Africa Confidential Vol 56 No 11, 29 May 2015: EGYPT www.africa-confidential.com/article-preview/id/11109/Crashing_car_barriers

EGYPT

Crashing car barriers

A new free trade regime threatens car-makers. Some are trying to keep global competition at bay

This month, Mercedes-Benz became the first of several major motor-manufacturers which are expected to halt assembly work in Egypt. Under the country's trade treaty with the European Union, duties on imported, fully-assembled vehicles are being progressively phased out by the end of the decade. That makes local assembly uneconomic. A large share of such factories belongs to politically-influential owners, such as the Ghabbour and Masreya families, who are looking at other ways of staying in business, say sources in Cairo. The families, which also control automotive retail markets, are intent on using their influence to protect their positions.

Last December, Egypt notified the World Trade Organisation that it had initiated a 'safeguard investigation', under which imports of products can be temporarily halted if they are believed to be potentially or actually causing serious injury. It stopped what it said were unsafe vehicle batteries coming in. This measure is one of the only ways that imports can be halted under WTO rules. The next day, the head of the Trade and Industry Ministry's Anti-dumping Department, **Ibrahim el Segeiny**, announced that battery manufacturer Chloride Egypt had complained about a sudden surge in imports, saying it decried this rise as a threat to the industry. 'Dumping' or the sudden import of a massive quantity of one product at extremely low prices, is not allowed under WTO rules.

Auto industry specialists believe both these complaints have no substance and are in reality efforts to stop imports that local products cannot compete with on price. So long as local industry was protected by tariffs, such measures were not necessary. Observers are now waiting to see whether local manufacturers can depend on the regime's support in using these methods to preserve their profitability.

A sign that the feeder industries to the assembly plants, such as battery-makers, can't weather the storm of international competition was evident in the absence of any auto projects at Egypt's much-vaunted investment summit in Sharm el Sheikh in March. Without tariffs to protect them, these industries may go to the wall. Mercedes said its parent company, Daimler, sold its minority stake in the Egyptian **German** Automotive Company, previously a joint-venture between local business people and Daimler, to National Automotive Co. (Natco), the 'strategic partner in Egypt of the production and distribution network of Mercedes-Benz passenger cars'. EGA is now turning to assembling cars and producing components for other companies. It says it will continue to supply Daimler, albeit minimally, by producing and exporting brake discs for it and Mercedes says it will maintain its after-sales services in Egypt.

Local assembly in the region is not

dead, however, as Mercedes has said it plans to relocate its assembly plants to **Algeria**, where local assembly remains viable because of the comparative privileges and facilities offered to the auto industry. This month, Algeria adopted new regulations on the import and sale of motor vehicles, which effectively restrict foreign vehicle imports and provide an incentive to maintaining dealers' distribution networks. In other words, Algeria now offers similar protection to what Egypt used to. Egypt's Bavarian Auto Group, the agent for BMW, said in a statement that rumours that BMW would follow Mercedes in ending local assembly were false. BMW already has products that are wholly imported from abroad, giving it a competitive advantage in order to defer a possible decision to leave.

Egypt's new treaty obligations with the EU under the Euro-Mediterranean Agreement also pose a threat to stakeholders associated with 'grey market' or unofficial imports. While Cairo imposed high tariffs and duties, some businesses got around them by importing finished vehicles to Gulf countries, where tariffs and duties are lower than Egypt's, and then re-exporting them to Egypt, ducking the tariffs and selling them for less than locally-assembled vehicles. The Greater Arab Free Trade Area was founded in 1998, grouping 17 Arab countries (including Egypt, **Libya**, **Morocco**, **Sudan** and **Tunisia** in Africa). That enabled Egyptian firms to exploit the tariff differential between Egypt and the Gulf countries. **Raouf Ghabbour**, the Chief Executive Officer of Ghabbour Auto, Egypt's sole distributor of the East Asian companies Hyundai, Mazda and Geely, has called for lower tariffs on car imports from Asia and the **USA**.

UNVIABLE

Even **Karim Ghabbour**, President of the local Mercedes vehicle assembler, Manufacturing Commercial Vehicles Co. (MCV), has publicly acknowledged that the sector is currently 'economically unviable'. He has hinted at developing non-trade barriers. He said that to attract foreign investors to manufacture in Egypt and export, factory production would need to be at least 200,000-300,000 cars per year, while the current output of local factories ranges between 10,000 and 30,000.

Ghabbour's company was established in 1994 to represent Mercedes in the commercial vehicle sector after Daimler purchased two factories from the Ghabbour Auto Group. MCV was part of a 2010 US Foreign Corrupt Practices Act case over a joint-venture with Arab American Vehicles (AAV), a subsidiary of the Arab Organisation for Industrialisation, which is affiliated to the Egyptian military. According to the US Department of Justice, Daimler made improper payments to help secure contracts with government customers for the purchase of Daimler vehicles. After the overthrow of President **Mohamed Hosni Mubarak** in 2011, promises were made but never fulfilled that the names of officials allegedly bribed in the case would be published.

Karim's statements appear to signal a drastic change in the Ghabbour family's tune. This January, Ghabbour Auto announced it would be investing US$1.5 billion in two new factories, signalling confidence in the sector but providing few details of this proposed expansion. This followed the Stock Exchange's suspension of trading in Ghabbour Auto's shares until it provided more information to the market about its planned rights issue, which it said it expected would boost the company's capital by $134 million. Questions have been raised over whether this was effectively a ploy by a cash-strapped company to have shareholders pump new cash – even devalued Egyptian pounds – into it. The whole sector has been badly hit by a recent cap on dollar deposits imposed by the Central Bank of Egypt that heavily restricted the sector's access to imports.

Egypt's ailing auto sector has at times been so short of credit it has had to operate on a cash-only basis. In mid-2013, when Egypt's credit rating declined, MCV lost its letters of credit guarantees for advance car purchases with its facility in Germany, which covered half of the cars it imported, one former MCV employee told *Africa Confidential*. One respected industry insider told us he saw no realistic prospect of the sector surviving 2020, which is when Egypt is obliged to phase out customs and tariffs to zero. ●