# Executive Summary

## *Key Highlights..*

*GDP Latest figures* ***suggest the economy's recovery pace is still slow.*** *GDP growth came at a humble 1.2 percent in H1-FY13/14, mainly due to security reasons and political developments. Moreover, disbursements of the announced two stimulus- packages –that focused on propping up government investments- were not fully captured in GDP growth during the period of study, mainly due to tendering procedures for stimulus related projects.* ***This suggests that recovery in the second half of FY13/14 would assume a faster pace.***

> ***Going forward, the government's strategy will shift to the second phase of reviving the economy,*** *via preparing an additional stimulus package that will focus solely on removing bottlenecks that hinder private sector investments in key economic sectors, namely; industrial, housing and construction, communications and tourism. This should accelerate the pace of growth, while crowding in the private sector, which is a key contributor to employment.*

***On the fiscal side*, budget deficit continued its decelerating trend in the first 9 months of FY-13/14 to reach 7.1 percent of GDP,** *compared to 10 percent during the same period a year earlier. This was mainly due to an increase in tax revenues and grants, accompanied with a slower increase in investments. Moreover,* ***total government debt*** (domestic and external) reached LE 1751 billion (85 percent of GDP) in December 2013, compared to LE 1644 billion (94 percent of GDP) at end of June 2013.

***As for the external debt,*** *it is important to highlight that:*

- **External debt service to exports of goods and services ratio** has been unchanged since 2008/2009 till 2012/2013 stabilizing at an average of 6.2 percent. Furthermore, this ratio declined at end of December to reach 5 percent, thus indicating a safer level to meet debt service obligations.
- ***Short-term debt to total external debt ratio*** *decreased from 17.1 percent at end of December 2012 to 6.2 percent at end of December 2013. This could be explained mainly for redeeming Qatari short-term deposit worth US$ 2 billion by end of December 2013, in addition to another matured deposits worth US$ 1 billion.*

***As for the monetary developments, M2 growth*** **increased at slower pace during February and January 2014, reaching 17 percent and 16.7 percent, respectively,** compared to an average of 18.8 percent during the first 6 months of the year 2013/14. ***Such deceleration did have a proportional impact on Headline Urban inflation, which stabilized at 9.8 percent*** *in March 2014 for the second month in a row, compared to an average of 10.9 percent in the first six months.*

***On the external sector side, BOP*** *showed a significant improvement during the period July-December 2013/2014 recording an overall surplus of US$ 2 billion, compared to an overall deficit of US$ 0.6 billion in the same period last year. Meanwhile,* ***international reserves*** *increased during March 2014 reaching US$ 17.4 billion - on the back of the increase in foreign currencies – thus recording a positive growth for the third month in a row, after a continuous decrease since July 2013.*

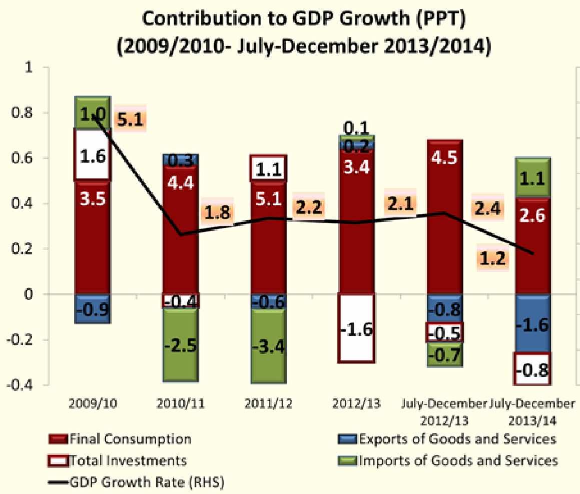
## *Real Sector…*

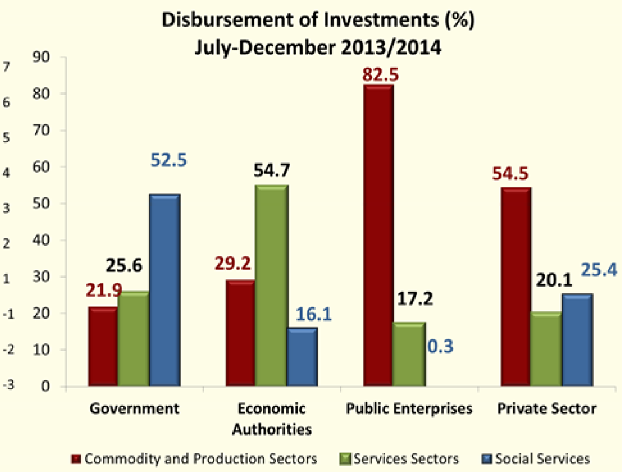
*Five key sectors led growth in H1-FY13/14…*

***Real GDP growth* came at a 1.2 percent in H1-FY13/14**, compared to 2.4 percent a year earlier, mainly in light of security reasons and political developments during this period.

**On the supply side,** key sectors that led growth in the first half of FY13/14 were the **agricultural sector and the general government**, with real growth rates of 3.5 and 5.5 percent respectively, contributing by 0.6 and 0.5 PPT, compared to 0.5 and 0.3 PPT a year earlier. **Wholesale and retail trade** real growth came at 3.2 percent in the same period (0.4 PPT compared to 0.3 PPT a year earlier), while **non-oil manufacturing sector and the construction sector** witnessed growth at 2.3 and 3.9 percent (0.3 and 0.2 PPT) respectively, same as a year earlier. Together, they represented around 56 percent of total real GDP in the period of study.

**Meanwhile, Tourism and natural gas extraction sectors continued to subdue growth** in the first half. Tourism has been severely hit due to several unfortunate events, falling by 30 percent y-o-y in the first half of FY13/14, while natural gas extraction fell by 8.2 percent in the same period, contributing negatively to growth.




***On the demand side, Private consumption*** grew by only 2.5 percent y-o-y in the period of study, after having accelerated by 4.2 percent y-o-y in Q1-FY13/14, implying that Q2-FY13/14 real growth came at a humble rate of 0.8 percent. Similarly, **public consumption** grew at 4.8 percent in the period of study, compared to 5.6 percent a year earlier, after having accelerated by 5.9 percent in Q1-FY13/14, implying a slow-down in growth (3.6 percent) in Q2-FY13/14.

***Investments*** continued to hinder GDP growth in the first six months of FY13/14 with a (-ve) real contribution of 0.8 PPT, compared to 0.5 PPT negative contribution in the same period last year.

As for the distribution of total **investments by economic agents** (in nominal terms),public investments ( government + economic authorities + public business sector) accounted for 25.6 percent of total investments in Egypt during the period of study, while the private sector accounted for 74.4 percent in the same period, noting that nearly half of government investments were directed towards social services sectors.

Meanwhile***, net exports*** posted a negative contribution of 0.5 PPT in the first half, down from -1.6 PPT a year earlier. ***Exports*** continued to decelerate in the first half of FY-13/14, decreasing by 9.5 percent with a contribution of -1.6 PPT to real GDP growth, compared to -0.8 PPT a year earlier. While ***imports*** dropped by 4.2 percent in the same period, contributing positively by 1.1 PPT, compared to -0.7 PPT in the same period last year.

***Industrial production index*** declined by 7 percent in February 2014 to 179.5 points, compared to 193 points in January 2014. However, this is still higher than the June 2013 level of 173.4 and the December 2013 level of 151.6.

***The EGX-30 index*** decreased by 322 points during March 2014, reaching 7805 points compared to 8127 during February 2014. Moreover, market capitalization decreased by 3.5 percent m-o-m during the month of study to reach LE 470 billion (22.9 percent of GDP) compared to a LE 487 billion during the previous month. Such decrease could be attributed to a market correction, as investors resort to short term selling to gain profits. Meanwhile, the value of traded stocks increased significantly recording L.E 29.3 billion in March 2014, up 14 percent m-o-m compared to February 2014, and 90 percent compared to December 2013, suggesting that the level of activity has increased significantly.

## *Fiscal Sector:*

***Budget Deficit continued its decelerating trend…***

***Budget Deficit*** **continued to decline during the first 9 months of FY 2013/2014 in value and as percent of GDP,** compared to the same period last year. This came as a result of a higher increase in revenues and slow increase in investments.

| July- March 13/14 Budget Deficit<br>LE 145 billion (7.1 percent of GDP) | July- March 12/13 Budget Deficit<br>LE 175.9 billion (10 percent of GDP) |
|---|---|
| **Revenues**<br>LE 282.7 billion (13.8 percent of GDP) | **Revenues**<br>LE 208.2 billion (11.9 percent of GDP) |
| **Expenditure**<br>LE 423 billion (20.6 percent of GDP) | **Expenditure**<br>LE 382.5 billion (21.8 percent of GDP) |

**Source:** Ministry of Finance, Macro Fiscal Policy Unit

***Both Tax and Non-Tax Revenues increased during the period of study…***

***On the revenue side,***

- Total revenues increased significantly during July-March 2013/2014 by 35.8 percent, recording LE 282.7 billion (13.8 percent of GDP), mainly due to the increase in both tax (8.2 percent of GDP), and non-tax revenues (5.5 percent of GDP) by 8.3 percent and 118 percent respectively.

- **Tax revenues** increased due to the rise in all tax receipts except for taxes on goods and services, and other taxes, mainly due to the decline in both of; excises on domestic commodities by 20 percent (particularly the decline in sales tax on petroleum products) and the decline in general sales tax on services by 8.6 percent (particularly the decline in hotel and restaurant, and communication services).

**Tax Revenues increased due to:**

**Taxes on Income, Capital Gains and Profits increased by LE 12.4 billion (19.8 percent growth) to reach LE 75.3 billion (3.7 percent of GDP)**

Mainly on the back of an increase in:
- Taxes on domestic salaries by LE 1.9 billion
- Taxes on industrial & commercial profits by LE 0.8 billion
- Receipts from EGPC by LE 14.9 billion to reach LE 30.6 billion (1.5 percent of GDP), after including the second settlement in January 2014

**Taxes on Property increased by LE 2 billion (17.2 percent growth) to reach LE 14 billion (0.7 percent of GDP)**

Mainly as a result of an increase in Taxes on T-bills and bonds payable interest by 21.3 percent y-o-y to LE 11.5 billion (0.6 percent of GDP)

**Taxes on International Trade increased by LE 0.3 billion (2.8 percent growth) to reach LE 12.4 billion (0.6 percent of GDP)**

In light of an increase in taxes on valued customs by 5.2 percent y-o-y to LE 11.9 billion (0.6 percent of GDP)

***…while Non tax revenues hiked mainly due to extraordinary grants, in addition to an increase in receipts from Sovereign Authorities***

**Moreover, the significant increase in non-tax revenues could be explained in light of the following:**

- Increase in grants to reach LE 51.4 billion during July-March 2013/2014 (2.5 percent of GDP), mainly due to:

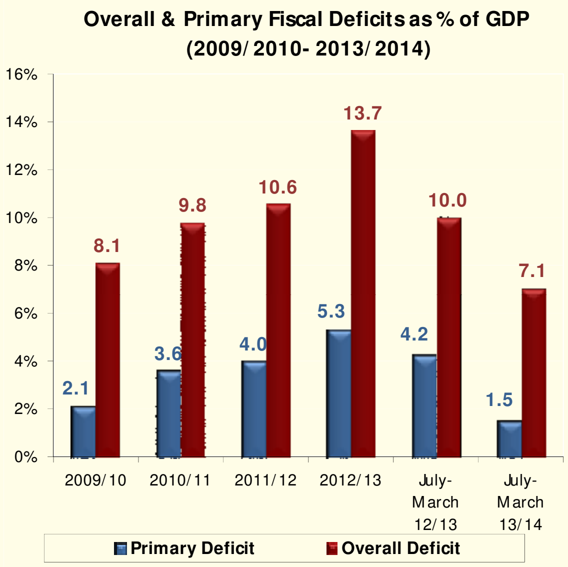
  a) LE 29.7 billion increase in grants—half of the dollar denominated deposits at the central bank- to be allocated to finance the first stimulus package related to the presidential decree no. 105, 2013.

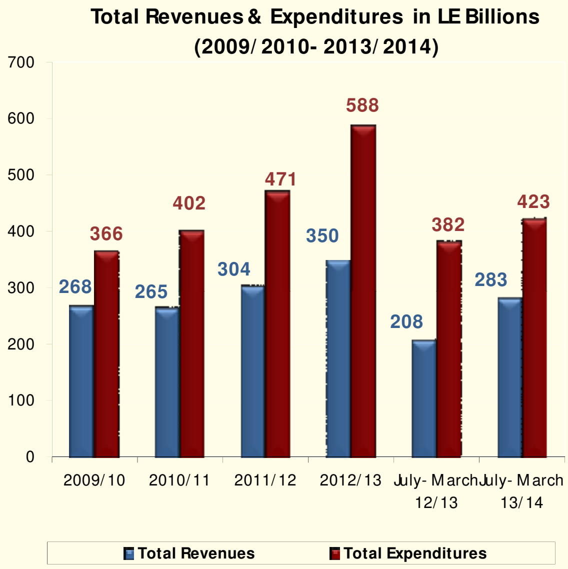
  b) LE 21 billion (the equivalent of US$ 3 billion) cash grants from Gulf countries.

- Increase in dividends collected from EGPC by LE 7 billion, dividends collected from Central Bank by LE 4.8 billion, and dividends collected from Suez Canal by LE 0.8 billion.

- Increase in revenues from sales of goods and services by 38.9 percent y-o-y to LE 15.8 billion (0.8 percent of GDP) mainly due to the increase in revenues from special accounts and funds[1] by LE 3.8 billion to record LE 12.9 billion in the period of study compared to LE 9 billion during the same period last year.

1 The increase comes in light of the law number 19 for the year 2013, which stipulated that budget entities should pay to the Ministry of Finance 10 percent of the revenues from special accounts and fund; additionally, 25 percent of the outstanding balance was repaid to the treasury in 30/6/2013.




Source: Ministry of Finance

***On the Expenditures Side:***

***Increase in Wages, Investments and Social Benefits***

Total expenditures increased during July- March 2013/2014 by 10.6 percent, recording LE 423 billion (20.6 percent of GDP), mainly due to:

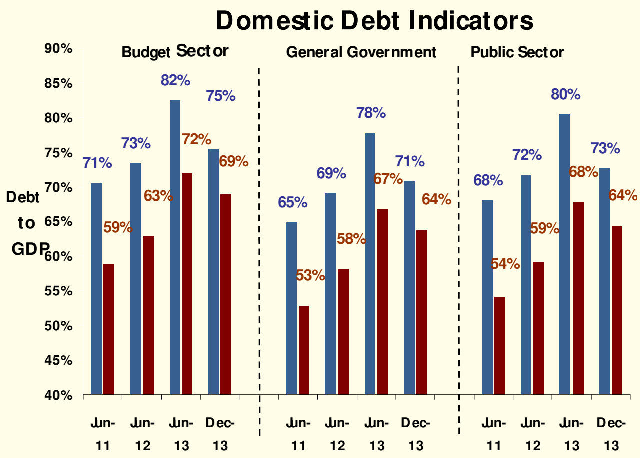
- The increase in wages and compensation of employees by LE 19.2 billion to LE 121.9 billion (5.9 percent of GDP).
- The increase in subsidies grants and social benefits by LE 1.5 billion to LE 118.2 billion (5.8 percent of GDP).
    - **Payments to pension funds increased by LE 12.6 billion** during July-March 13/14 (of which an increase of LE 2.4 billion only in March 2014), to reach LE 24.3 billion during July- March 2013/2014, compared to LE 11.8 billion during the same period last year.
- The increase in interest by LE 12.3 billion to LE 113.8 billion (5.6 percent of GDP).
- The rise in other expenditures by LE 2 billion to LE 26.4 billion (1.3 percent of GDP).
- The increase in purchase of goods and services by LE 0.01 billion to LE 16 billion (0.8 percent of GDP).
- The increase in purchases of non-financial assets (investments) by LE 5.6 billion (1.3 percent of GDP).

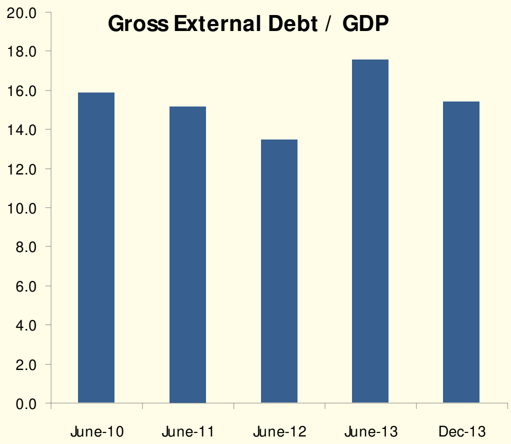
    It is worthy to note that some LE 26.7 billion were disbursed as purchases of non-financial assets (investments) during the first 9 months of 2013/2014, increasing by 26.5 percent compared to the same period last year, while investments are expected to increase further during the coming period.

***Increase in Domestic Debt…***

***Domestic budget sector debt*** recorded LE 1546 billion (75.4 percent of GDP) by end of December 2013, compared to LE 1294 billion (73.8 percent of GDP) by end of December 2012.

***It is worth mentioning that the total government debt*** (domestic and external) reached LE 1751 billion (85 percent of GDP) in December 2013, compared to LE 1644 billion (94 percent of GDP) at end of June 2013.




Source: Ministry of Finance

***External debt stock***[2] **(government and non-government debt)** recorded US$ 45.8 billion by the end of December 2013 compared to US$ 38.8 billion by the end of December 2012 (most of the increase represented aid from the Gulf Countries with concessional and preferential terms). External debt as percent of GDP recorded 15.5 percent by the end of December 2013, which is relatively low if compared to the average of peer countries (Middle East and North Africa countries recorded an average of 25.5 percent of GDP during the year 2013)**.**

**Main External debt indicators are as follows:**

§ **External debt service to exports of goods and services ratio** has been unchanged since 2008/2009 till 2012/2013 stabilizing at an average of 6.2 percent. Furthermore, this ratio declined at end of December to reach 5 percent, thus indicating a safer level to meet debt service obligations.

§ **Short-term debt to total external debt ratio** decreased from 17.1 percent at end of December 2012 to 6.2 percent at end of December 2013. This could be explained mainly for redeeming Qatari short-term deposit worth US$ 2 billion by end of December 2013, in addition to another matured deposits worth US$ 1 billion.

## *Monetary Perspective:*

***M2 reached an annual real growth rate of 7.2 percent…***

***M2 annual growth*** increased at **slower pace** during **February and January 2014**, reaching 17 percent and 16.7 percent, respectively, (LE 1417 billion and LE 1398 billion, respectively), compared to an average of 18.8 percent during the first 6 months of the year 2013/14. The above mentioned growth can be explained in light of a parallel slow-down in both money and quasi money during February 2014, reaching 22.5 percent and 15.1 percent, respectively, (LE 378 billion and LE 1039 billion, respectively), compared to an average of 28.1 percent and 15.6 percent, respectively, during H1-FY13/14.

Moreover, **net domestic assets** of the banking system annual growth showed a similar slow-down during February 2014 recording 19.7 percent (LE 1291 billion), compared to an average of 23.9 percent in H1-FY13/14, mainly due to a slower annual increase in **net claims on government and GASC** recording LE 937 billion. Moreover, **lending to private sector** almost

2 The notable increase in non-government external debt during the first half of the fiscal year 2013/2014 can be explained in light of a net increase of nearly US$ 4.4 billion in external debt on the monetary authorities compared to end of December 2012/2013. The breakdown of inflows is as follows: US$ 2 billion from UAE, US$ 2 billion from Saudi Arabia and US$ 3 billion from Kuwait. Meanwhile the Qatari short term deposit worth US$ 2 billion was cancelled and a Qatari deposit worth US$ 1 billion was converted into T-bonds during the period of study. Moreover, it is important to highlight that Egypt has returned another matured deposits worth US$ 1 billion to Qatar during the period of study.

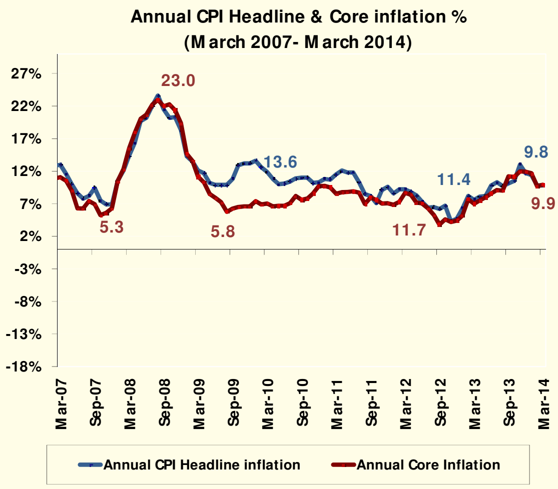
stabilized for the second month in a row, at an annual growth of 5.5 percent (LE 504.5 billion) in February 2014, while it decreased if compared to an average of 8.5 percent recorded during H1-FY13/14. Meanwhile, **net foreign assets** began to show signs of improvement recording a positive m-o-m growth rate for the third month in a row, while y-o-y deceleration slowed down reaching -4.7 percent at end of February 2014 (LE 126.8 billion), compared to -25.2 percent at end of February 2013 and average of -14.9 percent during H1-13/14.

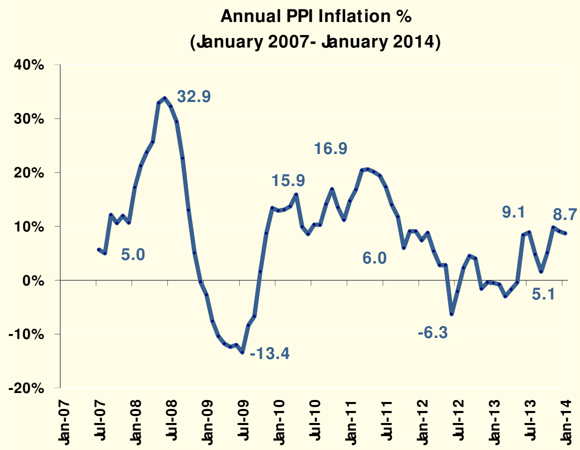
**Total deposits** annual growth – excluding deposits at the CBE – slowed down slightly reaching 19 percent y-o-y (LE 1325 billion) at the end of January 2014, compared to a growth of 20.6 percent at end of December 2013. Out of total deposits, 87 percent belonged to the non-government sector. To that end, **loans-to-deposits ratios** almost stabilized for the second month in a row at an annual growth of 41.7 percent, while decreased if compared to 47.4 percent in January 2013. (Detailed data for February 2014 is not yet available)

***Monthly CPI stabilized during March 2014***

***CPI annual Urban Inflation*** increased during the period **July-March 2013/2014** recording an **average** of 10.7 percent, compared to 6.3 percent during the same period of last year. Factors contributing to inflationary pressures include; higher food prices (the largest weight in CPI), and some other seasonal reasons, as well as an unfavorable base effect.

However, it is noteworthy that the annual inflation growth rate **stabilized for the second month in a row recording 9.8 percent during March 2014** (the lowest inflation rate since September 2013). This development is mainly attributed to the relatively stable annual inflation recorded by most groups particularly "Food and Beverages" group. Meanwhile, some other groups increased on the top of which "Furnishing, Household Equipments", and "Miscellaneous Goods and Services", and "Recreation and Culture". On the other hand, monthly inflation decreased to 0.7 percent during March 2014 compared to 1 percent in the previous month.




***Annual core inflation*** rose during March 2014 to 9.9 percent compared to 9.7 percent during February 2014. Meanwhile, monthly core inflation declined to 0.7 percent compared to 1 percent during the previous month. The monthly inflation could be explained in light of the increase in food prices contributing by 0.63 percentage points. This was coupled with higher prices of other services, and retail items, which contributed by the remaining 0.07 percentage points to monthly core inflation.

***CBE easing monetary policy in H1-FY13/14…***

During its ***Monetary Policy Committee*** meeting held on April 28, 2014, CBE decided to keep the **overnight deposit rate** and **overnight lending rates** unchanged at **8.25 percent** and **9.25** percent respectively, and to keep the CBE's **main operation** unchanged at **8.75 percent**. The discount rate was also kept unchanged at 8.75 percent. The committee justified that decision in light of balancing upside risks, the inflation outlook, with the downside risks to economic growth at present.

**In an attempt to absorb excess liquidity and to protect the domestic currency, the CBE announced the reintroduction of deposit operations.** In this context, on April 29, 2014, the CBE introduced LE 50 billion worth of 7-day maturity at a fixed annual interest rate of 8.75 percent.

It is noteworthy that the CBE has offered US$ 1.5 billion on January 27, 2014 at ***Foreign Exchange exceptional auction*** to meet banks import financing needs.

## *On the External Sector side:*

***BOP*** showed a significant improvement during the first half of 2013/2014 **recording an overall surplus of US$ 2 billion** (0.7 percent of GDP), compared to an overall deficit of **US$ 0.6 billion** in the same period last year, and compared to an average deficit of US$ 1.2 billion over the last 5 years. The recorded surplus can be explained in light of the notable decrease in the **current account deficit**, recording US$ 0.8 billion (0.3 percent of GDP) compared to a deficit of US$ 4.9 billion in the same period last year. This was mainly driven by the noticeable increase in **public transfers** coupled with the deceleration in **imports**. Moreover, the **capital and financial account** witnessed net inflows of US$ 3 billion (1 percent of GDP), compared to net inflows of US$ 6.4 billion during the same period last year, while net errors and omissions recorded an outflow of US$ 0.2 billion, compared to an outflow of US$ 2.1 billion during the period July-December 2012/2013 .

§ On a more detailed level, the decrease witnessed in the **current account balance deficit** can be attributed to:

- The significant increase in **public transfers** during the first half of 2013/2014 recording US$ 6 billion (2 percent of GDP) in light of grants received from Arab countries (US$ 1 billion from the United Arab Emirates, US$ 3.7 billion in-kind grants from Gulf countries in the form of petroleum shipments and US$ 1.3 billion international funding and grants from various countries), compared to US$ 0.6 billion during the same period last year.
- The decline in **trade deficit** by 16.8 percent to US$ 15.4 billion during the period of study, compared to US$ 18.5 billion during the same period last year. This was mainly due to the decrease in imports payments by 7.4 percent and the increase in exports proceeds by 7.5 percent, and thus resulted to the following:
  - Increase in exports to imports coverage ratio to reach 44.9 percent during H1-FY13/14, compared to 38.7 percent during the same period last year.
  - Rise in NIR imports coverage ratio to record 3.6 months of imports during the first half of FY 13/14 compared to 3 months of imports during the same period last year.

§ On the other hand, **services balance** deteriorated significantly by 95.5 percent to record a surplus of US$ 0.2 billion compared to a surplus of US$ 3.9 billion during the same period last year. This deterioration was driven mainly by an annual decrease of 66.4 percent and 18 percent in tourism receipts and other receipts, respectively.

§ Meanwhile, the surplus recorded in the **capital and financial account** was due to the following developments:

- The increase in **net foreign direct investments in Egypt** by 14.9 percent, recording a net inflow of US$ 2.8 billion (1 percent of GDP) during July-December 2013/2014, compared to US$ 2.5 billion during the same period last year.
- **Portfolio investments in Egypt** recorded a net inflow of US$ 1.2 billion (0.4 percent of GDP) during H1-FY13/14, compared to a net outflow of US$ 0.3 billion in H1-FY12/13,

due to the government issuance of bonds equivalent to US$ 1 billion, as a replacement for a Qatari deposit with the same value.

- The decrease in **liabilities of the CBE**, recording a net inflow of US$ 2.1 billion compared to a net inflow of US$ 3.4 billion during the same period last year, as CBE reimbursed part of the deposits that have been placed by some Arab countries (of which US$ 1 billion to Qatar).

Total number of tourists arrivals decreased slightly during the month of February 2014, reaching 617 thousand tourists compared to 642 thousand tourists in the previous month.

***NIR increased for the third month in a row..***

During March 2014, Net International Reserves (NIR) increased merely by US$ 0.1 billion to record US$ 17.4 billion, up from US$ 17.3 billion in February 2014, thus recording a y-o-y growth of 30 percent. The witnessed increase in March 2014 was mainly due to a 1.5 percent increase in foreign currencies (y-o-y growth by 52 percent). It is noteworthy that NIR has recorded a positive growth for the third month in a row, after a continuous decrease since July 2013. Moreover, the above-mentioned increase countered the fall in tourism revenues during the month of study, in addition to the increase in imports payments.