian investments are concentrated in the machinery sector, and North American companies are concentrated in the financial sector. More than one third of all American investments go to this sector, though it only represents one sixth of total FDI to Egypt. A possible explanation is that the banking, insurance and financial investment have become a thriving and growing field in Egypt since the early 1990s.[28]

The majority of entrants are small, though a few large firms have come into basic manufacturing and tourism. The dominant entry modes are Greenfield and joint ventures, with acquisitions being rather rare and unknown - in infrastructure, IT and pharmaceuticals. Within Egypt, as well as in Turkey, FDI flows are small in magnitude relative to domestic economic aggregates. They amount to only 2 per cent of gross domestic product, and about 10 per cent of gross domestic investment which was 1 percent in the 1990s.[29]

A feature of FDI in Egypt is the effort to diversify the geographical concentration of industry in Cairo. This effort includes the establishment of industrial zones, new industrial cities, free trade zones and technology parks. They are administered by different entities and offer different incentives to

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[26] UNCTAD, **Handbook of Statistics**, 2006.

[27] H. Handoussa, and M. Louis "Brownfield…..", p.8

[28] UNCTAD "Investment….", p.6

[29] Robert Springborg "Egypt…….", p.152.

potential investors. The first and second generation of eight new industrial cities established in the desert (Tenth Ramadan, Sixth October, Borg Al Arab, Sadat City, Amerya, Salheya, Badr and Obour) have been successful in attracting investment. New communities have also been launched in the Southern Valley. Industrial zones, which are located adjacent to existing urban areas, have also attracted a large number of investment projects. Recent investment projects are located in Upper Egypt, adjacent to the existing cities of Assiut, Minia and Sohag. Thus, small- and medium-sized enterprises appear to be responding to the provision of supervised land and related tax incentives in the less developed governorates of Upper Egypt.[30]

In Turkey as it is in Egypt case the majority of entrants are small firms. In 2000 the number of firms containing foreign capital was 5328. In 2003 the number of firms was 6511. During the 18 month period between the enactment of Law 4875 in June 2003 and the end of 2004, 2,461 new FDI firms came into existence and 634 national firms became FDI firms, with total FDI inflow of $3.8 billion, 80 percent of which originated from the EU.[31]

FDI concentrated in major industrialized and urbanized cities. Plus, seashore of the country attracted FDI because of the role of tourism. Since the new FDI law, 6,000 new FDI firms were established in Turkey. Between 1954 and 1999, the cumulative of foreign firms was 4,192. However, most of the newly established firms are small and medium scale and most of them are far away to be called as MNCs.

By 2005, most of the foreign firms concentrated in major cities; Istanbul, Ankara, İzmir, Antalya, Bursa and industry centers Kocaeli, Tekirdağ and Bursa. According to the ISO (Istanbul Chamber of Industry), in 2004, among the largest 1,000 industrial firms, there were 223 FDI firms, which accounted for 40 percent of the total sales, 49 percent of the total value-added, 44 percent of the total profits, 44 percent of the total exports, and 27 percent of the total employment.[32]

According to the sectoral distribution of MNCs operating in Turkey; 40 percent of the MNCs in Turkey operate in the financial intermediation sector. The transport, storage and communications sector has a share of 38 percent, very close to financial intermediation. Third largest sector MNCs belong to is manufacturing with a share of eleven percent. The wholesale and retail trade sector has a share of five percent.

5. Laws regarding FDI

The Egyptian Investment Code (Investment Law No. 230/1989) does not provide an explicit definition of foreign direct investment (FDI). The code, however, defines foreign capital as the invested funds owned by a natural person

[30] H. Handoussa, and M. Louis "Brownfield….."

[31] Republic of Turkey Prime Ministry Undersecretariat of Treasury, Statistics, 2007.

[32] İstanbul Chamber of Industry Report, Istanbul: ISO Yayınları 2005.

enjoying the nationality of a foreign country other than the Arab countries, or by a juridical person of which the majority of the capital is owned by persons enjoying the nationality of a foreign country. The Central Bank of Egypt provides data on FDI in the country. The International Monetary Fund also provides FDI data in its balance-of-payment statistics.

Although privatization and liberalization that picked up in the 1990s has prompted FDI in a range of industries, in particular cement, telecommunications and tourism. By 2002 the Government Egypt completed the sale of the majority of the public enterprises slated for privatization, garnering a large amount of revenues. However, the privatization programme is still on-going and some sales took place in 2005. The Government plans to accelerate the programme in the "strategic" areas, including telecommunications and other utilities (e.g. the Egyptian Electricity Authority).

In Turkey many foreign encouragement laws of FDI were enacted from 1947 to 1954. Since 1954 Law No. 6224, a very liberal encouragement Law of FDI, remained without any changes until 2003. However, in Egypt many laws regarding FDI were enacted until 1997. In contrast to Turkey, in Egypt, laws of FDI (that enacted in the early periods) were not liberal as Law No.6224. The comparison of encouragement of foreign direct investment laws of two countries will be revealed.

In Egypt, during Intifah, Law No. 43 was enacted in 1974. In 1981 The Companies Law No.159 was introduced governing the establishment and operation of companies in Egypt. Law 230 was enacted in 1989; and the new Investment Law 8 in 1997 introduced more incentives to private and foreign investment in Egypt and is considered an improvement to the regulatory framework. Among its most essential provisions is the grant of national treatment to foreign investments. Other provisions of the Law 8 regard guarantees for repatriation of profits and guarantees against expropriation. In this regard, the World Economic Forum “Global Competitiveness Report” (1997) ranked Egypt 28th out of 53 countries, and highlighted both positive and negative features of business climate in Egypt.[33]

However, official approval remains required for all foreign direct investment firms. In Turkey this application was abolished in July 2003. From that time FDI firms when entering Turkey do not take permission, just inform the bureaucracy for their operations. In Egypt further legislative reforms are planned, including a unified company law institutionalizing equal treatment for companies regardless of their country of domestic or ownership status. Reforms are also planned to reduce procedures, define minority shareholder rights, and improve rules for mergers and to amend corporate taxes.

The basic law governing the establishment and operation of companies in Egypt is the Companies Law No. 159 of 1981. It sets out the rules and procedures for incorporation in Egypt and regulates taxes, fees and employment rules. Foreign companies may incorporate under the Companies Law, but there are some articles that limit foreign ownership.

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[33] H. Handoussa, and M. Louis “Brownfield…..”, p.5

Thus, the majority of foreign companies as mentioned above choose to register under Investment Law No. 8, under the administrative authority of the General Authority for Investment and the free zones (GAFI). The law allows 100 per cent foreign ownership and permits foreign investment in 16 distinct fields, some of which were previously restricted, including industry and mining, tourism and oil production and related services. The Executive Decree of August 1997 added petroleum refining and cinema production. Other fields still require prior approval from interested ministries before an investor can approach GAFI (for example, all military products and related industries; tobacco and tobacco products).[34]

The Investment Code amended in 1995 has eliminated pre-incorporation approval and replaced it with a notification requirement for investment, facilitating investment to targeted economic sectors and promoting decentralization of industry from the crowded geographical areas. The law allows full foreign ownership and guarantees the right to remit income earned in Egypt and to repatriate capital.

The Egyptian legal system provides protection for real and personal property, but laws on real estate ownership are complex and titles to real property may be difficult to establish and trace.

Companies and projects are protected against nationalization or confiscation by article 9 of the Egyptian Constitution and article 9 of the Investment Law No.8. Foreign investors also now have the right to remit profits and to repatriate invested capital. Transfers are made in freely convertible currency and the market exchange rate. Companies under Law 159 however are subject to some restrictions in terms of the amount of capital transferred.

6. Difficulties Faced by Foreign Firms

A number of studies give idea about the difficulties that foreign investors faced in Turkey. Especially between 1954 and 1980 many foreign firms complained about administrative problems. After 1980 governments tried to improve the legislation process, however, these efforts did not end the complaints of foreign firms.

In Egypt too, foreign investors identified various obstacles (similar with Turkish case) to business establishment and operation. According to various surveys done in Egypt, for the majority of factors a mean score of three or more was recorded, and this indicates that there is room for improving the business climate, especially for establishment and operations, so that they can compete with other developing countries.

When entrepreneurs draw up a business plan and try to get under way, the first hurdles they face are the procedures required to incorporate and register the new firm before they can legally operate. World Bank Analysis shows that burdensome entry regulations do not increase the quality of products, make work safer or reduce pollution. Instead, they constrain private investment; push more people into the informal economy; increase consumer prices and fuel corruption.

[34] UNCTAD “Investment…….”, p.8.

Table.3 Doing Business 2010 Rankings

Doing Business 2010	Egypt	Turkey
Ease of Doing Business	106	73
Starting a Business	24	56
Dealing with Construction Permits	156	133
Employing Workers	120	145
Registering Property	87	36
Getting Credit	71	71
Protecting Investors	73	57
Paying Taxes	140	75
Trading Across Borders	29	67
Enforcing Contracts	148	27
Closing a Business	132	121

The World Bank, World Business Environment Survey, Washington: WB, 2010

The commercial legal system in Egypt is often accused of being slow and expensive. Corruption in the legal system in terms of irregular payments to judges, experts and personnel is not very common (the WEF report ranked Egypt 30th out of 59 in terms of corruption in the legal system). The clearance rate9 was reported in the mid-1990s to be 36 per cent (as opposed to 80 or 100 per cent in most developed countries), and the average time period to resolve a case is 6 years. This poor performance is probably due to the limited number of judges and their low remuneration.[35]

As it on the agenda in Turkish case, good governance and transparent and efficient institutions are seen crucial factors promoting and encouraging investment in Egypt. Lack of institutional reforms in Egypt slows down the inflow of FDI. One important reason why Egypt has been slow to achieve its economic objectives is due to the cumbersome and ineffective character of the structural and institutional systems.[36]

Most surveys have suggested that the ineffectiveness of the taxation system and petty corruption (as in the Turkish case) have increased business costs. Distorted competition taxes tend to be very high and the incentives given tend to offset each other and so have little incremental effect. Also, cumbersome procedures of the tax administration and the time consuming processes add a significant element of uncertainty to private investment in Egypt. Tax evasion is still considered a problem that reflects corruption. Bureaucracy has also been identified as a key constraint by business in Egypt (as it is in the Turkish case), hindering investment and especially FDI. Starting a new business in Egypt can

[35] Maryse Louis, and Alia El Mahdy, H. Handoussa “Foreign………”, p.55.
[36] H. Handoussa and N. El-Mikawy “ Institutional Reform and Economic Development in Egypt.” **Economic Research Forum**, Egypt, 2001.

be extremely difficult when faced with bureaucratic procedures, licenses and paper work.

Egypt still has a large inefficient and underpaid civil service with weak professional incentives and performance, and which is resistant to reform. Interviews with businessmen in Egypt suggest that substantial reforms to government administration are difficult given the immense political power of this sector.[37]

The legislative system in Egypt contains a number of weaknesses: The absence of a unified policy framework for the reforms; the vague and arbitrary nature of laws, often referring to other laws or parts of laws annulling or amending them; (similar with the problems about vagueness of Law No. 6224 in Turkey) The unconstitutionality of many laws; The frequent amendment of laws brings into question their credibility.

The persistence of a poorly performing institutional framework is perceived as the main bloc that has undermined the process of reforms and limited the flow of foreign investment into the economy. The legacy of public sector domination and of centralization continues to impact negatively on the functioning of the markets.

In sum problems of foreign investors operating in Egypt are very similar with the problems of their associates in Turkey. Complaints of foreign investors can be summarized as:

• Political instability

• Business licenses are not easy to obtain

• The legal framework has also been criticized for its slowness in resolving business disputes and commercial matters such as unpaid checks…etc;

• Rules and regulations are unstable and hard to predict;

• The role of central government in facilitating establishment procedures, determining economic policies that influence business operations and decisions such as the exchange rate policies, import and export regulations, transfer of profits, etc;

• The role of the local governments, especially in granting approvals, business licenses and real estate titles.

• Tax regime.

Conclusions

In both countries FDI inflow had been below the expected level for a long period of time. Amount of FDI inflow is roughly similar annually in two countries.

Although Egypt has not attracted the necessary levels of FDI to support export growth that the Government hoped for to achieve the more ambitious

[37] Robert Springborg "Egypt…….", p.160.

economic growth objectives, Egypt has made considerable progress over the past twelve years in liberalizing its business environment and encouraging foreign direct investment.

However, my study revealed that the changes suggest that much more remains to be done, especially with respect to governance, transparency of institutions and efficiency of government. Even so, Egypt has managed to attract growing sums from foreign investors during the 1990s, branching out from a largely Arab base to attract significant investment from North America and Europe.

In this sense Egypt shows common characteristics with Turkey. In both countries FDI firms complain about red tape, transparency of institutions and instable macroeconomic conditions. Managers of foreign affiliates assessed the Egyptian business environment relatively positively, though improvements during the 1990s were at best only moderate. Neither labor nor infrastructure is viewed as a major problem for foreign investors, though the influence of the government, the bureaucracy and the frequent and unpredictable state intervention was seen as a persistent problem.

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