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Egyptian Strategic Report 2019 The Egyptian Economy - Policies and Challenges

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Egyptian Strategic Report 2019 (The Egyptian Economy - Policies and Challenges)

There is much debate among observers on the reality of Egyptian economy, in light of the successive decisions, laws and enterprises, described as “national projects”, that have excessively relied on domestic and external borrowing for their financing, in addition to debate about the priority and even economic feasibility of such projects.

The report aims to provide an analytical picture of the overall Egyptian economic conditions, starting from analyzing the official figures with the aim of extrapolating the results in attempt to explore the validity of approach, the feasibility of action and the sustainability of the impact, as original goals of any development process. With regard to the Gross Domestic Product (GDP) growth, the growth boom is mainly due to growth in 6 sectors, accounting for about 77% of it during FY2017/2018, namely the mining sector by 15.8%, the manufacturing industries by 12.2% , the construction sector by 10.3% , the wholesale and retail traders sectors by 9.6%, real estate activities by 7%, and the agricultural sector by 6.8%.

The sectors that mainly contribute to the GDP growth are: the mining sector, the Suez Canal returns, tourism, and Egyptian expatriate remittances, that is, the main components of GDP in Egypt are “rentier”, mainly dominated by sectors that depend on consumption; and therefore, it can be said that current economic growth is neither inclusive nor sustainable. Consequently, the current GDP growth rate is lacking the main goal of achieving growth, i.e. raising the living standards of citizens, as the average citizen still suffers from high inflation, as well as poor education, health care and transportation services. The figures also show that the high GDP growth figures are mainly denominated in the Egyptian pound. However, if they were denominated in US dollar, we would find a GDP contraction, not growth, after FY2015-2016.

Also, the unprecedented high rates of domestic and external debts necessitates that about 40% of government spending in budget must be allocated for paying off the loan interest, and may result in a weakening the regime’s ability to borrow in the future, in addition to the direct impact of borrowing on the private sector’s domestic investments due to the high interest rates. This has resulted in a

lower total value of private sector investment amid the foreign investment's focus on hot money and the stock market instead of investment in productive sectors.

In addition, the high inflation rates as a result of flotation of the Egyptian pound, lifting fuel subsidies, and increasing energy prices, have mainly contributed to raising the cost of austerity policies on Egyptian citizens. With the absence of appropriate pay increases that cope with the inflation rates and high prices, the numbers of the poor in Egypt have escalated to unprecedented rates, adding about 5 million more citizens to those already under poverty line within only three years, to raise the total number of Egyptians under poverty line to more than 30 million citizens – where official poverty rates have increased to 32.5% in 2017, against 28% in 2015, according to the Central Agency for Public Mobilization and Statistics (CAPMAS).

Before 2011, the Egyptian economy had suffered from a set of structural imbalances to which it is still held hostage up to date. Rather, the extremely high rates of domestic and external borrowing have added more imbalances. In addition, the political interference in directing economic projects has contributed to creating a significantly dangerous economic situation in the medium and long term.

This report represents a detailed reading in the policies and challenges of Egyptian economy after 2013, focusing on analyzing and understanding some basic data and information about its development from mid-2013 until now. It provides a holistic view of the economic policies followed by the regime led by General Abdel Fattah Al-Sisi and their actual results, in order to answer the question of whether the current path is the right track for development that may lead to improvement of the Egyptian economy.

In this regard, the report concludes that the policies adopted by the Sisi regime so far have not achieved the desired results; but on the contrary, inflation, poverty and debt rates have escalated, with continued weakness of health care, education and transportation services. In addition, a critical reading of the results that the current government claims to be positive, tells us the opposite, as Bloomberg has indicated, that only 1% of the Egyptian people benefit from those results.

The report focuses on the final results of each of the key elements affecting the Egyptian economy without entering into detailed deep data. For example, the current report assesses the monetary policy as a whole, given its impact on inflation and external debt. At the same time, the report

addresses in more detail the factors that affect these indicators such as evaluating the performance of the Central Bank of Egypt and its policies, as well as the work of banks and the corruption in the banking system. The reason for this is the desire to present a brief assessment that may highlight the economic reality by analyzing the final results of policies rather than focusing on addressing their details.

The report discusses 6 main elements of the Egyptian economy, namely the Gross Domestic Product (GDP), the State's general budget, the outcome of monetary policies, the foreign and private investment, the analysis of poverty and unemployment results, the current aspects of poverty, and the social impact of the policies pursued. The report also addresses the army's incursion into economic activity and presents a holistic review of the Egyptian economy by analyzing leakage and injection factors. The report then concludes with presenting a summary and some recommendations, including an outlook of the Egyptian economy during the coming years.

The report is divided into two main parts:

The first part, prepared by Dr. Ahmed Zikrallah, is about the "Egyptian economy - policies and challenges", which provides a description and analysis of the economic policies adopted by the Egyptian regime during the period under study, and the most important challenges facing it.

The second part, prepared by Dr. Amr Darrag and Mustafa El-Nemr, introduces an "analytical reading" and practical summaries of the key policies and challenges facing the Egyptian economy during the period (2013-2019).

Following is the full analysis of "Egyptian Economy under Sisi: Reality and Future", prepared by Dr. Amr Darrag and Mustafa El-Nemr, as follows:

Egyptian Economy under Sisi: Reality and Future

Dr. Amr Darrag, Mustafa El-Nemr**

Executive Summary

Many observers have been debating on the status of Egyptian economy, in light of the government's successive decrees, laws, and "national" projects as described by the government. While some argue

that these projects have relied excessively on internal and external loans with respect to financing, others debate their priority and even question their economic feasibility.

This report provides an analytical presentation of the overall economic situation in Egypt through analyzing the official figures in order to extrapolate the findings regarding the validity of approach, the feasibility of action, and sustainability of impact; the genuine objectives of any development process.

The GDP growth boom is mainly due to growth in six sectors that have accounted for 77% of the total GDP growth during the FY 2017/2018, most prominently the extractive sector by 15.8%, the manufacturing industries by 12.2%, and the construction and building sector by 10.3%, as well as the wholesale and retail trade by 9.6%, real estate activities by 7% and the agriculture sector by 6.8%.

In view of the sectors that mainly contribute to the GDP growth, the main sectors are mining, Suez Canal revenues, tourism, and remittances of Egyptian expatriates. In other words, the GDP components in Egypt can be described as 'rentier' resources, mainly dominated by sectors that depend on consumption; and accordingly, we can conclude that current economic growth is incomprehensive and unsustainable. Also, the main objective of achieving growth is missing in the current GDP growth rates, i.e. to improve the citizens' standards of living; as the average Egyptian citizen continues to suffer from the high inflation rates, in addition to poor education, health care, and transport services. Moreover, the figures that show a high GDP growth are mainly denominated in Egyptian pounds; if the Gross Domestic Product is denominated in U.S. dollars, we find that there is a GDP contraction rather than growth after FY2015-2016.

Due to the rise of domestic and external debts to unprecedented levels, about 40% of government spending in the budget is consumed in repayment of loans' interests, which may have a negative impact on the government's ability to borrow in the future, in addition to the fact that the debt levels directly affect the private sector's domestic investments as a result of the high interest rates. This has led to a decrease in the total value of private investment and the foreign investments have focused on 'hot money' and 'stock exchange' rather than investment in productive sectors.

In addition, the high inflation rates resulting from the Egyptian pound flotation, removal of subsidies on hydrocarbons, and increased energy prices have contributed significantly to raising the austerity policy costs on citizens. In the absence of any wage increases commensurate with the high inflation and rising prices, the proportion of the poor in Egypt has risen to an unprecedented level, a total of 30 million Egyptians, after bringing about 5 million new Egyptians under the poverty line in just three years. According to the official poverty rates announced by the Central Agency for Public Mobilization and Statistics (CAPMAS), increased to 32.5% in 2017 against 28% in 2015.

The Egyptian economy had suffered from a series of structural imbalances before 2011; but unfortunately, they are still affecting it up to now. Moreover, the escalating domestic and external loan rates have exacerbated these imbalances, and the political intervention in directing economic projects has contributed to creation of an extremely alarming economic situation in the medium and long terms.

Introduction

The term 'development' is constantly used by every new political system without providing an accurate definition of the term, although it has a multitude of meanings, including positive change, economic growth, good governance, good education, GDP growth, human development, health service improvement and others.

Development is a political term that has a range of meanings that depend on the context in which the term is used, reflecting and justifying various agendas. It can simply be defined as bringing about social change that allows people to achieve their [human potential](#)¹. Another important point is that development is a process rather than an outcome: it is dynamic in that it involves a change from one state or condition to a better one.

Numerous studies have concluded that the benefits of economic growth are usually not equitably distributed to citizens, and that the importance lies in the development model followed by the state

¹ https://www.soas.ac.uk/cedep-demos/000_P501_USD_K3736-Demo/unit1/page_12.htm

rather than achievement of a higher percentage of [GDP](#)². In other words, development is not only a positive difference in the GDP growth rate, but it is necessary to know how deep this growth is, where depth of growth is produced by diversification of economic production and exports, export competitiveness, productivity and efficiency increases, establishment of new companies, and technological upgrading, all of which should reflect positively on the state's [human capital](#)³.

Although every ruling regime in Egypt reiterates that its goal is to promote development and reap the fruits of economic reform, but over the last six years, the Egyptian economy has gone through a series of laws, decrees and agreements that have produced an economic and social situation that is almost completely different from what Egypt has experienced during the sixty past years.

This report reviews the evolution of the status of Egyptian economy since mid-2013 until now, i.e. the period in which power was transferred through a military coup from an elected authority to a paramilitary authority, by shedding light on the economic policies adopted by the regime led by General Abdel Fattah al-Sisi and their real results, in an attempt to answer the question of whether the current path is a real development path through which the Egyptian economy has already improved or not. The report states that the economic policies adopted by the Sisi regime so far have not achieved the desired results. On the contrary, poverty and debt rates have increased, amid escalation of inflation rates and deterioration of health care, education, and transport services. In addition, a critical reading of the results, which the current government claims to be positive, tells us the opposite, as Bloomberg noted that only 1% of the [Egyptian population](#) have benefited from these results⁴.

² Bourguignon, F. "The Growth Elasticity of Poverty Reduction: Explaining Heterogeneity across Countries and Time Periods" 2003. Growth and Inequality

Ravallion, M. "Growth, Inequality and Poverty: Looking Beyond Averages" 2001 World Development.. Pages 29(11).

Essama-Nssah, B. ; Lambert, P.J. "Measuring Pro-Poorness: a Unifying Approach with New Results" 2009 Review of Income and Wealth.. Series 55, No 3: 752-778.

³ Transformation, African Center for Economic "Growth with Depth" 2014. African Transformation Report

⁴ Abeer Abu Omar and Paul Wallace, "Poverty Keeps Getting Worse in the Middle East's Fastest-Growing Economy" August 2019. Bloomberg. Accessed 2/9/2019.

This report also represents a reading in another detailed report published by the [Egyptian Institute for Studies](#)⁵, "The Egyptian Economy after 2013: Policies and Challenges", including a lot of detailed figures and data. This report focuses on analyzing and understanding the data and information contained in the long [report](#) to reach a real assessment of the current economic situation. This report also focuses on the final results of each of the key elements affecting the Egyptian economy without addressing deep detailed data. For example, the report addresses assessment of the overall monetary policy through the impact of economic policies on inflation and external debt. However, the lengthy report addresses with more details the factors affecting these indicators such as assessment of the performance of the Central Bank of Egypt and its policies in addition to evaluation of the work of banks and corruption within the banking system. The reason behind this is a desire to produce a brief assessment of the economic situation by analyzing the final results of policies rather than discussing those policies in detail.

The report addresses six main elements of Egyptian economy, namely, GDP, state budget, results of monetary policies, investment (both foreign and private sector), analysis of the results of poverty and unemployment, current manifestations of poverty and social consequences of the adopted policies.

The report also points to the military incursion into the economic activity, and provides a holistic vision of the Egyptian economy through analyzing factors of injection and leakage, and then moves to the conclusion and recommendations, ending with providing an outlook of the Egyptian economy in the near and medium term.

Gross Domestic Product

Gross Domestic Product (GDP) refers to the total monetary or market value of all the finished goods and services produced within a country's borders within a specific time, usually one year, as a comprehensive scorecard of the country's economic health. Although the main objective of raising growth rates is to have a positive impact on the lives of citizens, the situation in Egypt is otherwise.

GDP Structure

⁵ Ahmed Zikrallah, Egyptian economy after 2013, policies and challenges, EIS, 2 Aug. 2019.

There have been successive increases in GDP in Egypt over the past five years, where it rose from LE 1.82 trillion (about \$ 230 billion) in 2015 to LE 3.4 trillion and LE 4.3 trillion in FY2016/2017 and FY2017/2018 respectively. Also, the growth rate increased from 2.2% in FY2014/2015 to 3.6% in FY2016/2017 and 5.3% in FY2017/2018 with expectations to reach 5.5% to 6% in FY2018/2019. The GDP at the cost of factors and current prices is about LE 6 trillion, with a real growth rate of 5.6% in [FY2019/2020 budget](#)⁶.

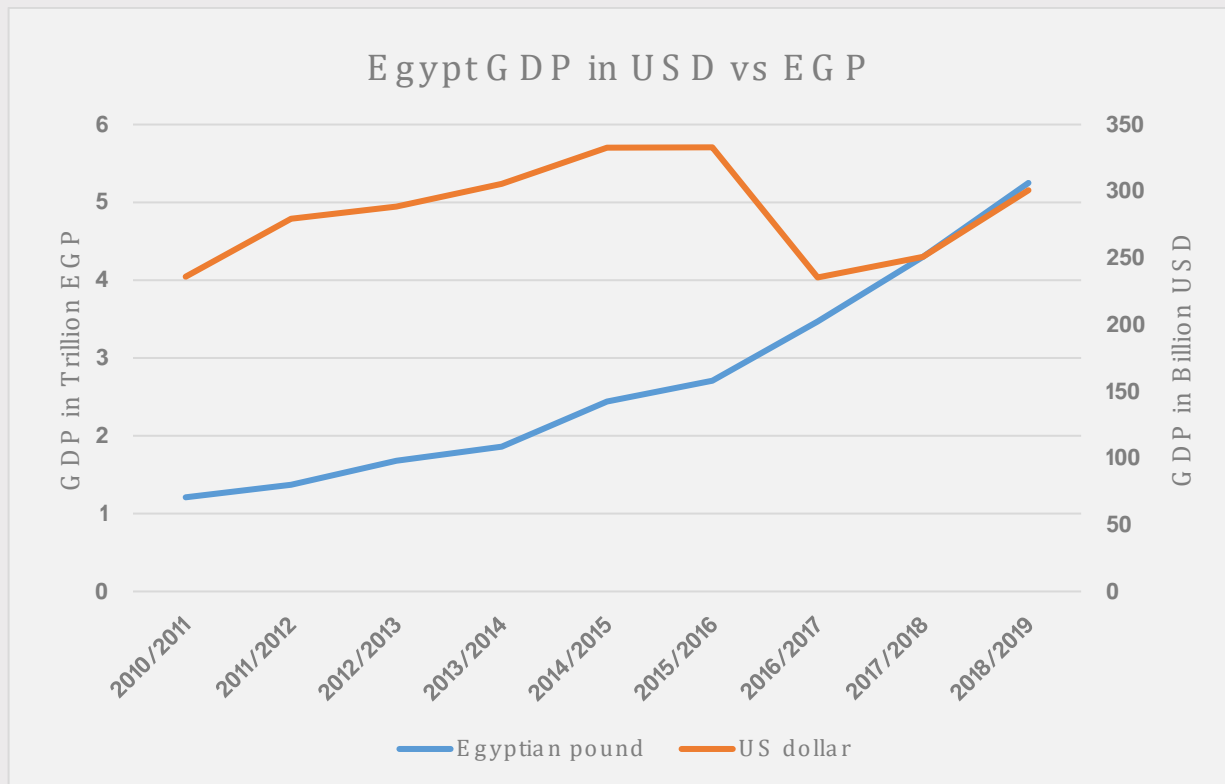
However, when we look at the dollar-denominated GDP, according to World Bank data, the Egyptian GDP has actually declined since 2013, as it reached \$ 250 billion in 2018 against \$ 332 billion in 2016 due to the government decision to float the Egyptian pound in November (2016), in addition to the policy of printing too much money, both of which led to high inflation rates significantly. It is noteworthy that the increase in the Egyptian pound-denominated GDP is also due to inflation.

Figure (1) compares the dollar-denominated GDP with the pound-denominated GDP: The sudden rise in the pound-denominated GDP in 2016 against a sharp decline in the dollar-denominated GDP in the same year reflects that the rise in the value of GDP was mainly due to the government decision to float the local currency and consequently the high inflation rates.

On the other hand, some argue that what is important in measuring the GDP is GDP growth rate, not GDP value. Although the boom in the GDP growth rate seems positive at first glance, a closer look at these figures indicates otherwise: First, in view of the main sectors that feed into the GDP, we find they include the mining sector (after subtracting the industrial output, construction, and retail and wholesale trade), the Suez Canal revenues, tourism, and remittances of Egyptian expatriates. The main components of GDP are rentier and do not lead to inclusive and sustainable growth. In other words, the main components of Egyptian GDP can be described as 'rentier' that cannot lead to comprehensive and sustainable growth.

Figure 1:

⁶ The draft budget of FY2019/2020, the official website of the Egyptian Ministry of Finance



Source: Central Bank of Egypt data (for EGP) and World Bank data (for USD)⁷

Second, the results did not reflect positively on the lives of citizens. On the contrary, the results were completely negative. Poverty rates rose to 32.5% in 2018 in addition to high inflation rates and continued deterioration of health care, education and transport services.

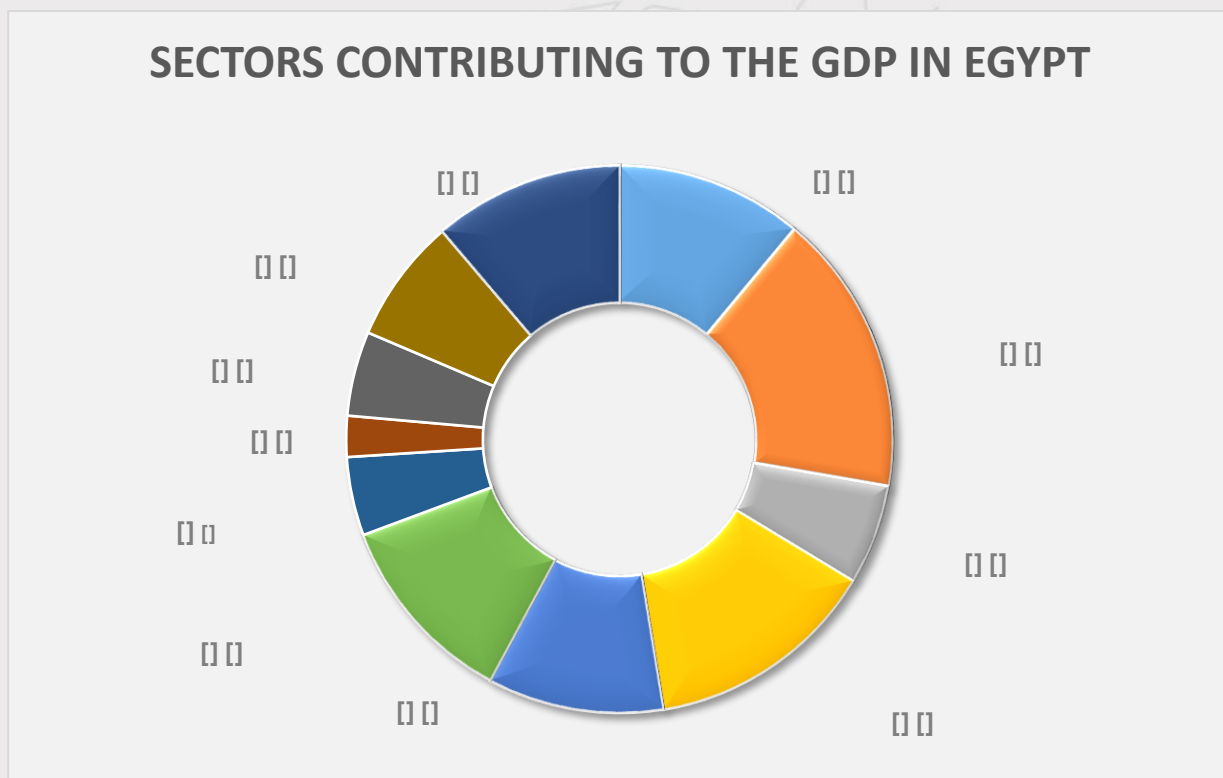
Figure (2) shows the percentages of various sectors' contribution to the GDP, where the manufacturing sector constitutes 17% of the GDP (and in case of excluding the refining sectors, it becomes 13% only), followed by the wholesale sector by 14% and the agriculture and fisheries sector by 12% and the real estate activities sector by 10%.

The nature of sectors that contribute to the GDP explains the negative impact on citizens despite the high growth rates. The growth in the mining sector is mainly due to the early opening of the Zohr

⁷ The GDP for FY2018/2019 was calculated by the researcher based on the dollar exchange rate mentioned in the general budget, i.e. LE 17.46.

gas field and the Sukkari gold mine. Despite the importance of the mining sector in the provision of raw materials for the purposes of production, domestic consumption and export, nonetheless, its sustainable participation in growth depends on the existence of an active industrial sector, which is not available in the Egyptian case, as well as on the size of reserves and new discoveries, which are unreliable as a major sustainable component of growth that can provide new jobs. As for the construction sector, real estate projects generate fixed assets but do not provide sustainable employment.

Figure 2:



Source: The Central Bank of Egypt⁸

As for the fiscal year 2019/2020 budget, the GDP at the cost of factors and current prices is about LE 6 trillion, with a growth rate of 5.6%⁹. It is expected that the most contributing sectors to the GDP

⁸ The Central Bank of Egypt, Monthly Statistical Bulletin 268, July 2019

⁹ The state draft budget for FY2019/2020, the official website of the Egyptian Ministry of Finance

are manufacturing and petroleum products sector by LE 984.9 billion, about 16.4%; the wholesale and retail trade sector by LE 814.6 billion, about 13.5%; the oil and gas extraction sector by LE 773.7 billion, about 12.9%; the agriculture, forestry and fishing sector by LE 676.3 billion, about 11.2%; and the real estate sector by LE 441.2 billion, about 7.35%.

Thus, **the GDP growth is dominated by sectors that rely on consumption rather than production and investment, and their productivity can be described as largely unsustainable.** For example, the real estate sector depends on a set of projects directed by the government, which does not reflect the real state of supply and demand in the Egyptian society, taking into account that a large part of it came to meet the demand of the rich higher class. Also, the real estate sector generally suffers from recession, due to erosion of the purchasing power and the high prices of building materials, as a result of the pound flotation and the economic measures required by the IMF program, which have contributed to adding more burdens on the sector. Some experts are arguing about the existence of a real estate bubble that is about to burst, which reflects the fragility of reliance on the sector as a major component of the growth rate in the coming period.

Contribution of the industry and agriculture sectors to the GDP

In order to improve citizens' standard of living, we must focus on the real side of economy, while enhancing the efficiency and effectiveness of essential services. Considering this, the contributions of industrial and agricultural sectors to GDP growth can be assessed; as the contribution of the industrial sector remains meager, about 17% of GDP and only 13% after excluding the refining sectors¹⁰.

These percentages do not put Egypt in the path of real development, nor can they absorb the numbers of workers entering the labor market annually, in addition to absence of technological development. Also, the increasing positive figures in the industrial field always ignore the army's ownership of some important projects, such as the cement complex, for example. The problem is that the revenues of these army-owned projects do not flow to the economic activity cycle in addition to existence of question marks on their feasibility, especially the cement complex, which caused a real crisis for

¹⁰ See prolonged report (Tables 2,3,2).

the [cement sector](#)¹¹. Another example is establishment of a 'furniture city' in New Damietta in spite of the severe recession that has hit the sector due to the devaluation of the local currency, which contributed to closure of hundreds of small furniture workshops in [Damietta](#)¹².

As for the agriculture sector, it contributed 12% of GDP during FY2017/2018. The sector accounts for 24% of the workforce in Egypt and also contributes about 20% of Egyptian commodity exports. Although the sector has the potential to expand its productivity, the limited agricultural economic resources have prevented it for several reasons, including:

First: the massive encroachment on agricultural land in the wake of the January Revolution, 2011, a situation caused by the army's control over Egyptian lands and their overpricing, and preference of major companies, especially Gulf ones, to Egyptian citizens, pushing people to building on arable land as the only possible outlet. It is noteworthy that authorities have always addressed the problem of violations though reconciliation and have recently announced payment of specific amounts for settlement of such violations, as one of the innovative methods of money collection. Also, the limited arable land is the main reason behind the increase in the food import bill.

Second: the poor investment in the agricultural sector, especially in infrastructure such as land reclamation, and digging irrigation and drainage canals.

Third: the low productivity of Egyptian agricultural labor compared to many other countries due to low educational and technical levels.

This led to an increase in the food gap in some essential crops, where the food gap in wheat increased by 14.3% in 2016 compared to 2015, and 69% for beans, 52.6% for lentils, and 152.8% for [vegetable oils](#) during the same period¹³.

In conclusion, we can say that the huge increase in the Egyptian pound-denominated GDP does not reflect an increase in the volume of goods and services provided, but it is rather due to the high

¹¹ EIS, Egypt's Cement Crisis and Military Dominance, Ahmad Zikrallah.

¹² Alborsa News, "The dollar deepens crisis of furniture sector"

¹³ Institute of National Planning: Egyptian Food Security Report, 2017

inflation rates, as the GDP value falls if it is denominated in dollar. In addition, the announced growth is mainly relying on rent-based inputs, not generated from productive sectors such as industry and agriculture; which means that it cannot be sustainable growth. As a result, the Egyptian citizen has not felt any improvement in the standard of his living or any positive impact for this announced growth.

The Public Budget

The general budget, including the government expenditures and revenues, starts in Egypt with the beginning of the new fiscal year in July. The FY2019/2020 budget, described as the largest budget in the history of Egypt, was ratified by the Parliament in June 2019. Following is a reading in the budget's most important items:

A reading in the FY2019/2020 budget

Budget revenues for FY2019/2020 were estimated at LE 1134.4 billion, an increase of LE 145 billion over the previous fiscal year. Expenditures amounted to LE 1575 billion, an increase of LE 151 billion over the previous fiscal year. The increase in the minimum wage limit for civil servants on March 30, 2019 increased wage expenses by LE 30 billion.

The spending structure consists of major items that the government cannot avoid, such as the debt interest estimated at LE 569 billion; allocations for subsidies, grants and social benefits at LE 327 billion, wage allocations LE 301 billion pounds, and allocations for investment at about LE 211 billion.

Although the investment item has increased by LE 63 billion, most of these expenditures are directed towards infrastructure and government real estate, areas that lack the value added and do not contribute to creation of jobs in a sustainable manner, where the analytical statement of the FY2018/2019 budget showed that the largest figure in the investment item was spent on the fixed assets, about LE 192 billion. These assets consist of residential buildings worth LE 24 billion, non-residential buildings worth LE 33 billion, and constructions worth LE 76 billion, with a total of LE 133 billion for the real estate sector only, i.e. more than 50% of the investment allocations went to the rent-based real estate investment that lacks any real market value added.

Another important item under spending is the subsidy item, as petroleum and electricity subsidies declined by LE 36.1 billion and LE 12 billion, respectively, as a result of the government's agreement

with the International Monetary Fund (IMF), which means higher inflation, higher prices, higher production costs and likely negative impact on exports.

In addition, although the Egyptian Constitution (2014) stipulates that the Egyptian government is committed to allocate no less than 7% of the GDP for health care and education (in [Articles 18 and 19](#) respectively), the government has not abided by this constitutional provision for the fifth time in a row; and allocations for both health care and education in the FY2019/2020 budget reached LE 205 billion, about 3.6% of the GDP.

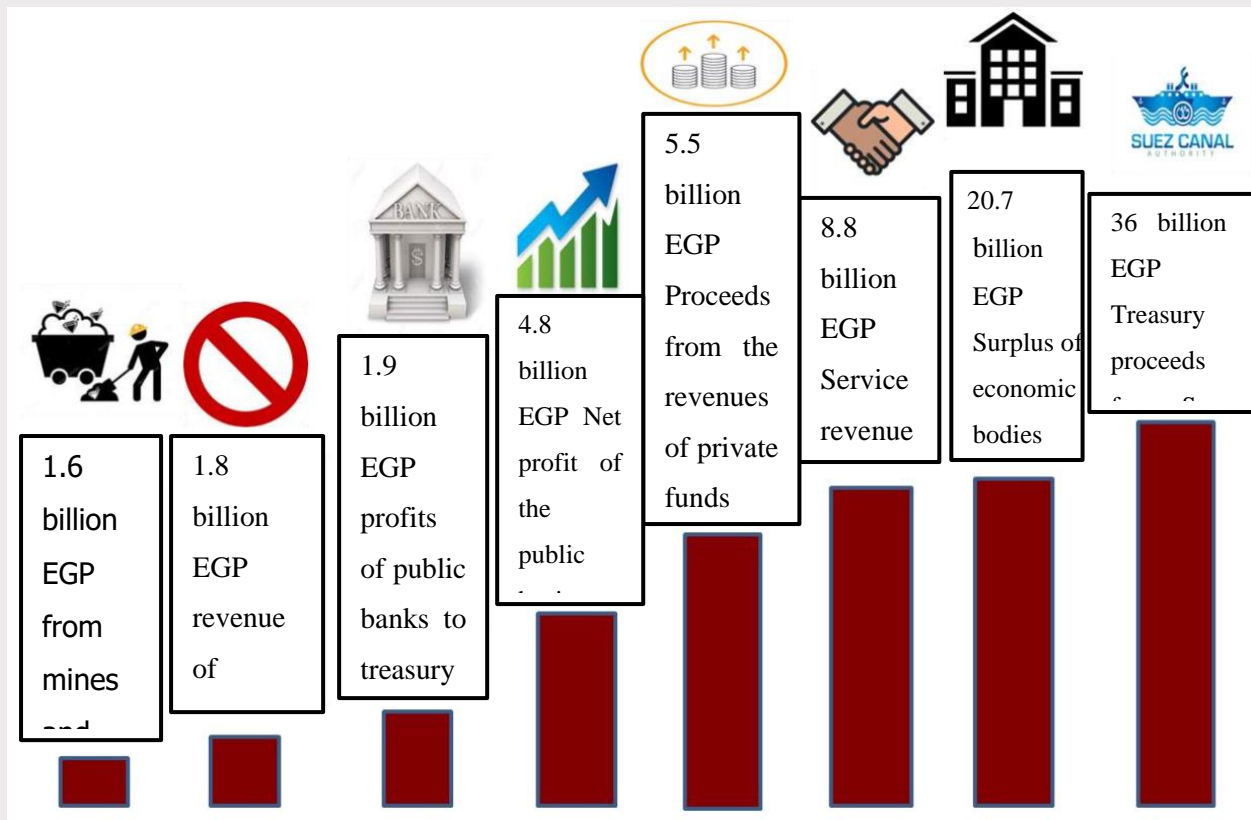
The structure of expenditures shows that there is no clear vision for a long-term development process. The government continues to seek cutting expenditure by removing subsidies and reducing the wage bill without directing spending on investment towards more productive sectors or towards creation of infrastructure that stimulates private sector investment, or even adhering to constitutional provisions for spending on human infrastructure, i.e. by spending on education and health.

On the revenue side, tax revenues account for 70% to 75% of the country's total public revenues. This high percentage raises a number of questions about the rest of the state's revenues which constitute only 25%; as reliance on taxes as a major source of revenues may lead to recession. Yet, there are still many possible adjustments that can control the revenue and expenditure sides in the public budget.

In addition, there are low figures entering the state budget from important institutions, as Figure (3) shows that the proceeds of the public treasury from the Suez Canal amount to only LE 36 billion (equivalent to about \$ 2.2 billion), therefore a question arises here: where did the rest of the Suez Canal revenues (amounting to more than \$ 5 billion in 2018) go?

Also, the revenues from mines and quarries entering the general budget amounted to only LE 1.6 billion, added to the estimated proceeds from special funds amounting to only LE 5.5 billion. Taking into account that these special funds should provide 25% of their proceeds (estimated at about LE 22 billion) to the state treasury, the questions that arise here are: Where did the rest of the proceeds go? How are they spent and who monitors this spending? Why is the state intransigent to increase the rate set in favor of the budget in light of the funding gap, and the burden of debt service?

Figure (3) the most important non-tax revenue items in the FY2019/2020 budget:



Source: Ministry of Finance

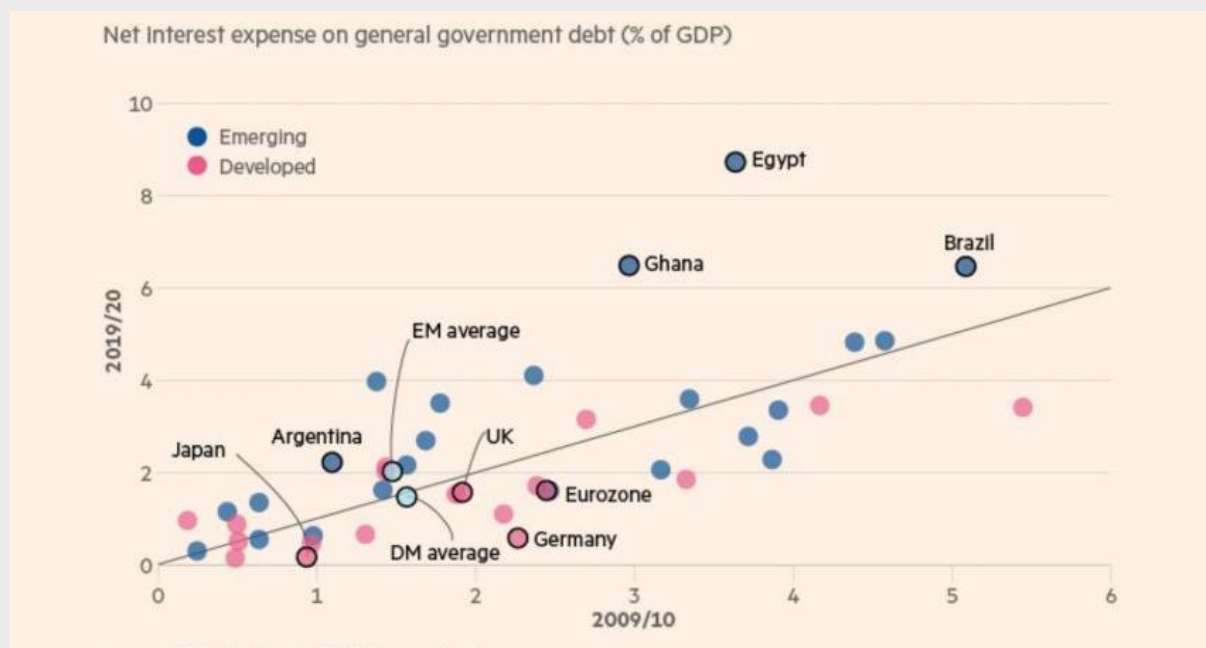
As a result of absence of a strategic vision aimed at changing the structure of the Egyptian economy, the government continues to rely on borrowing to finance the financing gap in the budget, which we will review in the following part:

Budget deficit

The need to provide funding sources is due to the fact that expenditures are higher than revenues, known as the budget deficit. The deficit in FY2019/2020 budget was estimated at LE 445 billion, 8.4% of GDP. In order to fill the gap, the government resorts to internal and external borrowing, thus increasing the debt burden which has amounted to LE 569 billion (devouring 50% of the total public revenues in the budget), which makes the budget deficit a chronic problem in the Egyptian case. The debt-to-GDP ratio is about 9% this year, compared to less than 4% 10 years ago, the highest rate in both emerging and developed markets (Figure 4). This means that the government always resorts to

borrowing in order to fill the financing gap and thus increases the bill of premiums and interest in the next fiscal year, which drives it to borrow again and so on. Figure (5) shows the evolution of the budget deficit from 2012 to 2020. Although the curve is in a declining form, the problem of financing by borrowing is still the policy adopted by the government.

Figure 4: Debt-to-GDP Ratio



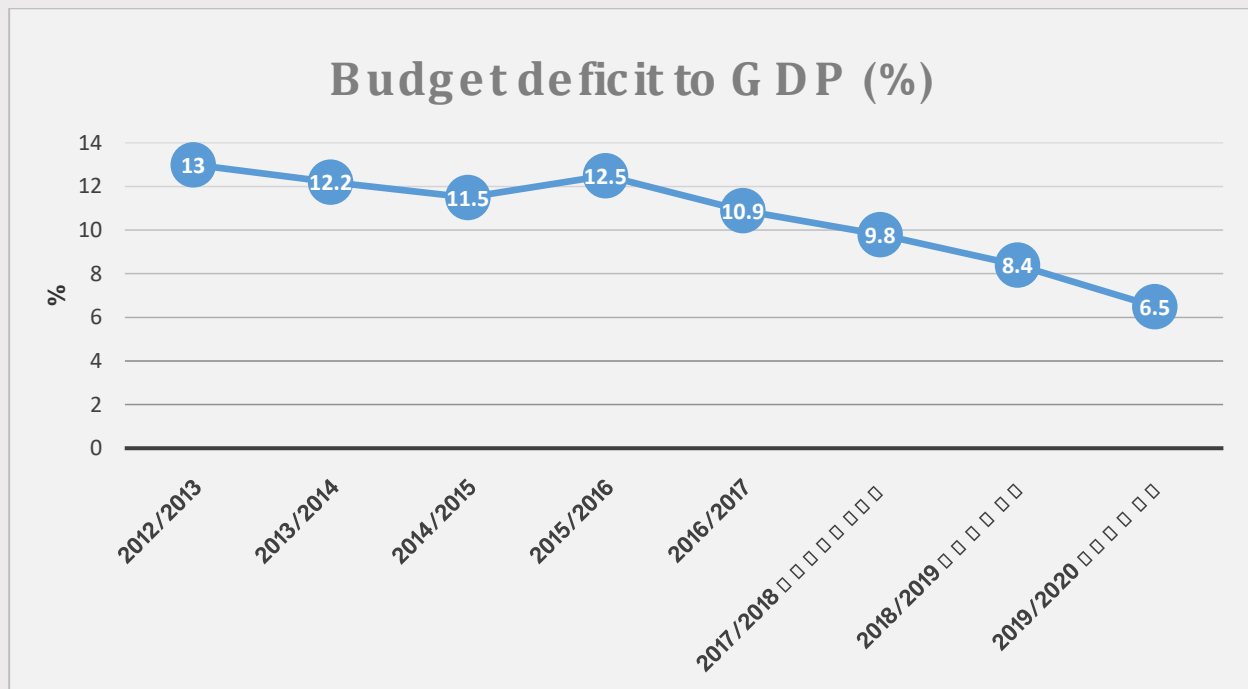
Source: [Financial Times](#)¹⁴

The problem of financing by borrowing does not only stop at increasing the deficit but it also affects private investment. The government borrows through the Central Bank of Egypt (CBE) which offers high-yield bonds and treasury bills to ensure sale. Domestic banks purchase these bonds for their higher and more secure financial return rather than financing private sector projects which is characterized by high risks in addition to the convergence of the expected return on bonds. Consequently, the government internal borrowing bill rises in terms of its commitment to repay debts

¹⁴ Steve Johnson, EM economies face high interest burden amid surging debt levels, Financial Times. 6 May 2019. Accessed 18/9/2019

and installments, in addition to discouraging the private sector to establish new projects (by reliance on borrowing from banks).

Figure 5:



There is also a serious increase in the rate of borrowing in absence of real investment returns for what has been spent during the past 5 years with no clear vision of how to restructure the economy, in addition to the government's weak control over the executive and security apparatuses that exercise guardianship on state expenditures and imports in the form of financial intermediaries amid Lack of parliamentary and popular oversight. Together, all these factors exacerbate the deficit problem and make it more difficult to solve over time. This brings us to talking about the debt file in Egypt:

It is clear from the above presentation that the interest on loans, which constitutes about 50% of total budget revenues, and approaches about 40% of total expenditures, swallows any likely attempt to increase government investments in health, education and infrastructure. This has led to a chronic budget deficit, prompting the government to increase taxes, reduce subsidies, borrowing, and printing

too much money to fill the gap, which directly affects the poor and middle classes who are already paying the cost of the current economic policies without feeling any kind of improvement.

Monetary policy

Monetary policy is the policy adopted by the monetary authority of a country (in Egypt, the Central Bank of Egypt - CBE) to control interest rates and inflation to ensure price stability of goods and products and general trust in the currency. However, the policy that the CBE has adopted has resulted in the following:

First: Increasing the exchange reserves:

The CBE monetary policy adopted during the last phase contributed to increasing the CBE foreign exchange reserves to exceed \$ 44.274 billion by the end of [May 2019](#), compared to \$ 44.218 billion at the end of April 2019, an increase of \$ 57 million, covering about 8 months with respect to commodity imports which cost around \$ 55 billion.

¹⁵Second: The decline in the inflation rate:

Inflation had witnessed successive increases following the exchange rate liberalization in November 2016 until September 2017, for almost a year, reaching 31.7% in February 2017, 34.2% in July 2017. Then, it began to decline, dropping to 11.1 in December 2018 against 22.3% in December [2017](#)¹⁶. The annual inflation rate in May 2019 was 13.2% against 11.5% in May 2018¹⁷.

Third: the inflow of investments in domestic debt funds (hot money):

The CBE decision to liberalize the local currency exchange rate in November 2016, where the Egyptian pound lost nearly half its value, has helped revive foreign inflows on bonds and treasury bills (to earn short-term profits on interest rate differences). These foreign inflows reached its peak at the end of

¹⁵ Ahmed Yaqoub, CBE: Egypt's foreign reserves rise to \$ 44.27 billion at the end of May 2019, Youm7, 3 June 2019

¹⁶ Heba Hosam, After two years of flotation .. What about inflation? And how it turned to decline over 24 months, Youm7, 8 Nov. 2018.

¹⁷ Amin Saleh, Important figures about inflation rate in Egypt, Youm7, 12 June 2019.

March 2018, about \$ 23.1 billion; then they declined to \$ 17.5 billion at the end of [June 2018](#)¹⁸. Then, foreign investment in government debt instruments rose again to \$ 16.8 billion early [May 2019](#)¹⁹.

This policy negatively affected two important issues: (domestic and foreign) debts and investment. The inflation rates that the government is talking about will be discussed in the coming part.

Domestic debt

The [domestic debt](#)²⁰ rose to LE 4.1 trillion in 2019, by 95% of GDP. The government must also pay off debt interest periodically with a total of LE 596 billion in the FY2019/2020 budget, in addition to debt installments due on the CBE, amounting to LE 375 billion in the same fiscal year.

The domestic debt is dangerous for the following reasons:

- 1- It is difficult for the countries with high domestic debt to access global financial markets on a short-term basis, which may cause real problems for debt sustainability at the medium-term level.
- 2- The high domestic debt leads the state to either to declare inability to repay the debt (default on repayment of debt installments) or its economy becomes an inflationary economy. The state's inability to pay leads to a critical economic crisis, as happened in Greece, which could lead to bankruptcy. On the other hand, inflation may reduce the real cost of domestic debt, as the state can pay off its debts with the real value of the pound. However, interest rates of future bonds and treasury bills offered by the government will have to be raised in order to find favor with creditors, which means that debt service will rise again in the medium and long term.
- 3- High domestic debt raises the cost of credit on productive sectors in the private sector and would thus lead to lower rates of private investment.

¹⁸ Escape of 'hot money' worries Egyptian government, \$5 billion came out of Egypt since last May, Alarabiya.net, 29 Aug. 2018

¹⁹ Ahmed Yaqoub, Ministry of Finance: \$ 16.8 billion foreign investments in Egyptian debt instruments, Youm7, 7 May 2019.

²⁰ Egyptian government debt surges in 2018, [Reuters](#), 21 May 2019

4- The largest cost of public debt in Egypt is related to the structure of public expenditure that goes to finance it, where the total interest and installments, amounting to LE 971 billion without any other public expenses, reached 86% of the expected state revenues (about LE 1 trillion and 134 billions) in the FY2019/2020 budget. This means that the government uses savings to finance its current expenditures rather than investment. Therefore, these expenditures do not generate a return, and do not contribute to increasing the future capacity of economy to produce or create jobs; and they even lead to crowding productive sectors willing to invest by raising interest rates and providing less dangerous lending opportunities to the banking system.

5- The high domestic debt may lead to the accumulation of debts, known as “debt overhang”, where the size of domestic debt accumulates to the extent that it becomes difficult for the state to borrow, even if the debt will be directed to real investment projects.

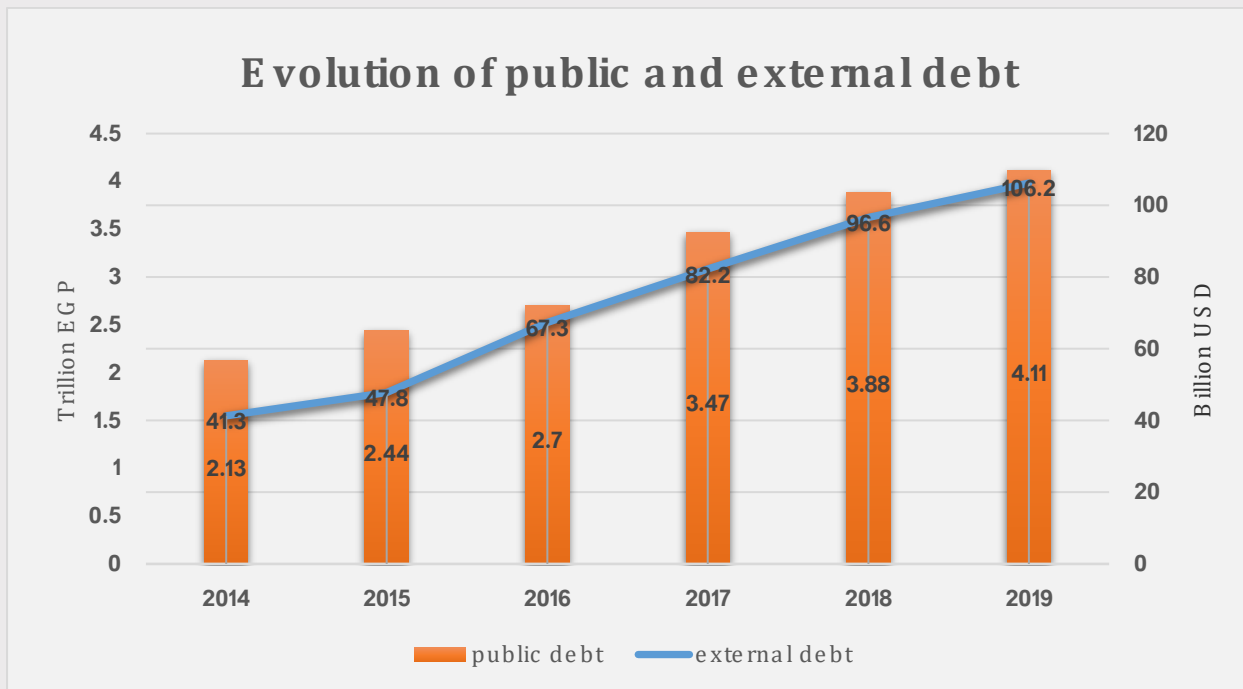
External debt

The CBE revealed on 26 August 2019 that the [external debt](#)²¹ rose to \$ 106.2 billion by the end of March 2019, with a rise of about \$10 billion from last December, where it was \$ 96.612 billion, an increase of 9.9%. Figure (6) shows increases in the external debt since 2014 that have reached unprecedented levels. It is noteworthy that the amount of debt accumulated since the military coup of July 2013, amounting to about \$ 60 billion over a period of only five years, exceeded the amount of debt that successive Egyptian governments have carried out for three decades.

Despite controversy over the security limit for borrowing from abroad, where some said the external debt should not exceed 60% of GDP, the ratio of external debt to GDP in Egypt reached about 37%. On the other hand, some argue it counts on what is known as sustainability of debt and the state’s ability to repay premiums and interest without the need to restructure its debt. Apart from these points of view, what is important here is how far the government benefits from borrowing in favor of the development process, which is missing in the Egyptian case.

Figure 6:

²¹ CBE: External debt rises to \$106.2 billion March 2019. Anadolu Agency, Accessed on 2/9/2019.



Source: The Central Bank of Egypt

Although the borrowing came under the slogan of financing development, the loans were spent on projects that do not benefit the development process, mostly for political objectives in absence of any economic feasibility or for the benefit of sovereign apparatuses (security services). In the last six years, foreign deposits worth \$ 18 billion, about \$ 50 billion in foreign loans, as well as huge Gulf cash and petroleum aid, poured into Egypt, which would have brought about a real development renaissance; but, unfortunately, all these loans and aid were completely spent pending repayment.

Resorting to the borrowing solution is not new to the Egyptian regime; but while the government had been previously interested in borrowing from local banks in local currency, considered less risky, it has recently started to expand borrowing from abroad in foreign currency, which led to an increase in the ratio of external debt to the total public debt. This new trend makes the burden of these external debts vulnerable to any negative change in the prices of Egyptian currency, and threatens the ability of the country to tolerate the debt burden, as reported by [Moody's](#)²² in a recent statement

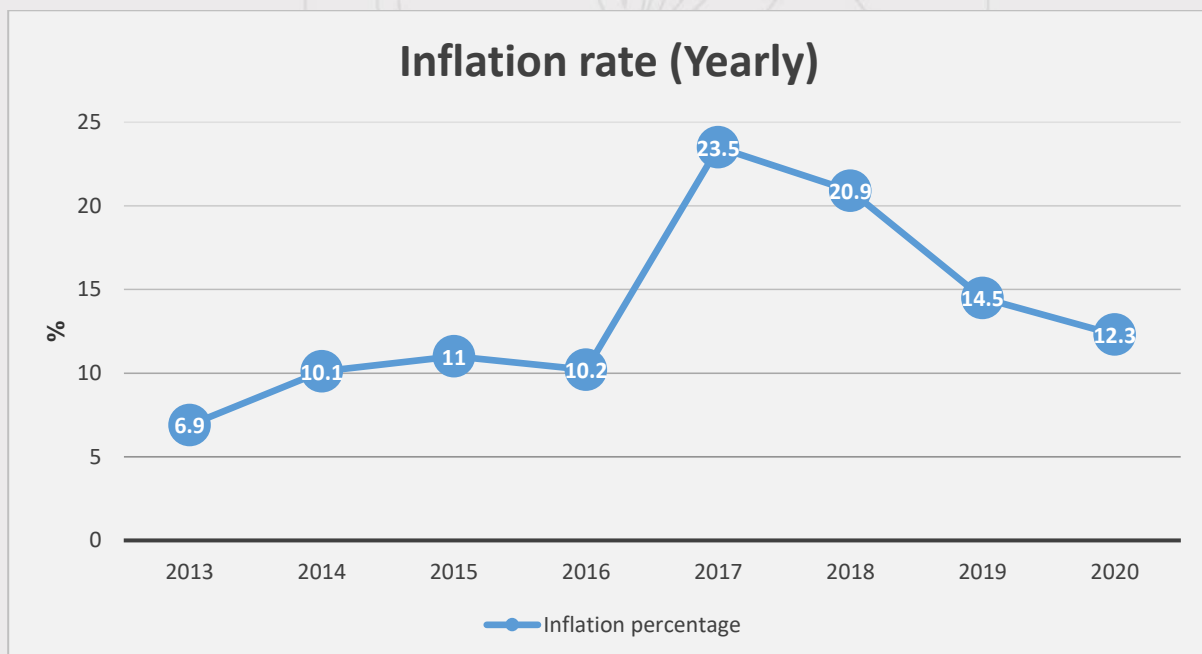
²² [Moody's](#) - Egypt's credit profile reflects very large government financing needs. 29 August 2019

that reviewed the credit situation of Egypt, which concluded that it reflects the government's weak debt affordability, with the external debt projected to reach \$ 115.7 billion by the end of 2020, which could pose a risk in the future. More seriously, most of these debts do not go to government investment or development projects, but are mainly used to cover the budget deficit, especially wages and salaries, which means that these debts do not contribute to the development process or increase growth rates, a situation that further weakens the government's debt affordability in the future. At the same time, the debt increase comes at a time when the government is adopting austerity fiscal policies. Instead of leading to reducing government spending and the budget deficit, and accordingly reducing the debt rate due to these austerity measures, the debt rate is escalating in Egypt!

Inflation

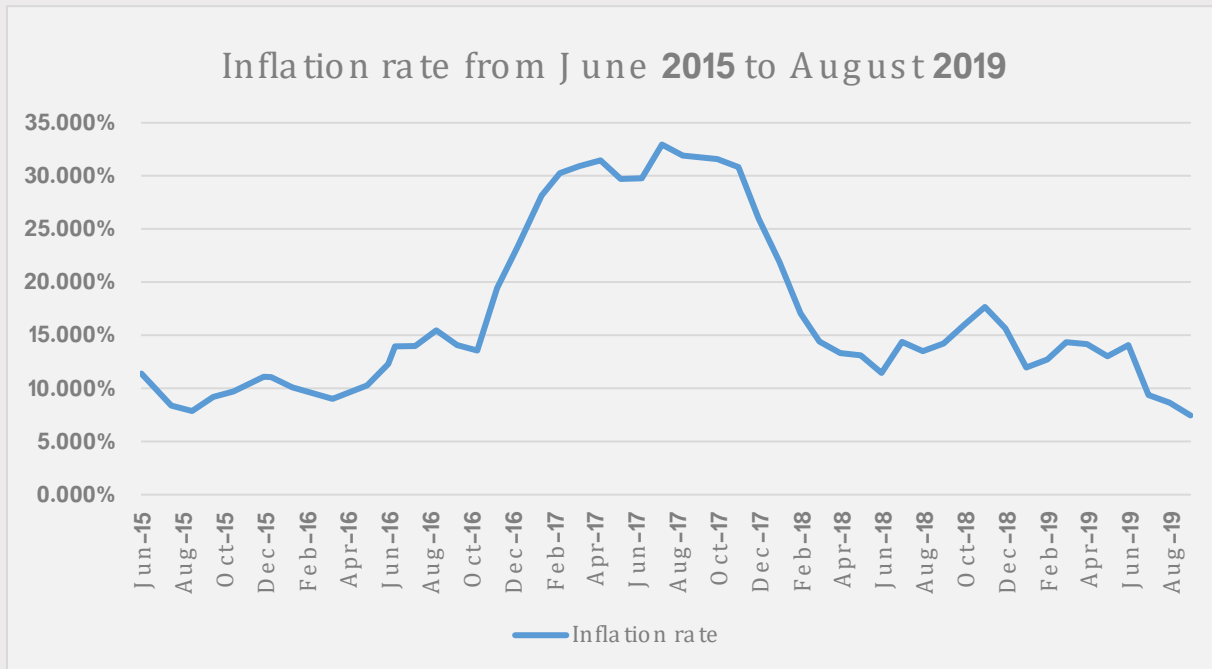
Figure (7) and (8) indicate the evolution of annual and monthly inflation rates in Egypt during the period from June 2017 to June 2019.

Figure 7:



Source: International Monetary Fund²³

Figure



Source: The Central Bank of Egypt²⁴

Much of the rise in inflation is due to the decision to float the Egyptian pound and the subsequent economic measures. Figure (8) shows the monthly inflation rates from June 2015 to August 2019, where the inflation rate rose to a peak of 34.2% in June 2017, against 24.3% in December 2016. Subsequently, the inflation rate dropped to 13% in June 2018. Inflation rose again to 17.5% in Oct. 2018, then fell to almost 7.46% in August 2019 at the time of preparing this report. It is possible to understand the decline in inflation rates, especially after removal of subsidies on hydrocarbons last July and the weak demand in the Egyptian market due to weak purchasing power of citizens, which led traders and producers not to raise the cost of increase on the citizen and bear that cost, in light of the decline in demand with the availability of supply.

²³ 2019 and 2020 data are predictable data

²⁴ The Central Bank of Egypt, Statistical Bulletin 268.

We can also understand this decline in light of the fact that the issue is relative compared to extremely high inflation in 2017. It is worth noting that the annual inflation rate is the ratio between the current and previous year prices; for example, inflation reached 34.2% in July 2017, then it dropped to 17.55% in October 2017, compared to the previous year, which does not mean, for example, that prices have fallen to the level before the start of the IMF program. Therefore, in order to calculate the inflation rate in Egypt during the years from 2012 until now, inflationary differences between those years must be calculated, which shows that the total inflation rates in Egypt have exceeded 150% over the last six years.

Many factors have led to increasing inflation rates during the last period, including:

1- Printing too much money to finance the state budget deficit, a conduct that the [CBE Governor](#)²⁵ in May 2018 said the government stopped relying on.

2- Flotation of the Egyptian pound, a decision that contributed significantly to raising inflation. Although the decision to float the local currency was necessary to put an end to the black market and as a prerequisite for the completion of the IMF agreement, however, the impact of the pound flotation on inflation exceeded expectations. Although the IMF predicted that the pound floatation, the introduction of value-added and the removal of energy subsidies could raise inflation to a maximum of 18% in [2016/17](#)²⁶, however, the results exceeded expectations and the inflation rate reached 34.2% in July 2017.

3- Removal of subsidies on hydrocarbons and electricity: According to the IMF agreement, the government has restructured the hydrocarbons and electricity prices, which consequently affected the prices of final products, especially those that include hydrocarbons in their production requirements, or through increasing transportation cost of production requirements or the final product. It is noteworthy that the draft FY2019/2020 budget comes after the government approved raising electricity prices for the fifth time since 2014.

²⁵ CBE Governor: We used to print too much money but we have stopped, Masrawy, 8 May 2018.

²⁶ IMF, "IMF country Report No. 17/17. Arab Republic of Egypt" Jan 2017.

4- Introduction of VAT: By the end of August 2016, the government approved the introduction of the value added tax (VAT). According to the Minister of Finance, the application of the tax would increase [inflation rates](#)²⁷ only once by from 2.3% to 2.6%. The impact of VAT on the proceeds of the tax revenue was huge: A quick review of tax revenues in the general budget indicates that tax revenues increased from LE 352 billion in FY2015/2016 to LE856 billion in the draft FY2019/2020 budget (approximately 243%).

5- Increase of customs rates three times in a row: The increase of customs more than once contributed to raising inflation rates, where Decree No. 419 of 2018 increased the tariff (fees) on hundreds of food commodities, infant milk, electrical appliances, machinery and equipment, by 40%²⁸ for the third time in a row. The average tariffs on a wide range of imports were raised after a severe currency crisis experienced by Egypt in 2013, and then again in January 2016, although Egypt changes the customs tariff every five years. As a result, the customs revenues that entered into the state budget increased from LE 17.7 billion in FY2013/2014 to LE 34.3 billion in FY2016/17 and is estimated in the current year's budget by about LE 45.3 billion, to reach LE 51.7 billion, as a target revenue in the FY2019/2020 budget. This rise is due to the increased reliance on import of essential commodities which [exceeded](#) \$ 60 billion by the end of 2018²⁹, where costs are borne by the end consumer, which contributed to the rise in inflation rate.

6- Raising the public transport fees: Raising the fees of various means of public transport contributed to further raising the inflation rates. The rise of public transport fees included buses, the underground (Metro), and railway trains.

There is no doubt that the increase in the prices of government public transport tickets led to the high prices of transportation of various types, under the pretext of the high prices of hydrocarbons and others. Also, raising fees of the use of new roads and bridges contributed to the exacerbation of these prices, in addition to the fees of using roads and tunnels controlled by the army, which are

²⁷ The Value Added Tax increases suffering of Egyptian people, Al Arab, 3 Oct. 2016

²⁸ Official Gazette, No. 36bis (a) dated 9 September 2018

²⁹ Egypt's exports jump 19% to \$ 26 billion in October 2018, Alarabiya, 26 Oct. 2018.

subject to the estimation of officers, which opens doors widely for exploitation of citizens, which is ultimately borne by the end consumer in the form of high inflation.

Of course, all these decisions, decrees, and laws fueled inflation rates, that were not matched by any increase in wages, except for the recent rise in the minimum wage limits that cannot in anyway cover the applied price rises, which contributed to adding new categories of Egyptians to those under the poverty line.

Investment

Economists agree on the importance and role of investment in the development process because it is one of the main components for the calculation of GDP, including the total consumption, investments, government spending, government investment and the difference between exports and imports. Public investment carried out by the government is listed under 'government investment' while investments consist of domestic private investment and foreign direct investment.

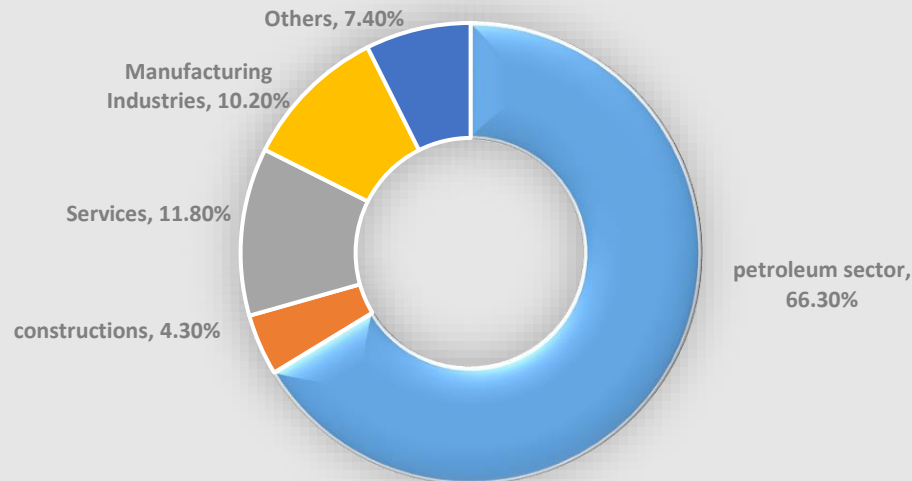
In this part, we will review the structure of foreign and private investment in Egypt:

Foreign direct investment

Foreign direct investment (FDI) in Egypt is one of the most important sources of foreign currency in the country. Attracting more foreign investment over the past two years has been a major concern, as part of the economic reform measures that the government is carrying out in agreement with the IMF, most notably, the liberalization of the exchange rate in November 2016 and the sharp decline in the Egyptian pound that was supposed to attract investment, as well as ending the foreign currency shortage. In addition, the government issued a new investment law, a law to facilitate the acquisition of industrial licenses, and a law for bankruptcy. The government also amended the law of companies, developed the investor service centers in order to attract foreign and domestic investments, and issued a map of investment opportunities in Egypt.

Figure 9:

Structure of foreign investment in Egypt



Source: The Central Bank of Egypt

Foreign investment contributes to the development process, provided that it is an added value to the economy. Economic growth results from a combination of many elements, including, labor efficiency, capital flows and technological development. Many studies have indicated that foreign investment is important to economy, provided that it is an added factor to both technological development and capital flows. Some researchers, such as [Borensztein](#)³⁰ and others, suggest that FDI is an important vehicle for the transfer of technology, contributing relatively more to growth than domestic investment. In addition, the study prepared by Borensztein states that “the higher productivity of FDI holds only when the host country has a minimum threshold stock of human capital”. Good results can only be achieved if there is a human capital in the host country that is trained to uptake the incoming technologies. “FDI contributes to economic growth only when a sufficient absorptive capability of the advanced technologies is available in the host economy,” Borensztein states in his study.

³⁰ E Borensztein, J De Gregorio, and J-w Lee, “How Does Foreign Direct Investment Affect Economic” 45 (1998): 115–35.

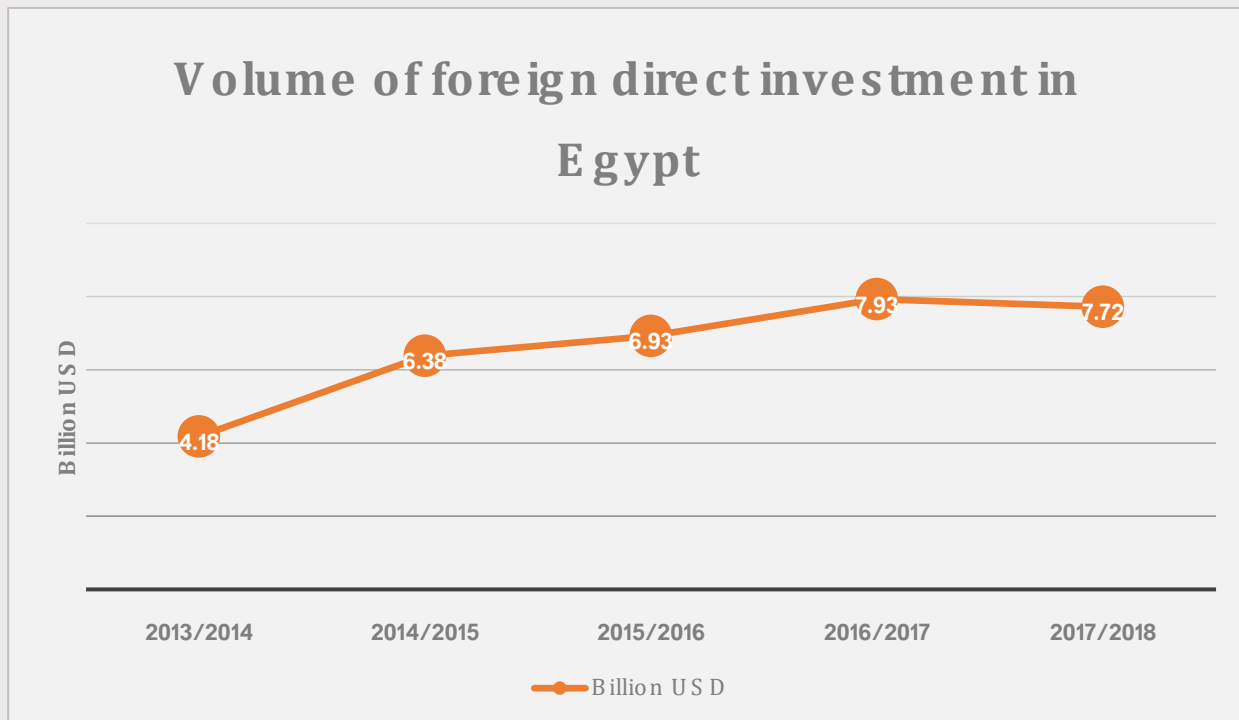
Figure (9) shows the structure of foreign investment in Egypt. The petroleum sector accounts for the vast majority of investments, a sector that is rentier and does not contribute to the transfer of new technology to the labor market in addition to being a capital-intensive sector that does not provide jobs commensurate with what is spent on its investments; the second element is that the benefit of foreign partner is high; and the third point is that Egypt has not benefited from these investments over the past decades in localization of the technology of this sector, or producing the investment requirements with respect to technology, although Egypt has the resources and human cadres that are able to accomplish this task successfully, as evidenced by the large presence of [Egyptians](#) in the petroleum sector in Gulf countries and international petroleum companies³¹. The oil sector is followed by the services sector by 11.8%, the industrial sector by 10.2%, the construction sector by 4.3%, and the agriculture sector by 0.1%³². It is clear from this distribution that very little foreign investment is directed towards productive activities that generate real growth and job opportunities to reduce unemployment levels.

Figure (10) shows the total foreign investments in Egypt since 2013/2014. It is clear from the figure that the largest figure obtained by Egypt was in FY2016/17 by 7.93 billion dollars, which is very meager, especially since it is not directed to productive sectors as we mentioned above.

Figure 10:

³¹ Abdelhafez Alsawi, Egyptian Economy: Declining Not Recovering, EIS, 12 June 2019.

³² The Central Bank of Egypt, Economic Journal, Volume 58, Issue 3 (July - March 2017/2018), p. 64.



The decline in net foreign direct investment (FDI) is mainly due to the lack of an overall investment climate. The overall climate refers to several levels, including the economic, legislative, political and institutional levels.

- At the economic level, the continued high interest rates negatively affects the attraction of real investments, the decline in the volume of demand in the Egyptian market after the economic reform measures that affected the purchasing power of citizens, the weak promotion of efforts exerted by the state during the recent period, the impact of developments in emerging markets, and the steady increase in military and intelligence economic activities.

- At the legislative level, the government has attempted to develop investment laws, which was reflected positively in Egypt's ranking in World Bank's 2019 'Ease of Doing Business' report, where it jumped 8 spots to rank 120th out of 190 countries in 2018, although it is still behind. However, legislative reform is far from being an overall reform of the legislative structure where the government adopts a special correction path for each piece of law separately by identifying a specific set of economic activities that the state seeks to stimulate, and granting investors a specific set of benefits,

incentives, guarantees and exemptions that distinguish them from other projects operating under the general legal framework of the country.

The incentive strategy is an effective means if the result is attraction of a large volume of foreign investments to compensate for the loss of incentives. Conversely, the failure of this strategy leads to the loss of opportunity for new revenues on the state budget in addition to the negative effects that may harm competition with the domestic product. In a study by [Nada Masoud](#) (2003)³³, the researcher addressed the impact of this strategy on the Egyptian case. The study concluded that this strategy did not have any obvious impact on attracting foreign investments, but on the contrary, it placed the budget burden on taxpayers without benefiting from foreign investments. The study stated that the policy on FDI in Egypt should have focused on deriving macroeconomic benefits from FDI rather than on attracting the FDI. These policies have not changed since the time of the study under the era of former President Hosni Mubarak, as there has been no significant improvement in this regard.

In Egypt, the focus has been on the wrong question of how to attract foreign investment, not on how to employ foreign investment in the development process. Egypt tried to offer incentives to attract foreign investment and not to create the general climate proper for investment, including raising the efficiency of education or manpower, or establishment of solid and competitive legal institutions and legislation. Creation of the proper legislative environment is what attracts foreign investment, not what the government is currently trying to do by only offering incentives to attract foreign investment.

- At the institutional level, the World Economic Forum's latest Global [Competitiveness Report 2018](#)³⁴ (where Egypt scored 53.59 points out of 100) stated that the main problems facing investors in Egypt are policy instability (15.2% of participants), inflation (14.2%), corruption (9.8%), bureaucracy (9%) and inefficiency of the workforce (7.9% of participants). Competitiveness Index in Egypt averaged 12.10 Points from 2007 until 2018, reaching an all time high of 53.59 Points in 2018 and a record low of 3.60 Points in 2015.

³³ Nada Massoud, "Assessment of FDI Incentives in Egypt Nada Massoud Working Paper 0336" 336 (2003): 22.

³⁴ weforum, 2018. Arab World Competitiveness Report, s.l.: World Economic Forum.

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At the political level, the army's intervention in the economic process is one of the most important factors that negatively affect attraction of investments, as some investors have stated that a major aspect of their concern about entering the Egyptian market is the army's competition with the private sector in the economic process (Momani, 2018)³⁵. (The report will discuss the military incursion into the economic process in a separate part later.)

In addition to those internal levels, some reports from investment banks indicated that the decline in direct foreign investments is not a local phenomenon. In the first half of 2018, the global DFI fell by 41% to reach \$ 470 billion, according to the report of the Trade and Development Board Of the United Nations (UNCTAD)³⁶. Global investment has declined due to complicated factors including trade war fears and, most importantly, tax reforms implemented in the United States since the beginning of 2018, which have encouraged more companies to resettle their business and return capital to the U.S., a country with huge investments around the world³⁷.

On the other hand, the influx of foreign investment in Egypt tends largely to debt instruments such as bonds and treasury bills. On the other hand, the influx of foreign investment in Egypt tends largely to debt instruments such as bonds and treasury bills. The CBE decision to liberalize the local currency exchange rate in November 2016, where the Egyptian pound lost nearly half its value, has helped revive foreign inflows on bonds and treasury bills (to earn short-term profits on interest rate differences). These foreign flows reached its peak at the end of March 2018, about \$ 23.1 billion; then they declined to \$ 17.5 billion at the end of June 2018³⁸. Then, foreign investment in government debt instruments rose again to \$ 16.8 billion early May 2019³⁹.

³⁵ Momani, B., 2018. Egypt's IMF Program: Assessing the Political Economy Challenges, Doha: BROOKINGS DOHA CENTER

³⁶ After a decline of 40% in Egypt .. Report: FDI decline is a global phenomenon, 16 Jan. 2019

³⁷ Ibid.

³⁸ Escape of 'hot money' worries Egyptian government, \$5 billion came out of Egypt since last May, Alarabiya.net, 29 Aug. 2018

³⁹ Ahmed Yaqoub, Ministry of Finance: \$ 16.8 billion foreign investments in Egyptian debt instruments, Youm7, 7 May 2019.

This investment is an addition to the external debt items and does not reflect a real investment; and with view to the volume of investment in hot money in 2018, we find that it reached three times more than the total foreign investment, which reflects investors' lack of trust in the Egyptian market where investment in hot money is characterized by fast market volatility and investors' ability to quickly withdraw funds, which reflects a lack of confidence in the local market.

Private investment

The overall economic situation in Egypt, especially after the CBE decision to float the Egyptian local currency, the removal of subsidies on hydrocarbons and electricity, and the military's encroachment on economic activity amid its various unique advantages and legal exemptions, have been painful blows to the Egyptian private sector. There is plenty of evidence that private sector activity is constrained by a burdensome business environment, restricted trade and, therefore, the sector has not fulfilled its role, although the regime claims that it adopts a liberal economic approach, where the private sector should have been its main pillar.

The fall in the Emirates National Bank of Dubai (NBD) Purchasing Managers' Index (PMI), which measures private sector' non-oil-producing activity in Egypt, indicates that the private sector activity in Egypt during the post-flotation period has steadily declined, although it improved in a few months, but soon declined again below 49.4, thus falling below 50, which is the boundary between [growth and contraction](#)⁴⁰.

Figure 11 shows the rates of public and private investment from 2002 to 2018, which are characterized by low rates, partly due to the global crisis in the wake of 2008 and the subsequent political events in 2011 and 2013.

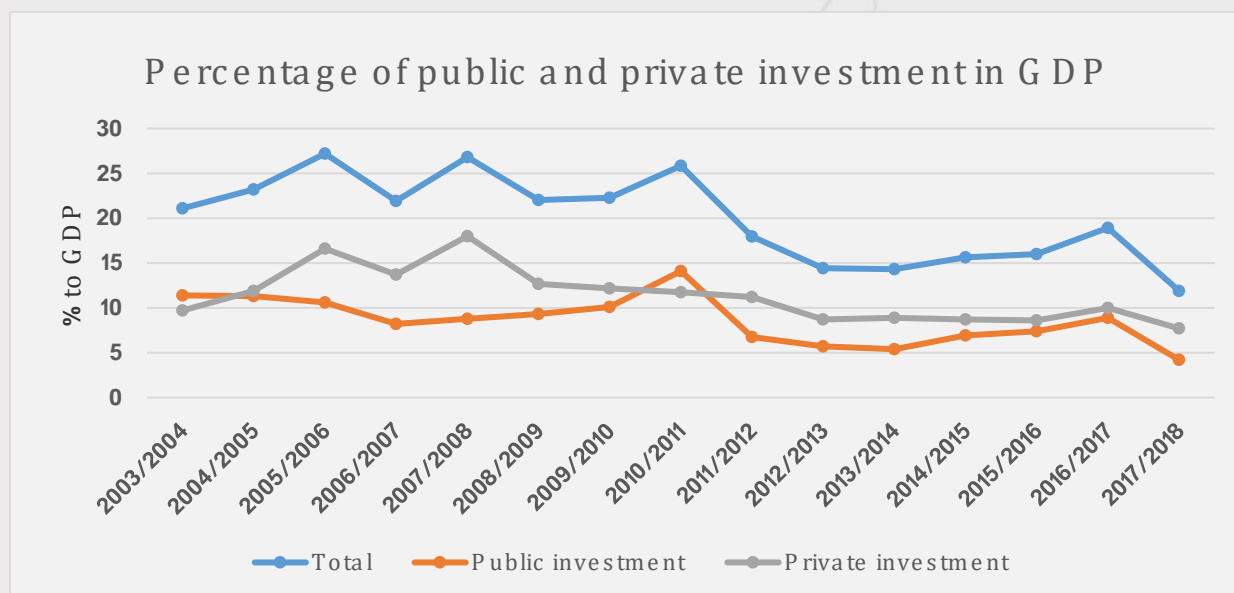
In addition, the state's competition with the private sector on getting bank deposits has led to lower rates of private investment financing, which has led, together with the high inflation rate, to raising domestic interest rates. This has been a significant constraint of funding; and it is sufficient to know

⁴⁰ IHS "IHS Markit Egypt PMI", August 2019. Link. Accessed 9/9/2019

that the private and household sectors accounted for only 23% and 8% respectively of the total financing of the banking sector in last fiscal year, while the public sector accounted for 69%.

The private sector also suffers from the challenges faced by foreign direct investment mentioned in the above part, where private sector activity is still hampered by a cumbersome and unpredictable regulatory framework, and it is difficult to access key market factors (land-controlled by the military or skilled labor) and non-tariff barriers to trade.

Figure 11:



Source: The Central Bank of Egypt⁴¹

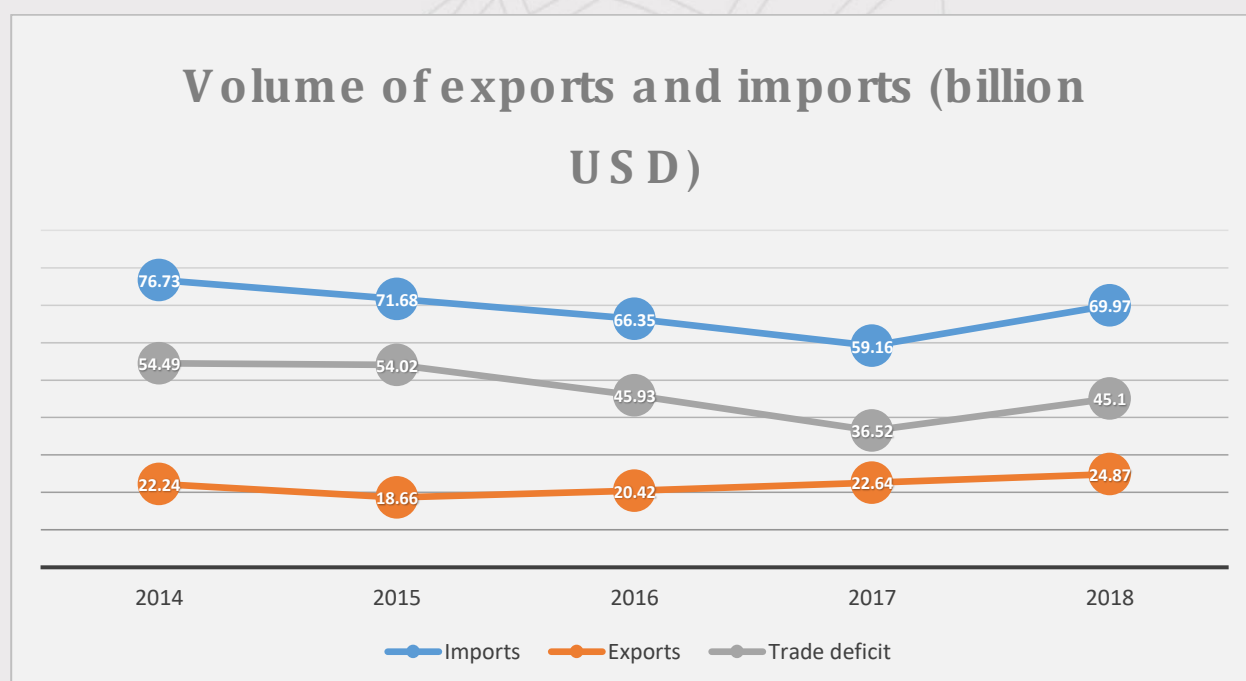
Overall, investment rates in Egypt remain modest and do not produce positive results on global competitiveness levels or on the ability to absorb new labor on an annual basis. The private sector, the middle class and the poor bear the burden of the IMF program, and will likely remain under pressure, especially after the recent hike in fuel prices, which means that conditions will remain difficult for private sector companies.

⁴¹ Public investment refers to the total investment in the government sector, public companies and economic bodies.

Development of exports and imports

Increasing exports and reducing imports has been one of the cornerstones of the IMF program. As the program reaches its final stage, data indicate that the situation before implementation of the program is almost continuing, as illustrated by Figure 12, which indicates evolution of the movement of exports and imports in Egypt from 2014 to 2018. Egypt's exports reached \$ 24.8 billion in 2018 against \$ 22.6 billion in 2017, an increase of 11.6%; and \$ 20.4 billion in 2016. Egyptian imports reached \$ 69.9 billion by the end of 2018 against \$ 59.1 billion in 2017, an increase of more than 15%, about 10 million dollars.

Figure 12:



The large gap between Egypt's merchandise exports and imports is one of the chronic problems of the Egyptian economy. It seems that there are no likely policies to bridge this gap, even in the medium term. According to the balance of payments figures for 2018, the trade deficit was around \$ 45 billion against \$ 37 billion in 2017⁴². In addition, oil exports represented 33.7% of the total merchandise

⁴² According to the data of Figure 12

exports. Oil merchandise exports do not represent a net revenue for the Egyptian state, but include the share of the foreign partner which amounts to about 40% of Egyptian [oil exports](#)⁴³. In light of the actions of the economic administration in Egypt, we find that the use of limited financial resources is mistakenly channeled into unnecessary and unproductive projects, which means that Egypt will continue to depend on importing food, tools, machinery and means of transportation as well as technology from abroad, deepening the production gap in Egypt over the [short and medium](#) term⁴⁴.

Overall, investment rates in Egypt remain modest and do not produce positive results on global competitiveness levels or on the ability to absorb new labor on an annual basis. The private sector, the middle class and the poor bear the burden of the IMF program, and will likely remain under pressure, especially after the recent hike in fuel prices, which means that conditions will remain difficult for private sector companies. A rising trade deficit is likely to put considerable pressures on the local currency in the future, which could result in another devaluation of the Egyptian pound.

Social effects of economic policies

As the citizen is the main focus of the development process, we should always consider the social consequences of economic policies, such as poverty rates and unemployment rates, in order to judge the success or failure of these policies, which this report will review in the following part:

Poverty

Indicators of poverty and unemployment are the real reflection that must be considered to assess the process of economic development and to decide whether the positive results at the macroeconomic level, if true, have led to real results on the standard of living of the citizen. In the latest statistics released by the Central Agency for Public Mobilization and Statistics (CAPMAS) in July 2019, the percentage of the poor in Egypt rose to 32.5% against 28% in CAPMAS 2015 report. This means that one third of Egyptians fall below the poverty line by adding more than five million citizens in only three years.

⁴³ Abdelhafez Alsawi, Egyptian Economy: Declining Not Recovering, EIS, 12 June 2019.

⁴⁴ Ibid.

According to the Egyptian official poverty line definition, the poverty line per capita in the FY2017/2018 was about LE 8827 annually (approximately \$ 533), LE 736 per month, while the extreme poverty line in the same period reached LE 5890 annually, LE 491 per month. Poverty, according to the latest research of income and expenditure in 2015, is LE 482 per capita monthly. While household annual income rose to LE 58.9 thousand (about \$ 3,550) from LE 44.2 thousand in 2015 (about \$ 5,357 dollars), the reality is that income fell 20% when adjusted for inflation, according to [Bloomberg](#)⁴⁵ and actually decreased when denominated in dollars.

It is also important to note that the data announced by CAPMAS refer to estimates of poverty in FY2017/2018, which means not taking into account the increase in fuel prices twice, adopting an automatic pricing mechanism of gasoline, raising the prices of electricity and natural gas of homes, raising the transportation fees, raising the price of butane gas cylinders and others; which means that this percentage does not reflect the current reality. In fact, many of those who were vulnerable to poverty have already fallen below its line, and the measures to raise the minimum wage limit mentioned above is only an attempt to stabilize some segments in their current state.

In addition, the issue of determining the poverty line is characterized by problems that challenge the credibility of official data. In its latest data, CAPMAS has set the poverty line at LE 735.5 per month, which is equivalent to about \$ 44.5 per month, and about \$ 1.5 per day, compared to about \$ 1.9 per day that is set by the World Bank as poverty threshold (a threshold that was also adopted by CAPMAS in 2015 figures), which means that the real poverty rate is much higher than what was announced, and that the increase in the number of the poor in three years since 2015 may even exceed five million, taking into account that the government calculates prices of all goods and services at the global prices.

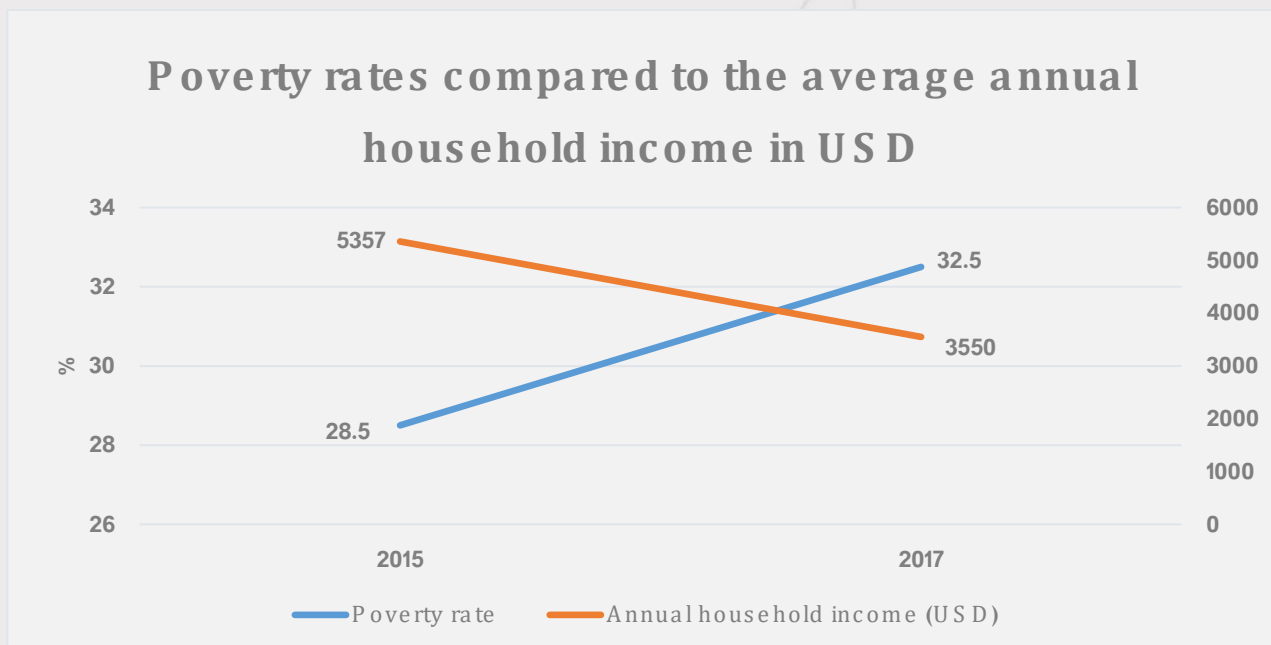
The report pointed to the improvement of the extreme poverty line set by CAPMAS to become about LE 491 per month (about 28.5 dollars), equivalent to 95 cents per day, compared to LE 482 per month in 2015; this move to the extreme poverty line by 9 pounds, between 2015 and 2018, cannot be

⁴⁵ Abeer Abu Omar and Paul Wallace, "Poverty Keeps Getting Worse in the Middle East's Fastest-Growing Economy" August 2019. Bloomberg. Accessed 2/9/2019.

acknowledged, given the inflation rates during that period – while the global extreme poverty line is \$ 1.25 a day, which means that more Egyptians have fallen below the extreme poverty line than the numbers estimated by CAPMAS.

Even if the official figures of Egyptians below poverty line are accepted, at least 5 million additional citizens have fallen below the poverty line in just three years, in addition to the nearly one million Egyptians who have fallen prey to extreme poverty.

Figure 13:



Source: *The Central Agency for Public Mobilization and Statistics*⁴⁶.

As for international reports on poverty rates, the World Bank announced at the beginning of May 2019 that the poverty rate among Egyptians increased from 24% in 2010 to 30% in 2015 and then jumped to about 60% in 2019. And the last rate declared by the World Bank pointed out that about

⁴⁶ The dollar exchange rate was calculated according to the official rate adopted in the general budget of the corresponding fiscal year.

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60% of Egypt's population is either actually [poor or vulnerable](#)⁴⁷, the same term used by CAPMAS in the February 2019 press release on income and expenditure research. However, this expression was omitted from the press release released in late August, which means that the number of the poor in Egypt is close to 14.2 million households, an average of 58.9 million people.

Overall, this recent jump in the proportion of the poor in Egypt to nearly one-third of the population according to Egyptian government data (or two-thirds according to the estimates of many experts) during the few years in which the economic reform program sponsored by the IMF and the World Bank was implemented, confirms that the program has not achieved any improvement in the lives of citizens, but it rather exposed them to price rises, decrease in the purchasing power of their incomes, and deterioration in public services, which affected the whole society, especially the middle class, due to lack of investment in productive areas, and consequently lack of sustainable employment and insufficient increase in income as well as removal of subsidies and escalation of taxes.

Obviously, failure to adjust the current approach towards productivity and distributive justice means not only persistence of the current poverty rate, but also threatens with adding new segments below the poverty line. The government has always resorted to address the fiscal deficit with austerity measures, , often under the auspices of the IMF, cutting public expenditure and raising indirect taxes on consumption. Both measures have usually resulted in throwing the brunt of fiscal-crisis management unevenly on the shoulders of the [poorer and more vulnerable populations](#)⁴⁸.

The government tried to raise the minimum wage limit to offset the impact of inflation, but the result is not positive at all. The following figure shows the annual increase rate in the annual wage budget during the period from 2010/2011 to 2019/2020.

Figure (14):

⁴⁷ World Bank "World Bank Group to Extend Current Strategy in Egypt to Maintain Momentum on Reforms" April 2019. Link. Accessed 9/9/2019

⁴⁸ Amr Adly, "Economic Growth is Making Many Egyptians Poorer" August 2019. Bloomberg. Accessed 2/9/2019.

Increase in inflation rates vs wage increases



Source: *The Egyptian Economy after 2013 Policies and Challenges*⁴⁹

Figure (14) shows that the increase in the minimum wage under the total inflation rates during the period from 2014 to 2019 resulted in a decline in the real value of wages, the rise in the minimum wage was 66% (in the period from the beginning of 2014 when the minimum wage was LE 1200 up to the new minimum wage of LE 2000), while the inflation rate increased by approximately 107% over the same period.

In addition, the period that witnessed the most decline in wage allocations increases, starting from 2015/2016 until the end of 2017/2018 (at rates: 11.1%, 7.6%, 5.5%, 6.4% respectively against 25.77% before that) is the same period that witnessed the highest inflation in Egypt amid devaluation of the Egyptian pound.

⁴⁹ Ahmed Zikrallah, Egyptian economy after 2013, policies and challenges, EIS, 2 Aug. 2019.

Prominent manifestations of poverty among Egyptians

After more Egyptians fell below the poverty line, some manifestations related to poverty have been monitored, including:

1- A report by the Cairo Chamber of Commerce in January 2019 monitored the development of the volume of the trade of [secondhand clothes](#) that reached 273.8% in 2017⁵⁰ against 23.4% in 2014.

2- The International Food Policy Research Institute (IFPRI) issued a report confirming that 20% of Egypt's children suffer from stunting due to malnutrition, 27% of children under five are suffering from anemia, and 11% of child deaths are due to malnutrition. Interestingly, the Ministry of Health acknowledged the crisis, revealing that the rate is 40%, noting that 17% of them are [severely stunted](#)⁵¹.

The UN Food and Agriculture Organization (FAO) said in a report issued in 2014 that one out of every three children in Egypt suffers from stunting, expressing fear of likely high rates of the disease, linking the increased disease rates with malnutrition⁵². FAO also announced that Egypt suffers from a chronic problem of malnutrition in children under five, leading to stunting of 30% of children⁵³.

3- The number of infant deaths (under one year) reached 15.1% in 2016 against 14.6% in 2015, and the mortality rate among children under five reached about [19.6%](#) all over the country⁵⁴.

4- Dropout from education: Statistics indicate that the number of dropouts after enrollment reached 6.143 million Egyptian children⁵⁵.

⁵⁰ Cairo Chamber of Commerce (monthly magazine) issue 98. January 2019. Accessed on 2/9/2019.

⁵¹ Mohamed Farag Abul-Ila, Stunting among children records 30%, Sout Al Omma, 28 June 2018.

⁵² Mostafa Hosni, Stunting – a story of poverty and negligence, Almasry Alyoum, 16 Sep. 2018.

⁵³ Mohamed Farag Abul-Ila, Stunting among children records 30%, Sout Al Omma, 28 June 2018.

⁵⁴ Egypt in Figures, a booklet issued by the Central Agency for Public Mobilization and Statistics, 2018, p. 11.

⁵⁵ Ibid. p 18

5- The illiteracy rate in Egypt is 25.8% of the population⁵⁶, in addition to a percentage of 10.4% of the population can only read and write due to attending literacy programs⁵⁷ without receiving real education.

6- The number of Egyptians within the age group above 18 is 56.9 million, of whom 24% have never been married (13.6 million), while the rate of the divorced is 12% (6.8 million)⁵⁸.

The unemployment

The unemployment rate reflects feasibility of the economic measures adopted by the state, and the role of growth rate in job creation for different social classes. In this context, the Central Agency for Public Mobilization and Statistics ([CAPMAS](#)) issued a press release in mid-August 2019⁵⁹, stating that the unemployment rate in Egypt declined at an accelerated rate starting from the first quarter of last year, dropping by more than 3.8% in 18 months from 11.3% in December 2017, to 7.5% in June.

The decline in unemployment rates in Egypt does not mean that the labor market has fully benefited from the increase in economic growth, where the employment rate decreased to 38.5% of the total population in FY2018/2019 against 40.4% in the first quarter of FY2017/2018, in coincidence with the decrease of the labor force to 41.6% of the total population against 40.3% during the same period. According to the Labor Force Survey, 621,000 unemployed people have become employed as of December 2018 compared to the end of 2017, and that 147,000 exited the labor force.

The statement pointed out that the labor force, which reflects all individuals who are able and willing to work, including new university graduates, has not expanded, but rather shrank to 28.06 million last June against 29.04 million in June 2018 and 29.18 million in June 2017. This means that the labor force has fallen by 1.12 million workers in two years, and by 980,000 people in just 12 months.

⁵⁶ Ibid. p. 25

⁵⁷ Ibid. p. 30

⁵⁸ Ibid. p. 31

⁵⁹ CAPMS: Unemployment rate fell to 7.5% in the second quarter of 2019.

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This decline is incomprehensible, especially with the annual population growth rate of around 2.5%, mostly youth, and the current economic situation in Egypt. The decline in the labor force in a country where the majority of the population is young and amid the high rates of population growth is unjustifiable and needs a convincing explanation.

In addition, the rate of participation of women in the labor force declined in 2018 to 16.7% compared to 23% in 2017, which is one of the lowest rates in the world, reflecting several obstacles to the persistence of women in the labor market, or obstacles in entering the sectors that generate the economic growth rate. The decline in the number of employed women shows a significant imbalance either in the labor market or in the statistical methodology, especially as the number of employed women increases in times of high inflation and erosion of real incomes. Therefore, the decline in the number of employed women in coincidence with the increase in the number of employed men seems to be illogical.

To conclude, there is an unprecedented rise in poverty rates, which causes the middle class to fade away in favor of further expanding the poor class in unprecedented proportions. In addition, the decline in rates of the employed and the drop in the labor force may be attributed to heading towards the informal market, with negative consequences resulting from absence of insurance, health care and appropriate labor rights in addition to the non-payment of taxes. All this leads to social unrest and real challenges for the Egyptian economy.

The military incursion into economic activity

The detailed study of the economy of the Egyptian armed forces is outside the scope of this report, but given the significant impact of the growing influence of the army in the Egyptian economy, it is significant to refer to some key features in this regard:

The army's overheated and unprecedented expansion of economic activity appears to be a backlash, not only for the January 25 Revolution (2011) and its subsequent potential reduction of some of the economic spin-offs of top military commanders, but also to reports circulated by the end of the Mubarak era about plans to privatize some of its projects.

Generally speaking, controlling state land is the most dangerous tool that the military has for further encroachment on the Egyptian economy. The objectives of the army's projects are not limited to

achievement of profits, which was once the main objective of these projects, but also to a number of other objectives, including:

- 1- Exploitation of political contestation to expand control on the largest possible economic space, which may explain the rush in establishment of large projects in suffering sectors such as the cement sector, where the Armed Forces Engineering Authority established the Beni Suef cement factory (2018).
- 2- Control of the main roads which constitute the outlets of supply of most goods, including roads to and from ports and airports, between different regions, and between various governorates.
- 3- Control of the production of some strategic goods, such as insulin drugs, infant milk and others, to emerge as a savior in times of crisis, and to use as a punitive tool in the event of chaos.
- 4- The use of state projects (bridges, etc.) to raise the value of land controlled by the army and use this to enter as partner in various projects.
- 5- Controlling the economic activity of the private sector, which grew and flourished during the Mubarak era, by creating a competitor or an alternative.
- 6- Expansion of the profit-making segment from the army's projects to the small and medium army ranks, after they had been limited to senior ranks, to ensure continued loyalty of the small and medium military leaders in addition to the senior commanders to the current authority.

Therefore, the army cut deep into a large number of projects after June 2013 (after the military coup). In addition to dominating dozens of road projects and bridges by direct order, the army supervised all projects financed from the public budget, under the pretext of fighting corruption of the private sector and ensuring seriousness, commitment, and punctuality. Of course, the share of this supervision in the value of these projects has not been announced. The army also seized the road advertising sector, as well as provision of student meals to schools and universities and the privilege of managing and operating the stations to collect fees of scales and service in many roads.

The army also penetrated management of the contracting file. According to the military spokesman, the Armed Forces Engineering Authority (AFEA) oversees about 2,300 projects employing [5 million](#)

[Egyptians](#)⁶⁰. Taking into account that the labor force in Egypt is estimated at 26 million citizens, about 20% of citizens work under the management of the armed forces, according to the military spokesman It is noteworthy that the AFEA relies on subcontracting due to lack of enough human potential of engineers and workers.

With extension to other sectors, the army has become the main destination for management of projects in other sectors such as the Ministry of Health and establishment of many other projects such as the Beni Suef Cement Complex (the largest cement factory in the world), the Ghalyoun Pond Project for Aquaculture, a factory for self-destructing syringes, an air-conditioning factory, chains of outlets for selling food products in governorates, a company for the pharmaceutical industry, a company for steel industry, where the army's National Service Agency acquired 40% of the Egypt Steel Group, which has a production capacity of about 2.2 million tons as the second largest productivity in the market after Ezz Group.

Subcontracting has many forms, some of which were exposed by the latest videos of the contractor and actor Mohamed Ali, where subcontractors are assigned construction projects by direct order depending on the contractor's relations with senior army officers. After that, the contractor goes to get a loan from the bank to start implementation, and after completion of the project, AFEA pays the amount with profits of 5-7%. In this way, the subcontractor cannot resort to any body to protect him in case of disagreement with AFEA or delay in payment of dues, and consequently the funds borrowed from banks are liable to loss.

Numerous studies have confirmed the seriousness and extent of the army's intervention in the Egyptian economy, which we will refer to briefly in this report. [Shana Marshal](#) noted that "By protecting the strategic assets of its major investment partners during periods of unrest and taking control of the bidding process for major government procurement, the Egyptian Army has become the primary gatekeeper for the Egyptian economy."⁶¹ As [Yezid Sayigh](#) indicated, the companies

⁶⁰ Hassan Morsi, Military Spokesman: 5 million civilians working on 2,300 projects overseen by the armed forces, Masrawi. 2 September 2019. Accessed on 18/9/2019.

⁶¹ Shana Marshall, The Egyptian Armed Forces and the Remaking of an Economic Empire, Carnegie middle East Center, April 2015.

affiliated with the armed forces are currently operating under the principle of interest groups which are competing for the implementation of projects⁶², which transforms the army economy into something like a free economy in which the army competes with the private sector, and in the absence of accounting transparency, the army's control over the economy gives very little space for free competition with the private sector, making the military the only controller of various economic projects. Sayigh pointed in another study to the extent of the army's incursion in economy during the Hosni Mubarak era, saying, "After 1991, the Egyptian Armed Forces expanded their thorough penetration of almost every sphere of Hosni Mubarak's crony patronage system. The senior officer corps was co-opted by the promise of appointment upon retirement to leading posts in government ministries, agencies, and state-owned companies, offering them supplementary salaries and lucrative opportunities for extra income generation and asset accumulation in return for [loyalty](#) to the president,"⁶³ which is still true to the Sisi regime.

Freezing Egyptian economy cycle

The Egyptian economy had suffered from a series of structural imbalances before 2011; but unfortunately, they are still affecting it up to now. Moreover, the escalating domestic and external loan rates have exacerbated these imbalances, and the political intervention in directing economic projects has contributed to creation of an extremely alarming economic situation in the medium and long terms. The report will attempt to address this situation, which is likely to lead to freezing the economic cycle in Egypt, by comparing the factors of leakage outside the circle of economic activity, and the injection factors, as follows:

A- Leakage factors

Egyptian authorities (represented in the head of the regime) directed the government to implement a series of projects, which cost huge sums, borne by the public budget, external loans, or citizens' savings.

⁶² Yezid Sayigh, The return of military interest groups in Egypt, Carnegie middle East Center, December 2015

⁶³ Yezid Sayigh, Above the State: The Officers' Republic in Egypt, August 2012.

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Objectivity, economic prudence and methodology of priorities were absent from the method of selection of these projects. The funds spent on these projects were frozen and did not result in a significant return to compensate the capital or afford loan installments.

The most prominent examples of these projects include:

The Suez Canal shunt

The Suez Canal Authority announced that the cost of digging will reach \$ 8 billion: \$ 4 billion to dig a shunt parallel to the current Suez Canal waterway and another \$ 4 billion to dig 6 tunnels under the Suez Canal. The government then offered investment certificates to citizens that mature after five years with a 12% yield, raising LE 64 billion, equivalent to \$ 8.5 billion, in a few days, mostly withdrawn from bank deposits.

Besides discussing the feasibility of digging the tunnels and the new shunt, the results do not indicate any increase in the Suez Canal revenues. Rather, the rush to dig the shunt implicated the Suez Canal Authority itself into successive loans - for the first time in its history - amounting to about \$ 2 billion. In addition, the cost of tunnels, whether for the crossing of cars or for the transfer of water to the Sinai Peninsula, benefits are still limited, and there have been no breakthroughs in the reclamation of land depending on this water so far.

Anyway, some \$ 6 billion have been leaked - to raise the morale of Egyptians, as Sisi put it - in addition to some \$ 2 billion of internal and external borrowing.

The new administrative capital

Almost all foreign companies have withdrawn successively from the financing of the new administrative capital, including the UAE Emaar Properties and Chinese companies, which prompted the government to rely on domestic financing and purchase of land from local real estate companies. However, the government has recently resorted to borrowing from China despite many warnings from experts.

As a result, the administrative capital projects leaked a large part of the local liquidity and took it out of the economic activity cycle. After construction in the administrative capital is completed, it is not expected to take advantage of the huge mosque or church or luxury hotels that have been built

before many years. Even the private sector's real estate projects will remain closed for years. Only some administrative buildings will be used and a small percentage of the total construction for a long time.

Express train project

The National Authority for Tunnels signed an agreement with Bombardier Transportation, Orascom Construction and Arab Contractors to design and build two new monorail lines in Egypt: the new administrative capital and the other in the 6th of October city. On completion of the construction phase, the consortium will be responsible for the Operation and Maintenance (O&M) of both lines for 30 years. The total value of the design, build, operate and maintain contract exceeds \$4.5 billion (4.1 billion euro). Bombardier Transportation's share is \$2.85 billion US (2.6 billion euro).

In general, borrowing this huge amount - especially from China - will impose repayment difficulties on the Egyptian economy amid difficulties of over-borrowing, which contributes to leakage of money outside the economic activity cycle, which may have catastrophic effects in the coming period.

National Roads Project

The total investments of road projects have amounted to LE 253 billion until June 2020, of which 113 projects have been implemented so far at a cost of LE 115 billion. This made Egypt jump 43 spots in the international rankings, coming in the 75th position, where it had been in the 118th. position before. With the beginning of 2019, the country built 334 bridges and tunnels, including 4 bridges across the Nile.

Undoubtedly, roads and bridges are the lifeblood of economic life, but two questions arise here:

- Was Egypt in need for all these roads and bridges?
- Were they built according to studies that reflect plans of economic and social development to meet needs of expansion?

In general, the state has not revealed any development plan to show the economic reasons behind building all these roads and main routes. The government's keenness on implementing some of these projects can be explained by its intention to raise the value of land owned by the army on both sides

of the roads, where the military use as shares in partnership with local or foreign investors in various projects.

In general, a significant part of the road and bridge network will put off the maximum benefit of public spending on them for years to come, which means leakage of a significant part of these funds outside the cycle of national income.

New airports

The new airports are the most prominent example of waste and freezing of funds, as many airports have been established or under construction in a radius of 75 kilometers, including the Administrative Capital Airport, Ras Sidr Airport, Malaz Airport, and re-operation of Al-Tur airport, all in the presence of Ismailia Airport and Cairo Airport. It is noteworthy that Upper Egypt is completely absent on this plan, which confirms absence of the development dimension. Of course, there is no convincing explanation for such constructions, and it is strange that the government insists on completing the scheme, resulting in the freezing of a significant part of the costs and thus leakage outside the national income circle.

New factories

The government plans to establish seven new investment zones and build productive plants. The industrial map includes establishment of 13 industrial clusters in 13 governorates with implementation rates reaching 90%, while some have already been completed, according to official statements.

These factories are fully equipped, and some of them are said to be completely furnished with equipment and machinery. Therefore, the most important question remains: who will run these projects? It is well known that the domestic investor is groaning from the imposed economic measures - especially the high interest rate - amid a significant decline in foreign investment during the past three years.

Apart from absence of developmental and integral linkages between these factories, it is clear that most of them will remain empty for quite some time until the local consumer regains some of his lost purchasing power, or foreign investment regains trust in the Egyptian economic climate.

In addition, wouldn't it have been better to invest in the operation of the already suspended factories which are estimated at [7,000 factories](#)⁶⁴, rather than the construction and operation of 66 new ones?

These are only examples of projects that the Egyptian regime rushed to accomplish without any feasibility studies, resulting in freezing and leakage of funds that could have contributed to the revival of productive activity, rather than creation of a fictitious state of unsustainable growth.

In addition, there is an indirect negative cost for the leakage of these funds, including curtailing the ability of banks to create credit, reducing the consumer purchasing power of citizens, and contributing to recession, in addition to crowding out the private sector for funds, and crowding out the productive sector in general.

Loan installments and interest

The Central Bank of Egypt (CBE) data shows that the medium and long-term debt service estimates for 2019 rose to \$ 16.9 billion at the end of September 2018 against \$ 14.7 billion in previous estimates by the end of June 2018, compared to \$ 2.08 billion short-term debt expected to be repaid during the first nine months of this year. The total outstanding obligations during 2019 will be approximately \$ 18.9 billion.

The CBA data also shows that the Central Bank of Egypt has succeeded in repayment of more than \$ 36 billion of debts and external liabilities during the last three years. Undoubtedly, all these funds abroad is a leakage outside the circle of economic activity and an additional drying up of its resources.

More leakage (military activity)

The army economy is another example of money leakage outside the economic activity cycle, as projects are assigned to companies by direct order, exempted from taxes and customs and no one knows how profits are distributed and where the major shares go, in addition to lack of optimal use

⁶⁴ Essayid Abdel Razek, Economists: Closed factories, 'a neglected treasure', .. and 5 obstacles facing the industrial sector, Masralarabia, Jan. 2019.

of resources and projects directly managed by the army, which represents a form of leakage out of the circular flow of economic activity.

Also, the military factories that have been built without a market study, or those that contributed to the disruption of the private or public sector and suspension of the production of some of their projects, whether partially or totally, is one form of the leakages outside the circular flow of economic activity.

Migration of some national capital

Expansion to the seizure of funds of political practitioners, whether Islamists or liberals, as well as the broad powers of the sovereign bodies (military and security services) in economic activity and the prevailing political uncertainty has contributed to migration of some medium-sized Egyptian businessmen out of the country. Their funds are transferred either informally through brokers, or through the official purchase of international certificates of deposit (securities) from the London Stock Exchange, and more recently through electronic money. Whatever the transfer method has been, the result is the drainage of these funds and leakage out of the circular flow of economic activity.

B- Sources of injection

Historically, the Egyptian national economy depends on a group of sources of external injection, which bear the burden of bridging the foreign currency gap resulting from the trade balance deficit, in addition to filling the financing gap resulting from the budget deficit.

Sources of injection can be analyzed as follows:

External loans

Egypt's external loans has increased sharply since 2013, reaching about \$ 106 billion by the end of March 2019 against \$ 39 billion at the end of 2013, according to a recent statement by the Minister of Planning. The response of international and regional institutions to Egyptian borrowing requests has been normal after the Egyptian government adopted the IMF program, as well as some political arrangements regarding the roles played by the Egyptian regime and its regional and international alliances.

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In addition, Egypt has resorted to issuance of dollar bonds more than once during the past two years, and the increased appetite of international market for purchase due to the high interest rate and stability of the pound exchange rate that allow achievement of large hot profits, especially after the World Bank and the IMF had praised the Egyptian government's economic reforms, which represented a relatively cheap tool for borrowing compared to the domestic market's interest rate.

Many experts believe that the Egyptian government has consumed most of the doors available for borrowing and reached its maximum limits with some regional bodies, which means that the frequency of injections through external borrowing has decreased during the past two years. Perhaps, the return to the Islamic Sukuk law that has been ignored since 2013 may be an acknowledgment of the drying up of borrowing sources. In fact, the transfer will be reversed to be abroad as part of the repayment of loans and their interest.

Remittances of Egyptian expatriates

Remittances of Egyptian expatriates has increased by \$ 778.2 million to \$ 25.5 billion in 2018, compared to \$ 24.7 billion in 2017; and experts justified this increase by the return of thousands of Egyptians working in the Gulf region, especially Saudi Arabia, to their homeland permanently because of disposition of many Egyptians due to adoption of policies of replacement of foreign labor by national labor, the increased residence fees and higher prices; which prompted Egyptian expatriates working in some Gulf countries to return home with their savings, including end of service allowances.

Data released by the Central Bank of Egypt in March 2019 shows that remittances of Egyptians working abroad declined during the first nine months of FY2018/2019 by 6.1% on an annual basis, which indicates that remittances are declining in general, and the increases after the pound flotation were only to meet the needs of their households as a result of the successive price increases, as well as the permanent return of a significant part of expatriates, as a result of the above conditions. Generally, the decline referred to earlier is the beginning of expected successive declines of remittances of Egyptian workers abroad during the coming period, which represents a decrease in a form of injection that Egypt has relied upon since the oil price boom in the 1970s until now.

Foreign direct and indirect investment

This report has earlier discussed in detail the decline of foreign investments to Egypt during the past two years, but the direct investment in natural gas and petroleum exploration remains one of the most important sources of injection in the Egyptian economy, but it is criticized because a considerable part of income goes to foreign equipment, machinery and expertise, which leads to leakage of these funds out again, in addition to the foreign partner's share of the resulting revenue. Investment in domestic debt instruments cannot be relied upon as an injection tool in the Egyptian economy. Hot money chases after the high interest rates and easily move between countries; therefore, reliance on them should only be temporary.

Tourism proceeds

The tourism sector achieved an estimated growth rate of 16.5% in 2018, the best since 2010. Tourism contributed 11.9% of GDP and created 2.5 million jobs, equivalent to 9.5% of the total number of jobs in Egypt.

According to data of the World Travel and Tourism Council, tourists spent \$ 12.2 billion in Egypt last year, and expected that the number of tourists travelling to Egypt this year will reach 11.7 million tourists.

Of course, the continued injection of tourism in the national income is related to a set of factors, although it is mostly outside the Egyptian economy model, but it is expected to be relatively stable during next year, which is likely to stabilize the contribution of that sector in the coming period.

Suez Canal revenues

Although no leaps have been made after digging the new Suez Canal shunt, the rate of Canal injection into the economy continues, although it is likely to be affected by the expected slowdown in global growth and trade, albeit within normal limits.

It seems that the big effect on the Suez Canal injection into economy will be paying off the Suez Canal Authority debts, even through new loans, which means that leakage would be equal to or less than the expected injection. In general, the rate of the Suez Canal injection in the national economy is more stable and sustainable.

C- Between injection and leakage in Egyptian economy

The above analysis of elements of injection and leakage to and from the circle of economic activity and national income indicates an apparent predominance of the phenomenon of leakage elements. Unfortunately, most of this predominance is due to state projects, which led to the freezing of a large part of domestic funds through borrowing from local banks to spend on projects that will not generate any significant proceeds. In this context, the Egyptian government has failed to shift towards production, which would create added values that could lead to further injection into the national economy.

We believe that after the next two years, in which loan and interest repayments will escalate, the flow of loans and deposits will decline, and the remaining roads and the projects of the new administrative capital will be completed, the current growth rate will decline and the economy will contract further - especially in light of likely implementation of the planned restructuring of the administrative sector. However, it may not necessarily fall into the recession tunnel due to the presence of some sustainable injection factors. However, the Egyptian citizen will be severely affected, and poverty rates will further increase, which means that the years after 2020 are difficult years for the Egyptian economy, unless there are radical changes, all related to factors outside the current economic framework.

Conclusion and Recommendations

The report has reviewed the results of the economic policies adopted by the Sisi regime and concluded that the current policies do not target the interest of citizens, but rather seeks improvement of macroeconomic figures, which has not produced real positive results. Despite the high GDP growth rate, the sectors contributing to such growth are not productive sectors, such as industry and agriculture sectors, but rentier sectors such as the extractive sectors, remittances of Egyptian expatriates working abroad, and tourism. In addition, the huge increase in the Egyptian pound-denominated GDP does not reflect an increase in the volume of goods and services, but it is due to the high inflation rates. This is evidenced by the fact that the value of GDP decreases if denominated in dollars. As a result, the Egyptian citizen has not felt any improvement in living standards or any positive results of such growth.

The report has also reviewed the FY2019/2020 budget, where the interest on loans represents approximately 50% of its total revenues and nearly 40% of its total expenditure and swallows any possibility to increase government investments in health, education and infrastructure. It has also led to a chronic deficit that is likely to continue to afflict the Egyptian budget, prompting the government to raise taxes, cut subsidies, and resort to borrowing to fill the deficit, which directly affects the poor and middle classes that are already bearing the costs of current economic policies without feeling any improvement.

As for the consequences of monetary policies, domestic and foreign debts rose to unprecedented levels, which could affect Egypt's ability to borrow in the future. Also, adding escalating debt interest burdens to the public budget reduces the state ability to channel these funds to real development projects.

As for inflation, despite its declining in recent months, the high inflation rates during the past years have resulted in a decrease in the real value of wages by 20%, considering the high inflation rates. The decline in current inflation rates is also due to the decline in demand in the Egyptian market as a result of high poverty rates and the increasing living burdens due to price rises over the past years, which resulted in the lack of the citizens' purchasing power and accordingly the inability of traders to raise prices despite the recent increase in fuel prices.

In terms of investments, investment rates in Egypt are still modest and do not lead to positive results with respect to global competitiveness or the ability to absorb new manpower on an annual basis. The private sector and the middle and poor classes bear the burden of the IMF program and will likely remain under pressure, especially after the recent hike in fuel prices, all of which means that conditions will remain difficult for private companies.

The results of these policies reflected on poverty rates significantly, where at least 5 million new Egyptians fell below the poverty line, a rate of 32.5% in the CAPMAS 2017 report against 28% in 2015. As a result, the middle class is rapidly disappearing, and the poor class is significantly expanding.

As for unemployment; despite the official figures that indicate a decline in unemployment rates, this is mainly due to the decrease in employed women and the creation of unsustainable jobs in national

projects. The decrease in the rate of workers and the decline in the labor force may be attributed to heading towards the informal market, with negative consequences resulting from the unavailability of insurance, health care, appropriate labor rights in addition to the failure to provide due taxes. All this leads to social unrest and real challenges for the Egyptian economy.

It can be concluded that the current economic policies do not lead to a real development process in the short and medium term. The Egyptian economy needs a structural change based on existence of a long-term development vision that focus on achieving real results on the ground, where the citizen must be its main focus.

The report has reviewed the Egyptian government approach of adopting austerity economic policies that do not ultimately lead to investment in human infrastructure such as education and health. On the contrary, poverty rates have unprecedentedly increased, and the costs of economic austerity have been thrown on the shoulders of citizens and the private sector. It is apparent that the future of the Egyptian economy will be very negative if the current policies continue.

The report recommends the following:

- A strategic plan for the development process should be devised for changing the Egyptian economy structure into a productive economy.
- Fair distribution policies should be adopted, which requires a plan to stop adopting policies to reform macroeconomic indicators by reducing public spending and raising taxes, thus throwing the reform costs on the shoulders of citizens and the private sector.
- The regime must shift from austerity policies to expansionary policies that seek to stimulate economy and increase market liquidity.
- The general investment climate must be controlled, starting from controlling the political climate, setting limits for the military intervention in the economic process, and allowing free access to information.

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