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Economic Reports

18 March 2020

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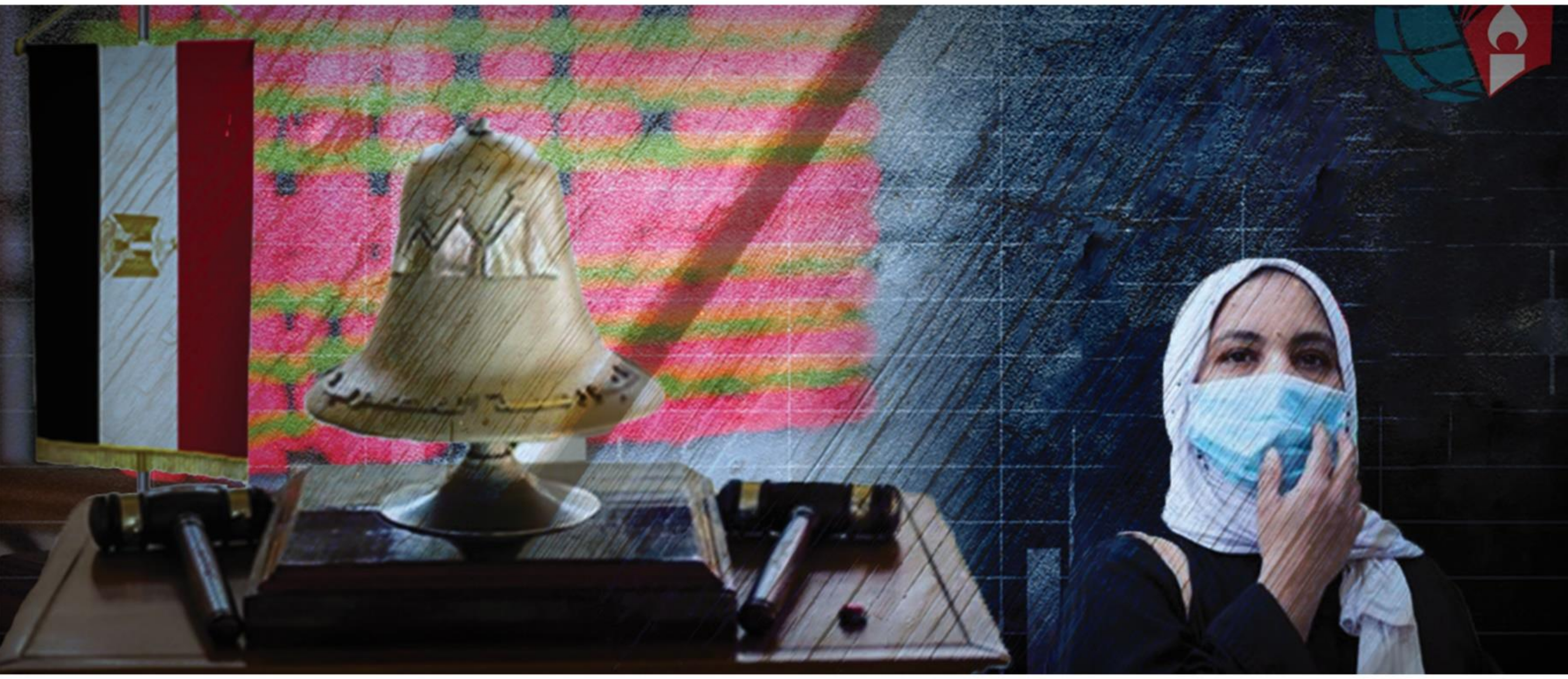

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Repercussions of the Spread of COVID-19 on Egyptian Economy

Dr. Ahmed Zikrallah

With the sweeping spread of the coronavirus in February and March 2020, and the repercussions of this on global economies, questions arise about the nature of the likely effects that this "pandemic" can cause in Egypt, especially with the rising numbers of infected cases and the unpreparedness of the Egyptian health sector that has been suffering from government negligence over the past period, and also in light of the rentier nature of the Egyptian economy, where every resource is of paramount significance to the State and its economic and social stability.

Rentier economy is defined as the State's reliance on one or more income sources, often natural sources, that do not require complex production mechanisms, whether intellectual or material[1]. Thus, a rentier State is "a State that gets a substantial part of its revenues from external sources in the form of rent[2]. Although determination of rentier sources is debatable, it is agreed that the dominance of external rentier elements is the determinant of whether the State should be described as a rentier State or not." However, the phenomenon of rentier proceeds in general is not limited to a specific economy, as there are rentier elements in every economy that differ in intensity from one country to another[3].

In short, rentier economy is the one that its activity is restricted to areas and sectors that generate large returns with no need to engage in a productive or creative activity. In fact, debate is not centered on whether the Egyptian economy is a rentier economy or not, but rather on the degree of intensity of this rent in the country's economic component. In general, the Egyptian economy relies on a group of main elements that have represented the majority of income sources over the past period, including the Suez Canal revenues, tourism revenues, remittances of Egyptian expatriates,

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[1] Kanaan Hamagharib Abdullah: The Impact of Rentier Economy on Political System, Journal of University of Human Development, Volume 3, Y3, p.599

[2] Mohamed Nabil El-Shimy: Rentier Economy "Understanding and Problematic", Arab Democratic Center, January 6, 2016

[3] Hossein Mahdavy, "The Pattern and Problems of Economic Development in Rentier States: The Case of Iran", in Studies in the Economic History of the Middle East, ed. M.A. Cook (Oxford University Press, Oxford 1970)

foreign investment, and investment in domestic debt instruments, in addition to petroleum exports, and most recently the natural gas exports.

Undoubtedly, the above income sources are of great importance to the Egyptian economy, given that their returns are to a large extent determined by factors that can mostly be described as being outside the Egyptian economic model, that is to say domination of international economic variables on the extent and continuity of these flows. This paper will attempt to extrapolate the potential impact of the spread of the COVID-19, both worldwide and at home on the Egyptian economy, through the following points:

First: Likely impact of COVID-19 on the Egyptian Stock Exchange

The emergence of the coronavirus has deepened the declining performance of the Egyptian Stock Exchange that started from the second half of 2018 through the whole of 2019 until now. However, the only period that witnessed improvement of the stock market performance that had followed the flotation of the Egyptian pound, due to the competitive prices of Egyptian shares denominated in the local currency after it had been devalued by nearly 100%.

The first week of March 2020 ended with major losses, as the stock market fell by 5%, losing LE22.5 billion. On Monday, 9 March, the main index EGX30 recorded the largest daily loss since 2012, after closing down by 7.3% (after falling to 8.2% during the session), and then losses continued, where the decline rate index exceeded 33% since early 2020 until 16 March.

These losses were an extension of the harsh conditions that the Egyptian Stock Exchange witnessed during February, as it ended the month's transactions with a collective decline of all its indicators, and a decline of more than 5% of its market capital.

Of course, the Egyptian stock market losses came within the framework of the losses of the global and regional financial markets that were caused by panic over the spread of COVID-19, especially after the sharp decline in oil prices over the last two weeks. However, despite the fact that the losses of Egyptian stock market come in this context, yet, there are other causes, including the government's willingness to privatize the rest of public sector companies by listing them on the stock exchange, and adoption of the average share price as a pricing mechanism in the last month, which may impose further delay on offerings during the coming period.

The postponement of government offerings is considered violation of terms of the government's agreement with the International Monetary Fund (IMF) that strongly supports its the external borrowing process required to recycle debts, which means losing one of the significant resources for covering the public budget deficit.

The decline in the Egyptian Stock Exchange value as a global context may lead to withdrawal of a portion of foreign and Arab investments that entered the Egyptian market during the post-floating period, especially in light of the mechanisms of the transfer of investor funds approved by the Central Bank of Egypt (CBE), which is likely to put pressure on the Egyptian pound during the coming period.

It is expected that the decline in oil prices will continue, amid international reports that it may drop to below $30 a barrel, as a result of the slowdown in global activity, which is likely due to the recent raging Saudi-Russian conflict that has led some experts to expect that the oil prices decline may reach $20 a barrel. In general, this decline will have negative repercussions on the growth rates expected by international economic organizations. In addition, this decline in oil prices will constitute an economic and social catastrophe for all Gulf countries – as some studies estimated OPEC losses when the oil price drops to $30 a barrel by about $500 million a day, where the Gulf countries only bear approximately $300 million, including the countries that support the Egyptian regime. Accordingly, reserves of these countries will evaporate within two or three years according to some estimates, and of course, this disaster will be transmitted to the rentier Egyptian economy not only through the stock exchange, but also through the remittances of Egyptian expatriates.

Second: Remittances of Egyptian expatriates

Egypt ranked fifth globally with respect to money transferred from its citizens abroad during 2019, as the remittances of Egyptian expatriates exceeded $26 billion. Also, the remittances of Egyptians working abroad increased by 109.5% since the liberation of the exchange rate until the end of 2019, where the total remittances in 2016 reached about $12.6 billion, compared to $26.4 billion at the end of 2019, and $24.7 billion and $25.25 billion during 2017 and 2018, respectively.

Thus, the remittances of Egyptian expatriates constitute 8.8% of the Gross Domestic Product (GDP)[4]; and the Egyptian financial system depends on these remittances as a main source of foreign currency that reduces pressure on the Egyptian pound through pumping foreign currency in the banking sector, which contributes to financing imports, as well as balancing the balance of payments.

It is noteworthy that the number of Egyptian expatriates is estimated at 14 million, where the Arab region only hosts 65%. However, there has been a significant decline in demand for Egyptian labor over the last three years, most probably due to the decline in oil prices since 2014, which is expected to worsen during the coming period.

Egyptians working abroad are likely to face a major crisis during the next year or the coming two years, to be optimistic; and perhaps half of them will return to Egypt, which means not only losing half of remittances of expatriates, but the government will have to create job opportunities for these returnees, which is likely to put additional pressure on the Egyptian low-wage labor market, in addition to its arbitrariness and being outside the official track.

In addition, there are some Egyptian workers who are currently stranded in Egypt after some Gulf countries imposed an entry ban on Egyptians. Although Kuwait announced the possibility of renewing their residence card electronically, other countries have not taken positive steps in this regard. Moreover, there is no guarantee that workers in the private sector or even the government sector in these countries will retain their jobs after failing to return to their work in due time. Also, there are expectations that many of them are likely to be dismissed as part of plans to replace them with national workers.

In general, the decline in remittances of Egyptian expatriates will put a great pressure on the State's foreign currency revenues, and accordingly on the exchange rate of the Egyptian pound during the coming period, which may lead along with other factors, to erosion of the foreign exchange reserves accumulated during the post-LE flotation period, as they are likely to go to repayment of foreign loans

[4] For more details about the most important Egyptian revenues:
- Dr. Amr Darrag, Mostafa El-Nemr: "Egyptian Economy under Sisi: Reality and Future", The Egyptian Institute for Studies
- Dr. Ahmed Zikrallah: Egyptian Economy After 2013: Policies and Challenges, The Egyptian Institute for Studies

in the event that the global panic over the spread of coronavirus continues and its likely impact on the international debt market, which may prompt the Egyptian government to seek a new IMF loan.

Third: Tourism revenues

The United Nations World Tourism Organization (UNWTO) had expected that the number of tourists to Egypt this year will exceed 15 million, compared to about 13 million tourists in 2019, an increase of about 15.38%[5].

The CBE has announced that the tourism sector achieved a significant jump in revenues during the last fiscal year 2018-2019 with a rate of 28%, where tourism revenues reached $12.57 billion, compared to $9.8 billion in FY2017/2018.

Thus, tourism is considered the third source of Egypt's national income, after remittances of Egyptian expatriates, which ranked first with $26.4 billion, non-oil exports that came second with $17.1 billion, followed by petroleum exports with $8.8 billion, and Suez Canal revenues by $5.7 billion last year.

The measures taken by countries where the COVID-19 has been widespread or those trying to prevent its outbreak indicate that isolation, closing borders, and imposing restrictions on airport arrivals and departures will be key measures during the coming period, especially with countries that have historical precedents in concealing official statistics.

In general, the impact of incoming tourism to Egypt will be within the framework of the impact of the spread of COVID-19 on global tourism, as a result of decisions adopted by some to prevent travel or entry to them, in addition to personal initiatives of individuals refraining from movement, at least during the current year, which means that Egypt is likely to lose a percentage of this income on which it depends in meeting its obligations.

Hossam Al-Shaer, head of the Egyptian Chamber of Tourism, has recently stated that reservations decreased by 70% -80% compared to the same period last year[6].

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[5] Al-Arabiya, "There are expectations that the number of tourist arrivals will exceed 15 million"

[6] Bloomberg, "Egypt's Economy Faces a Double Whammy"

There are two main sectors that are linked to the tourism sector and the impact of the spread of COVID-19 on it, namely, the air transport sector, and Hajj and Umrah companies, where the potential impact on them can be addressed as follows:

1- Air transport companies:

The Minister of Civil Aviation stated that the indebtedness of EgyptAir amounted to LE20 billion from 2011 to 2015. However, after making a loss in FY2002/2003 of about LE246 million, the company started making profits for the next seven financial years, to reach LE533 million in FY2009/2010. After that, it again started to make losses on a continuous basis up to now. Thus, EgyptAir has completed its ninth consecutive fiscal year of losses.

EgyptAir officials attribute these losses to the decline in tourism, especially that between 83% and 91% of tourists arriving in Egypt come by air, as well as the increase in expenses due to the high cost of fuel, the pay of about 33,000 employees, and high cost of maintenance.

However, these justifications are not accepted by specialists who attribute the losses to mismanagement and execution of politically-oriented flights to some countries that may not meet their operating expenses. They say that although tourism improved in FY2012/2013, where the number of tourists reached 12.2 million, yet losses only decreased by only LE1.7 billion.

In November 2018, Ahmed Adel, the chairman of EgyptAir Holding Company, revealed that suspension of the direct flight line with the Qatari capital, Doha, for a year and a half, negatively affected the company's gains, noting that the situation in the region, especially in Libya and Syria, caused heavy losses to the Egyptian company, because there were profitable lines for these countries, and suspending them caused great losses for the company[7].

An EgyptAir official estimated the losses of suspending flights to China at $2 million per week and said that EgyptAir operates about 15 flights per week to 4 destinations in different regions of China due to a recent growth of trade and tourist traffic with Egypt[8].

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[7] Chairman of "Egypt Air": Suspension of the Doha route negatively affected our profits

[8] "Egypt Air" losing $2 million on a weekly basis for suspension of flights to China

In light of the likely negative impact of COVID-19 on the tourism sector, the likely abolition of Umrah trips or reducing their numbers, and the likely reduction of the numbers of Egyptian workers abroad, the future of the air transport sector in Egypt will be extremely difficult.

2- Umrah and Hajj companies:

The Egyptian authorities have always considered spending on Hajj and Umrah a leaking of foreign currency, especially that the number of Egyptian Umrah performers in 2016 exceeded one million and a quarter. The number of tourism companies registered at the Egyptian Chamber of Commerce reached about 2,500 companies, including only 300 outsourcing companies, while the remaining 2,200 companies all work in Hajj and Umrah trips. Therefore, the State, in cooperation with the Saudi side, made a set of decisions that led to a decrease in the number of Umrah performers.

The number of Egyptian pilgrims decreased from one million and 300 thousand in 1437 AH to 376 thousand pilgrims in 1439 AH, but the number quickly reached 538,940 pilgrims in the year 1440 AH, according to the statistics of the weekly Umrah Index issued by the Saudi Ministry of Hajj and Umrah.

In general, the Egyptian administration considers reducing the number of Umrah performers in order to preserve foreign currency; and these numbers are also likely to be significantly decreased during the current year and perhaps next year, especially after the procedures carried out by some Gulf countries against Egyptian workers and Egyptians in general. Therefore, reducing the number of Umrah performers and possibly the number of pilgrims or canceling the whole season may be in favor of the official point of view of the Egyptian regime, but from the overall point of view the two things seem equivalent, given the expected losses of the national airline in case of canceling or reducing the numbers of Umrah performers and pilgrims.

Fourth: Suez Canal revenues:

The Suez Canal achieved revenues of $5.9 billion during FY2018/2019, an increase of 5.4% on an annual basis, which is the highest revenues ever achieved by the canal which is one of the most important sources of "hard currency" to the country.

There are pessimistic expectations about the global economy during the current year due to the spread of the coronavirus and its negative impact on global growth. In this regard, the United Nations Conference on Trade and Development (UNCTAD) announced early March that China's exports of vital parts and components for products ranging from automobiles to cellphones are estimated to have shrunk by an annualized 2% in February, costing other countries and their industries $50 billion. "There is a ripple effect throughout the global economy to the tune of a $50 billion fall in exports across the world," Pamela Coke-Hamilton, director of UNCTAD's division of international trade said, adding, "The figure, which covers only the month of February, is preliminary and may be a 'conservative estimate'," she said[9].

According to UNCTAD, countries or regions suffering the highest export losses due to the disruption are the European Union (EU), with nearly $15.6 billion, the United States ($5.8 billion), Japan ($5.2 billion), the Republic of Korea ($3.8 billion), Taiwan ($2.7 billion) and Vietnam ($2.3 billion)[10].

This simply means a decline in global trade movement during the coming period; and whatever the rate of decline is, as it cannot be estimated precisely being dependent on the ability to control the spread of the coronavirus, the reports about the declining Suez Canal revenues seems logical not only due to the decline of trade but also because of the rapid declines In oil prices, resulting from pessimism about the growth rate of the global production, which inevitably means a reduction in global production and hence affecting the movement of maritime transport.

Fifth: Egyptian exports:

Egyptian non-oil exports achieved about $17.1 billion in 2019, while petroleum exports reached $8.8 billion in the same year. However, the diversity in Egyptian commodity exports along with the decrease in returns of each product compared to the volume of global production and export makes the expected decline in Egyptian commodity exports will not be significant.

The oil exports are expected to face a major problem as a result of the global declining in oil prices. In addition to crisis of declining returns, the problem may extend to the escape of investors working in the fields of mining and exploration, especially in light of expectations that oil prices may not even

[9] Shortage of Chinese components causes $50 billion drop in global exports in February

[10] Reuters, "Shortage of Chinese parts caused $50 billion fall in February's global exports: U.N."

meet the actual extraction costs; and the same applies to recent Egyptian gas exports, estimated at $1.2 billion in 2019.

This means that Egypt's loss in relation to the petroleum sector has doubled: first, for the declining prices, which may last for two years, and second, for the diminishing foreign investment in exploration and extraction, which constitutes most of the foreign investment incoming to Egypt in recent years.

I think that the problem that must be raised right now is the extent to which the domestic prices of energy (gasoline-gas-electricity) respond to the global decline in oil prices. In this regard, I believe that the Egyptian authority is in a real dilemma before the Egyptian consumers, as well as Egyptian and foreign investors operating in Egypt who are allowed to import gas from abroad according to the last energy law.

The essence of the problem is the contract with Israel, which includes a predetermined price of more than $5 per million cubic feet of thermal units, with annual payments amounting to approximately $2 billion. To face this situation, the Egyptian authorities will either sell at a loss or sell the product to domestic consumers at high prices. Anyway, coronavirus has come as a savior to the regime, albeit temporary, of immediate accountability – and coronavirus will serve as a pretext for the non-improvement of the citizen’s living or services provided to him – after the catastrophic failure of the regime to turn Egypt into a regional energy hub, as well as its involvement in the gas agreement with Israel.

Sixth: Egyptian pound’s exchange rate

The exchange rate of the Egyptian pound determines its purchasing power and accordingly the impact of this on the citizen’s standard of living. However, the Egyptian authority tries to promote recent improvements in the pound’s value as a success of its policies, although the citizen’s standard of living has not witnessed any improvement.

The exchange rate of the pound is determined by the dollar revenues to Egypt, which are mainly rentier revenues; and as we mentioned above, they were severely affected by the spread of the coronavirus. In addition, there are more areas that are likely to negatively affect the Egyptian economy, including:

1- Foreign direct and financial investments:

Over the past period, Egypt has relied on investments in local debt instruments as a main source of foreign exchange, to finance the budget deficit, and to maintain the pound's exchange rate. Foreign investments in government debt instruments reached $22 billion by the end of December 2019, which enabled the monetary administration to preserve the accumulated reserves coming from loans obtained in the period that followed the pound flotation.

Amid the continued spread of the coronavirus, part of the indirect investments are expected to focus on investment in the US dollar, the Japanese yen and the Swiss franc as safe havens. Indeed, Egypt has witnessed foreign portfolio investment inflows with a value ranging from $2 to $2.5 billion over the past two to three weeks[11], in light of investors' pursuit of safe investment havens amid market fluctuations. It is expected that the monetary administration will use its reserves to reduce the major declines in the pound's exchange rate. However, the continuation of the crisis and accordingly bill withdrawals means evaporation of reserves and their inability to stop the declining value of the Egyptian pound, which is highly likely in the coming period.

The major problem that Egypt may be exposed to is the likely continued declining of share prices in world markets; as these declines will push hot money investors, who hold treasury bills and bonds in Egyptian pound, to liquidate their winning portfolios and buying the dollars that they had previously sold when they first entered the market. It is to be mentioned that the CBE over the past year put this as a justification for the exaggerated decrease of the dollar price against the Egyptian pound, despite the unstable nature of these investments, which means putting more pressures on the exchange rate.

It is noteworthy that Egypt has thus paid twice the price of these funds, one by raising the interest rate and the other by reducing the dollar price – which is economically unjustified – which means allowing investors to double their profits.

Amid foreign loan entitlements and Israel's dues for its natural gas exports, Egypt is likely to witness a sharp decrease in the foreign exchange reserves – perhaps erosion of 50% of them – especially in

[11] Enterprise Bulletin

case the government fails to borrow from international markets, in what is known as recycling its debts.

Therefore, the result will be either an abnormal increase in foreign loans, or a sharp decrease in the foreign exchange reserve, both of which mean an increase in the dollar value and more burdens on the Egyptian citizen over the rest of the current year; but if the spread of the coronavirus continues, the situation is likely to become more complicated.

As for the direct investments, as above mentioned, the demand on oil exploration and extraction, the main component of foreign investments in Egypt, is expected to decrease on a continued basis. The foreign investment in oil exploration and extraction during 2014-2018 acquired a share between 53% of investments in 2015/2016 and 71.7% in 2013/2014[12]. Also, amid the resounding losses of global capital during the last period, I do not think that direct investments can compensate for a small percentage of indirect investments, which means that the impact of the exit of financial investments has nothing to compensate for, in addition to expectations of a logical decrease in direct investment itself.

2- External borrowing:

Over the last period, the Egyptian regime has relied on foreign loans to support the foreign exchange reserves and finance the public budget deficit, where foreign loans increased from approximately $39 billion at the end of 2013 to approximately $110 billion at the end of 2019.

In light of the current global circumstances and the domestic circumstances of the Egyptian economy, questions arise about the extent of importance of external loans during the coming period, and how far the government will be able to borrow.

Foreign loans are expected to become the last resort of the Egyptian authority in the face of crises caused by the outbreak of the coronavirus, amid the government's need to borrow for purposes of recycling loans, stabilizing the pound’s exchange rate, and facing the trade balance deficit amid import inflation and failure to achieve the desired export increase.

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[12] Al-Jazeera, “Egypt – Negative Results of Foreign Investments”

Add to this the great losses of major international banks due to the decline in their share prices, the slow growth of debtor companies and unanswered questions about their ability to pay off their debts, the major losses of global stock exchanges, and the oil price losses of the regime's allied states – all these things may indicate that Egypt's external borrowing may become more difficult during the coming period, not necessarily the volume of funds available for borrowing only, but it may extend to the terms of borrowing, which seems to be more likely.

3- Government services funded from the general budget:

Undoubtedly, the expected decline in some revenues that can be described as rentier revenues, such as tourism revenues, revenues from the Suez Canal, and remittances from Egyptian expatriates; will have a negative impact on the State's budget deficit, which is the essence of the International Monetary Fund agreement with the Egyptian government, in addition to the negative impact on the government's ability to spend on public services provided to citizens, especially health and education.

Recently, the Minister of Finance stated that the Finance Ministry might review budget targets if the crisis persisted, where the government's target for economic growth is about 6% in the current fiscal year and about 6.4% in the next fiscal year 2021/2020, while the initial budget surplus is expected to continue at 2% In the coming fiscal year. The ministry will also reevaluate its target to reduce the in the budget public debt in the next fiscal year to 79% of GDP under the current situation[13].

The automatic pricing mechanism for petroleum products every three months will deprive citizens and manufacturers of the benefits of the low oil prices; and the effect of that decrease remains positive only on the public budget deficit, as each dollar reduced through the low oil prices provides four billion pounds for the budget (the price of oil in the budget is $76 per barrel); and this positive impact is likely to be absorbed by the expected higher interest rates on borrowing.

4- Lack of imported goods

Many experts point out that the negative effects of the spread of the coronavirus on Chinese production will extend to the global economy. The Wall Street Journal indicated that "China's shadow

[13] Enterprise Bulletin

has grown so long that even industries that have shifted production beyond the country can't wriggle free of its grip on supply networks[14].

Locally, manufacturers are expected to suffer from disruptions in trade and supply chains; and may find it difficult to provide some production components and spare parts amid difficulty in finding alternatives, while suppliers may encounter supply difficulties.

Indicators of this have already started to appear in the Egyptian market with the diminishing of some commodities imported from China, especially electrical appliances and sanitary ware, which raises expectations of an imminent increase in their prices, as many production lines of electrical appliances and sanitary ware depend on importing parts from China.

The Egyptian Al-Borsa (Stock Exchange) Newspaper has reported that several factories started to reduce production and several traders started to store devices in anticipation of a rise in their prices with the decreasing Chinese imports. The paper also indicated that these factories are trying to find alternative markets other than the Chinese markets, amid a rise in prices of electrical appliances by 3-5% and in the sanitary and plumbing tools by 10-20% since the spread of coronavirus in Egypt, taking into account that Egypt imports 80% of its sanitary ware from China.

Conclusion

- The spread of coronavirus in Egypt is still at its primary stages; and therefore, it is extremely difficult to anticipate accurate rates of its spread and the negative repercussions of this on the Egyptian economy. However, the rentier nature of the Egyptian economy increases the likely external impact and makes it faster and deeper, posing extremely negative effects on the national economy in the short and medium term.

- The outbreak of the coronavirus highlighted the structural defects of the Egyptian economy, especially its dependence on rentier sources, amid failure of the government to shift towards productivity and competitiveness.

[14] Wall Street Journal, "Companies That Got Out of China Before Coronavirus Are Still Tangled in Its Supply Chains"

- The Egyptian regime’s dependence on hot money and external borrowing, amid failure to attract foreign investment, has entrenched the rentier nature of the Egyptian economy. In addition, the expected decline in oil prices as well as involvement in importing gas from Israel has deprived the Egyptian consumer and the local investor of benefiting from price declines.

- It is expected that investors in treasury bills will demand higher interests, otherwise their hot money will seek other safe havens, and the external borrowing sources that the government is likely to resort to for facing these negative economic repercussions will gradually deplete if the crisis continues.

- The government has failed to support private sector growth which has declined steadily over the past three years. It has also failed to improve the citizens’ living standards and raise consumption, which is the main obstacle to the private sector. Therefore, the private sector crisis is likely to worsen with the expansion of the military economic empire, thanks to the unfair competitive advantages. Also, the supply crises that have already begun as a result of the decline in Chinese production, will put pressure on the private sector under the expected favoritism of the competing military enterprises.

- The initial reading of the economic repercussions of the spread of the coronavirus in Egypt and the whole world indicates the inevitability of an increase in the interest rate. Also, the domestic and international bond offerings are not expected to succeed at the same rate of its success in the past, and will even partially fail, which means that the recycling of domestic and external debts will face a great dilemma. While the domestic debt is expected to jump to LE5 trillion by the end of this year, the external debt is expected to exceed $150 billion. However, Egypt is likely to resort to the International Monetary Fund again for seeking new loans.