

CASE: HISTORY OF INTERNATIONAL INVESTMENT
IN THE EGYPTIAN TEXTILE INDUSTRY

1. Current Operation of DIB-EGYPT LLC

Before explaining our experience in Egypt, I want to briefly introduce the current operation of DIB-Egypt LLC.

DIB-Egypt LLC has been established in 1997 with 100% Korean investment. This is the 7th operation year from start of business.

With our own additional investment to renovate the facilities, DIB-Egypt is currently producing 4,800 tons of quality cotton yarns per year, using 100% Egyptian cotton, long staple and extra long staple fibers. We have 600 local workers working on 24 hours a day and 350 days per year.

Considering rather small domestic market in Egypt, we have intensively developed overseas export market, and now 100% products are being exported to foreign countries, mainly Europe, and partially to Asian market. Currently, DIB-Egypt's yearly export to Europe accounts for about 15% of the total Egyptian cotton yarn export to Europe.

Our total cumulative export volume since business start till end of last year reached about US\$ 80 million, and by end of this year US\$ 100 million is forecasted.

And, now, our long-term investment plan is to become a leading textile company in Egypt, and to make further investment for business expansion. This is, of course, subject to our full convince of investment circumstances like stable cotton supply matter and further subject to successful negotiation with the local government.

2. Background of Investment in Egypt

In order to understand why we made decision to select Egypt as our overseas investment location, we need to consider the situation at that time.

Our mother company, Dong-il Corporation, with 50 years experience in cotton spinning and textile industry, is the largest textile group in Korea, covering from upstream of cotton spinning industry, to midstream in dyeing& finishing, sewing thread and

interlining, and finally to downstream textile industry such as suit, knitwear, and brand apparels like Lacoste. Currently it has overseas investment factories in Indonesia and Vietnam.

Until mid-'90s, our mother company used to have 4 spinning factories in Korea, but due to increasing burden of labor cost, we have seriously considered shift of part of those factories to abroad. This was the direct motive to make an overseas investment in Egypt.

As you might know well, there are many aspects to consider when deciding the ideal location for overseas investment. Keeping key factors to make spinning industry successful, we have reviewed cotton producing countries like India, Pakistan, China, Turkey, and Uzbekistan as well as cheap labor-cost providing countries such as Indonesia and Vietnam.

After almost one and half year's study, we finally selected Egypt. The reason was Egypt has been producing high quality cottons, and we wanted to utilize its local cotton.

There were two factors which we seriously considered during our decision-making period. One is we knew Egyptian cotton well to produce high quality yarns.

The other is that if we invested there, we would be supplied with enough local cotton without problem.

At that time, it was a little bit risky for Asian people who didn't have experience with Middle-East, far from Korea and with quite different cultural background.

All we believed at that time is "Without risk-taking, No business".

That was the start of our investment operation in Egypt seven years ago.

3. Egypt as an Investment Location

Historically Egypt is the country producing high quality cotton in the world.

It's needless to repeat why Egyptian cotton has the best characteristic figures not competing by other varieties in elsewhere.

Therefore, if we give the top priority to the cotton producing location for investment, Egypt would be a No. one country, although the marketing of such high quality cotton products are rather limited because of its expensive price.

Secondly, if we consider marketing to European countries, Egypt would be one of countries for suitable location due to its adjacent location to Europe and duty-free merit.

Thirdly, there are generally enough work forces with cheap labor cost, although we may need to carefully review this matter in terms of efficiency and productivity.

Those three factors are considered to be main strong points to induce foreign investment in the cotton spinning industry in Egypt.

However, there are also negative aspects that we must not neglect, as follows:

- 1) When comparing with its long history and its size of nearly 2.9 million spindles capacity spinning industry, the spinning-related industry has not developed fully. Most of machinery parts and consumables necessary for spinning industry are to be imported from abroad, causing high cost and extra expenses, long lead time and no way in case of emergency situation.
- 2) Similarly, despite the size of spinning industry, its downstream industry is relatively less developed. Upstream industry can not be developed alone, without balancing with downstream industries like garment and apparel through weaving, knitting & dyeing.
- 3) Size of domestic market is very low level. This forced new investment to develop new export market primarily.
- 4) As far as export market is concerned, it has only Europe and United States, while there is slight chance to export to neighboring countries like Middle East and African countries, because of low level of market potentiality in those regions.

All above aspects are the ones we might consider when making investment decision. Now, I would like to explain what kind of difficulties our operation has faced.

4. Difficulties in Doing Business in Egypt

1) Raw materials

Here, I want to just point out technical aspects of cotton matter, and later on I want to talk about the cotton supply aspect.

We may point out that cotton for local mills are generally lower grades after better quality cotton is exported. With this lower quality, it's difficult to compete with our competitor countries that also use the imported Egyptian cotton for the same market.

Also, we have to mention the contamination is one of fundamental problems, although it is said it has been improving.

Another difficulty is that we have to buy all the required cotton at a certain period and pay at almost one time. Without payment in advance, we can not secure the required quantity of cotton. This causes heavy financial burden as well as heavy load of storage space and safety matter. There must be a proper system to ease this burden.

2) Labors

The establishment of work attitude was very important mission. We have spent huge amount of invisible investment in changing mentality to set up a sound work attitude.

Another important matter is that practically we could hardly dismiss anyone who was found to be disqualified. It affects good working mood and work moral in the factory.

Also, full-time working on Friday is the minimum requirement for continuous operation of spinning industry, but it needs extra costs and efforts under the current laws and social customs.

3) Other Problems affecting the Business

Customs clearance is another serious difficult issue which many foreign companies are complaining: delays and unreasonable expenses, sometimes missing & damaging during clearance would be major headache, especially when importing.

As technical matter, electricity power cut often happens without prior notice, which causes loss and sometimes damages in production.

5. Cotton Matter: Our Experience and Suggestion

We have invested in Egypt mainly for the purpose of utilizing local cotton and labors. However, ironically the most serious difficulty we have faced every year was cotton problem: shortage of required quantity of local cotton has caused many problems in keeping proper production planning, further negatively affecting marketing activities, and finally discouraging the sincere intention of foreign investor.

I don't think the natural short production is the problem, but I think it's a matter of mismanagement of supply & demand.

First of all, let me explain what we experienced, and then I would like to suggest some ideas..

This year cotton supply has been reduced substantially, maybe for first time during two

or three decades, due to less plantation area. We were informed that as a method to feed all spinning mill with limited supply of cotton, the government decided to intervene the distribution to local spinning mills by applying a unique rule.

Accordingly, we were allocated with reduced quantities of local cotton of long staple fiber variety, about half of its last year consumption. Since we already forecasted the overall shortage in the local cotton production, we prepared for securing the required cotton in advance and made contract with cotton company to buy our requirements.

However, we could not get our contracted cotton which we already paid for. The essence of business was restricted, ignoring the free market policy, regardless of whether private company or foreign investor.

Later on, there was a chance to be supplemented with the imported cotton, but we could not use due to foreign clients' quality requirements. As a result, we could not fulfill the supply of considerable export orders which we already received long time ago because of no more cotton, and subsequently we lost our export market to our competitor countries while separately paying claims for non-delivery of orders.

I am much worrying about the possibility that it might happen again in the future from time to time whenever there is a shortage of local cotton supply.

For long term development of spinning industry as well as to encourage foreign investment, I would like to suggest followings.

Firstly, there must be a certain level of government role in local cotton supply sector. Egyptian government intended to liberalize the cotton sector, but at least it must be responsible for the steady supply of local cotton enough to meet the requirements for both local demand and export demand.

It is very clear to foreign investor that if local cotton supply situation seems uncertain in the long run, no foreign investor would be interested in investment.

Secondly, there must be a certain portfolio in distributing local cotton between domestic mills and exporting cotton itself, keeping that priority must be given to the local consumption as far as it deserves the value added creation.

Thirdly, distribution among local mills must be done by a very reasonable and practical principle. Priority must be given to the mills which can maximize the value from the view-point of national economy. For this reason, export-oriented mills are suggested to be served first with priority.

Fourthly, there must be a governmental level taking care of foreign investment in respect of supply of local cotton. As mentioned earlier, our investment in Egypt can not be justified without availability of local cotton. We did not invest here in order to use imported cotton. This is the clear objectives for all foreign investors.

Fifthly, currently not only cotton distribution but also cotton yarn export has been controlled under government influence. We agree that this price control system contributed generally to set up the guideline as minimum price and hence to prevent dumping sales. However, all foreign clients regard this price as maximum price to pay. No client wants to buy at higher price while other Egyptian mills are selling at the guideline price.

Also, the guideline price is likely to be used by some companies as a good excuse to sell their products whatever their real manufacturing cost may be.

Therefore, in order to strengthen the competitiveness of Egyptian yarn export in the world market, it is also recommended to lift such government-controlled pricing system.

In conclusion, it is strongly recommended to let cotton and yarn sector be completely free from government intervention except minimum role of government to ensure the steady supply of local cotton.

Lastly, I hope our experience as above could be a good guideline for the prospective foreign investors, and further helpful to government for setting up reasonable policy to encourage the spinning industry and foreign investors.(END)