Stepping up structural reforms to improve Egypt’s business climate

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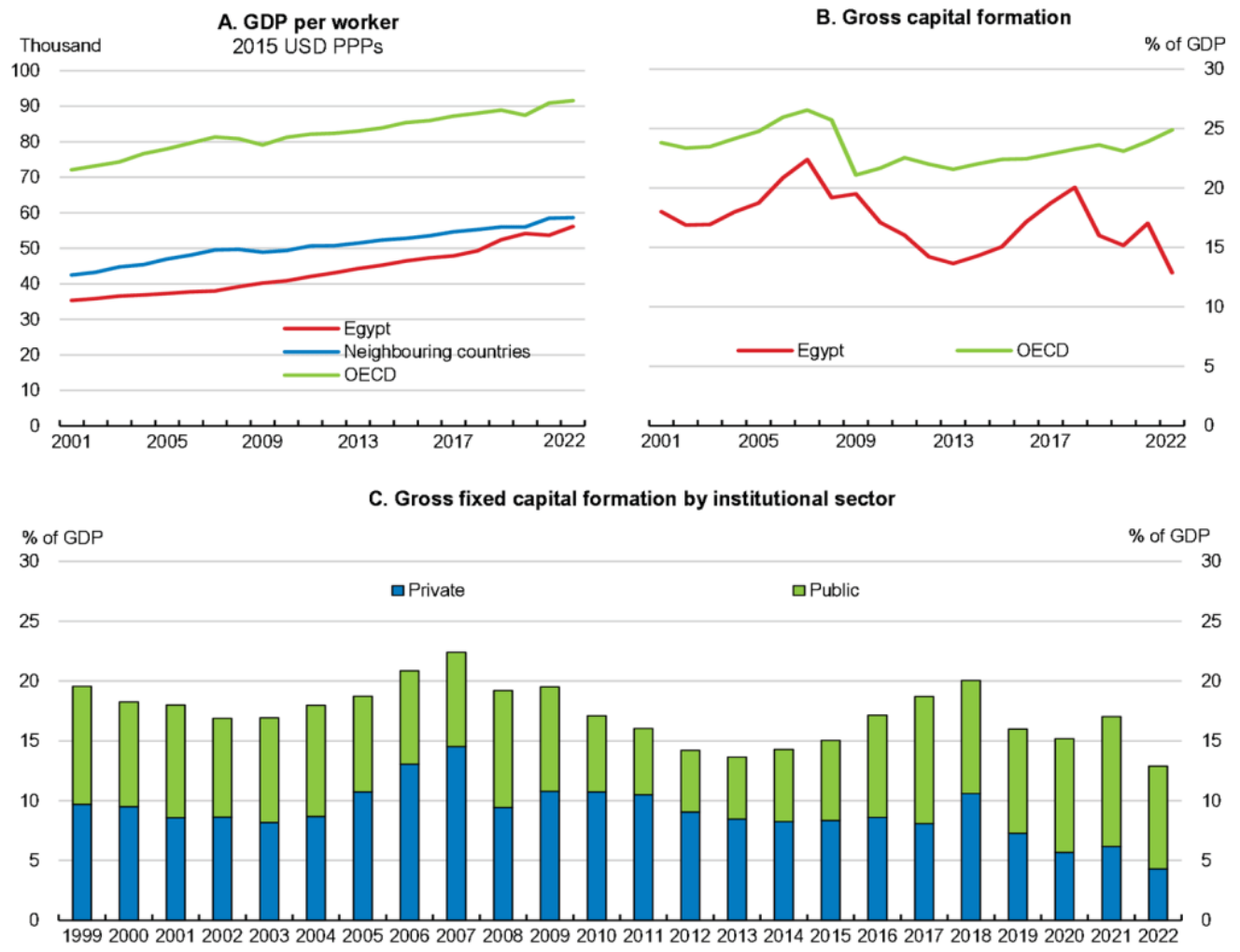
Egypt’s challenging business climate is holding back productivity and therefore also living standards. Labour productivity is still far below the OECD average (Figure 1), with low overall investment and a declining share of private investment in the total. Low investment in innovation, and research and development (R&D) also contributes to low productivity growth, as Egypt spends less than 1% of GDP on R&D. Market mechanisms, such as business entry and exit, and growth of the most efficient firms, appear to be weaker than in many similar emerging markets. Underlying these facts are deep-seated structural causes that impede market competition, investment and efficient resource allocation. These barriers stifle the country’s potential for long-term sustainable growth and restrict the development of a robust private sector. To ensure sustainable economic growth, as set out in Egypt’s National Structural Reform Programme, thorough policy reforms are required that can boost market competition. Regulatory and trade barriers, as well as a dominant state presence need to be addressed to revive private sector activity.

Figure 1: Low output per worker is related to low investment



Note: Data for Egypt in all three panels refer to fiscal years (from July of indicated year to June of the following year). Neighbouring countries refer to Algeria, Israel, Jordan, Lebanon, Morocco, Tunisia and Türkiye.
Source: IMF, World Economic Outlook database – October 2023; OECD, National Accounts database; Ministry of Planning and Economic Development; and OECD calculation.

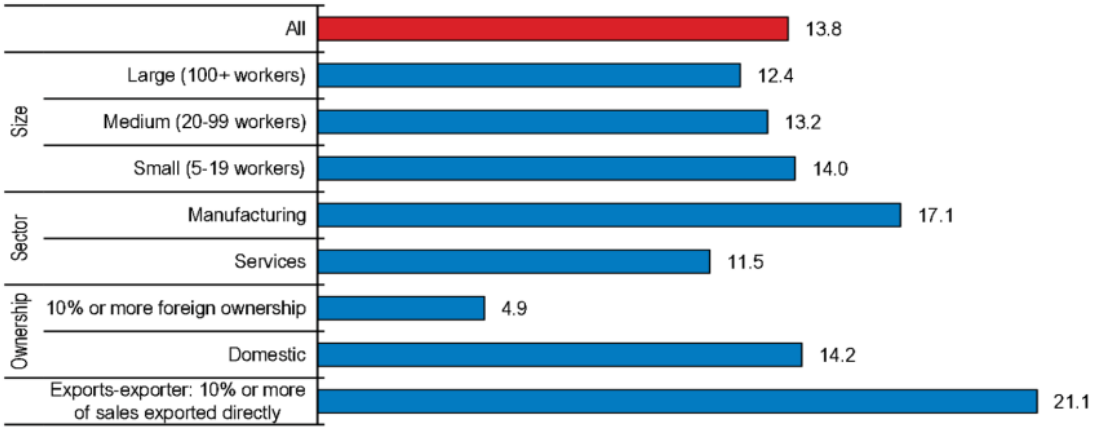
Removing regulatory barriers to enhance market entry and expansion

A central and long-standing challenge is the heavy regulatory burden that acts as a barrier to market entry and expansion, while also promoting informality. Complex and lengthy processes for obtaining business licenses and permits during the post-establishment phase constrain both domestic

businesses and exporters (Figure 2). Despite recent reforms, the administrative load remains heavy, stifling Egypt's business dynamism compared to regional and global averages, with comparatively low entry and exit rates. Moreover, overall regulatory quality remains low, reflecting lengthy and opaque decision-making processes and implementation.

Figure 2: Business licensing is a constraint on domestic businesses and exporters

Percentage of firms in Egypt identifying business licensing and permits as a major constraint, 2020



Note: Share of respondent firms out of 3075 firms surveyed.
Source: World Bank, Enterprise Surveys.

To support a more dynamic private business sector, Egypt needs to streamline its business registration and licensing processes. Licensing requirements can be replaced by online registration in most cases, while a more efficient on-line application system would speed up processes. A new online platform for business registration was opened up in 2023, but difficulties remain with local permits. Simplifying procedures and reducing bureaucratic hurdles can encourage new business formation and attract more investment. Additionally, improving the transparency of administrative procedures would also reduce opportunities for corruption, which is a crucial step towards creating a fair and competitive market landscape.

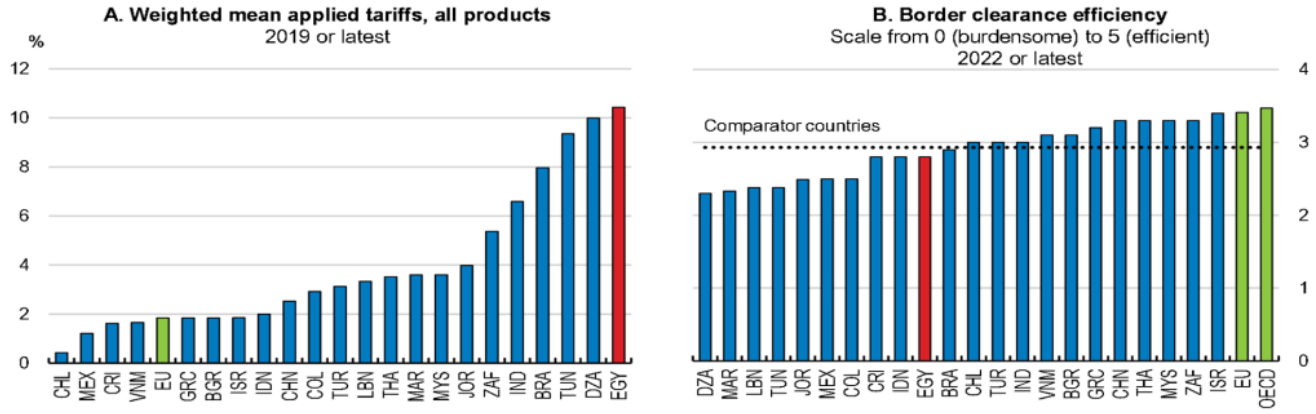
Strengthening competitive pressures through trade and

investment

High tariff and non-tariff barriers to trade mean that the Egyptian market remains relatively insulated from global competition. Such trade restrictions limit the country's integration into global value chains and reduce the spillover benefits of foreign technology and know-how, which are essential for boosting productivity.

Liberalising trade policies and reducing tariffs can enhance Egypt's competitiveness on the global stage. The creation of the National Single Window (*Nafeza*) to support external trade, should help speed up customs procedures. Border clearance has improved but remains comparatively slow (Figure 3). To support faster import release, the authorities are working on a new risk management system, which should speed up processes by reducing the number of inspections to those selected by the risk matrix. However, Egypt should also simplify its tariff regime, as tariffs remain high and unwieldy, with particularly high tariffs for agricultural products, and for products that compete with Egyptian manufactured goods (with tariff rates of 40-60%), in a system with 7 850 tariff lines. Foreign traders whose products already meet domestic standards should not have to preregister their products, and import licences could be replaced by a simple registration with the customs authorities, as is the case in Europe. A more open and predictable trade regime would benefit domestic businesses and investors, as well as supporting more inward foreign investment. This in turn would facilitate the transfer of technology and expertise, thus foster productivity growth.

Figure 3: High import tariffs and slow border clearance are hampering trade



Note: In Panel A, data for the countries presented refer to 2019 except for Thailand (2015), Tunisia (2016), Israel (2017), Mexico (2018), Jordan and Malaysia (2020). Weighted mean applied tariff is the average of effectively applied rates weighted by the product import shares corresponding to each partner country. When the effectively applied rate is unavailable, the most favoured nation rate is used instead.
Source: World Bank, World Development Indicators; World Economic Forum (2019), Global Competitiveness Index 4.0.

Reducing the state's footprint in the economy

State-owned enterprises (SOEs) play a significant role in Egypt's economy, to the detriment of competitive market conditions by crowding out private sector activity. The government's recent steps to level the playing field, though commendable, need to be more comprehensive and sustained. Over-reliance on SOEs in various sectors, such as utilities and transport, but also in manufacturing, prevents private enterprises from competing on an equal footing. Privatisation and divestment of SOEs should be pursued more aggressively to reduce the state's dominance in the market. This move will not only improve efficiency but also stimulate private investment. The OECD's guidelines on privatisation could serve as a valuable framework for Egypt in this regard.

Further actions to support private businesses: Access to finance and digital diffusion

Access to finance remains a significant hurdle for many businesses in Egypt. Banks overwhelmingly prefer to lend to the government, leaving private enterprises, especially small and medium-sized enterprises (SMEs), with limited financing options which hampers business expansion and innovation. Enhancing financial inclusion by opening up the banking sector to competition, notably by FinTechs with Open Banking regulation, can mitigate this issue. Policies aimed at improving the creditworthiness of SMEs and developing a robust microfinance sector will also support private sector growth. Improving digital financial services could play a critical role in this transformation.

Digital inclusion is key to boost productivity and competitiveness. However, Egypt lags behind in terms of digital infrastructure, and adoption by SMEs. The legal framework for digital business models needs significant improvement to allow for dematerialised businesses to expand. Investing in digital infrastructure and fostering a regulatory environment that supports digital innovation are therefore crucial steps to create a more vibrant business sector and help enhance overall economic efficiency.

References:

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