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Economic Conditions in Egypt: Current and Future

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Economic Conditions in Egypt: Current and Future

Gouda Abdel-Khalek

MEEA/AEA Panel

How to Transform the Arab Spring into Economic Spring? Challenges
and Opportunities

Contribution to MEEA/AEA Plenary Session

ASSA Meeting, Philadelphia, Jan. 2014

I-Introduction:

It was just an “apparently small” incident of a young man setting himself ablaze that eventually led to the downfall of several regimes across the Arab World. The “apparently small” incident of the Tunisian Mohamed Boazizi happened to trigger far-reaching consequences both in Tunisia and far beyond. And its impacts are still unfolding. This provides yet another interesting example of the “butterfly effect” of Chaos Theory.

The popular uprisings which started in Tunisia and Egypt in late 2010- early 2011 immediately following that “apparently small” incident represent something of tectonic proportions. In Egypt, Tunisia, and Yemen, we witnessed the downfall of several oppressive regimes that many thought were invincible. Within only three years, the Egyptians ousted two presidents and drafted two constitutions. And events are still unfolding.

Before the start of the revolution in Egypt, its polity experienced three inter-related crises: a crisis of distribution (absence of social justice as a result of non-inclusive growth), crisis of participation (characterized by the absence of democracy), and a crisis of legitimacy (Mubarak regime surviving only by political suppression and manipulating elections).

II- Current Economic Conditions:

Three years on, Egypt's economy is facing considerable challenges: sluggish growth, deteriorating internal and external balances, rising unemployment, and worsening social conditions. Add to that heightened popular expectations.

(i) Internal and external balance:

Currently, the Egyptian economy is suffering because of both external and internal shocks. External shocks are represented by the world food crisis of 2007-2008 and the global financial crisis of 2008. Internal shocks are represented by the January 25 popular uprising and the collapse of the Mubarak regime which resulted from it. Such negative shocks resulted in reduced foreign investment flows and exports, and at the same time raised imports. Public expenditure also rose on account of increased wages to satisfy demands by many groups for higher income. The outcome was slower growth of GDP and higher current account and budget deficits. (Table 1)

These internal and external shocks had significant effects on the main economic indicators (Table 1). Economic growth plunged to around 2% during 2010/2011-2012-2013, and is projected to be about 3% in 2013/2014. This contrasts with 6.2% for 2006-2010.

The current account deficit rose from 2.9% of GDP in 2010/2011 to 3.6% in 2013/2014. The rise in the budget deficit was even more pronounced, from 8.8% in 2010/2011 to 14% in 2012/2013. Although it fell by 1 percentage point in 2013/2014, it is still significantly above its level in 2010/2011. Domestic public debt rose as a proportion of GDP jumped by a staggering 15.2 percentage points, and foreign debt rose by more than three percentage points during the same period. Foreign reserves went down from about 3 months' worth of imports to 3 months' worth over the period. The result of these developments was increased pressure on the value of the Egyptian pound. Consequently, the country's sovereign credit rating was downgraded more than once.

(ii) Unemployment: The unemployment rate is now almost 13%. Although this unemployment rate is lower than in many countries (Figure 1), it is a record high by Egyptian standards. In addition, three factors magnify the unemployment problem in Egypt. First, no unemployment benefits are paid in Egypt's case to the unemployed. Second, the rate is the official figure, which underestimates unemployment. Third, according to expert opinion, the actual unemployment rate may be around 20%. Unemployment among the

Table (1)

Main Economic Indicators

	2010/11	2011/12	2012/13	2013/14
GDP Growth	1.8	2.2	1.8	2.8*
Inflation	11.1	8.6	6.9	10.3*
Budget Balance	-8.8	-10.8	-14.1	-13.1*
Current a/c	-2.9	-3.3	-2.9	3.6*
External Debt	14.8	13.4	16.2	18.0*
Public Debt	76.6	80.6	89.5	91.8*
Reserves	4.7	2.7	2.6	3.0*

* Preliminary estimates

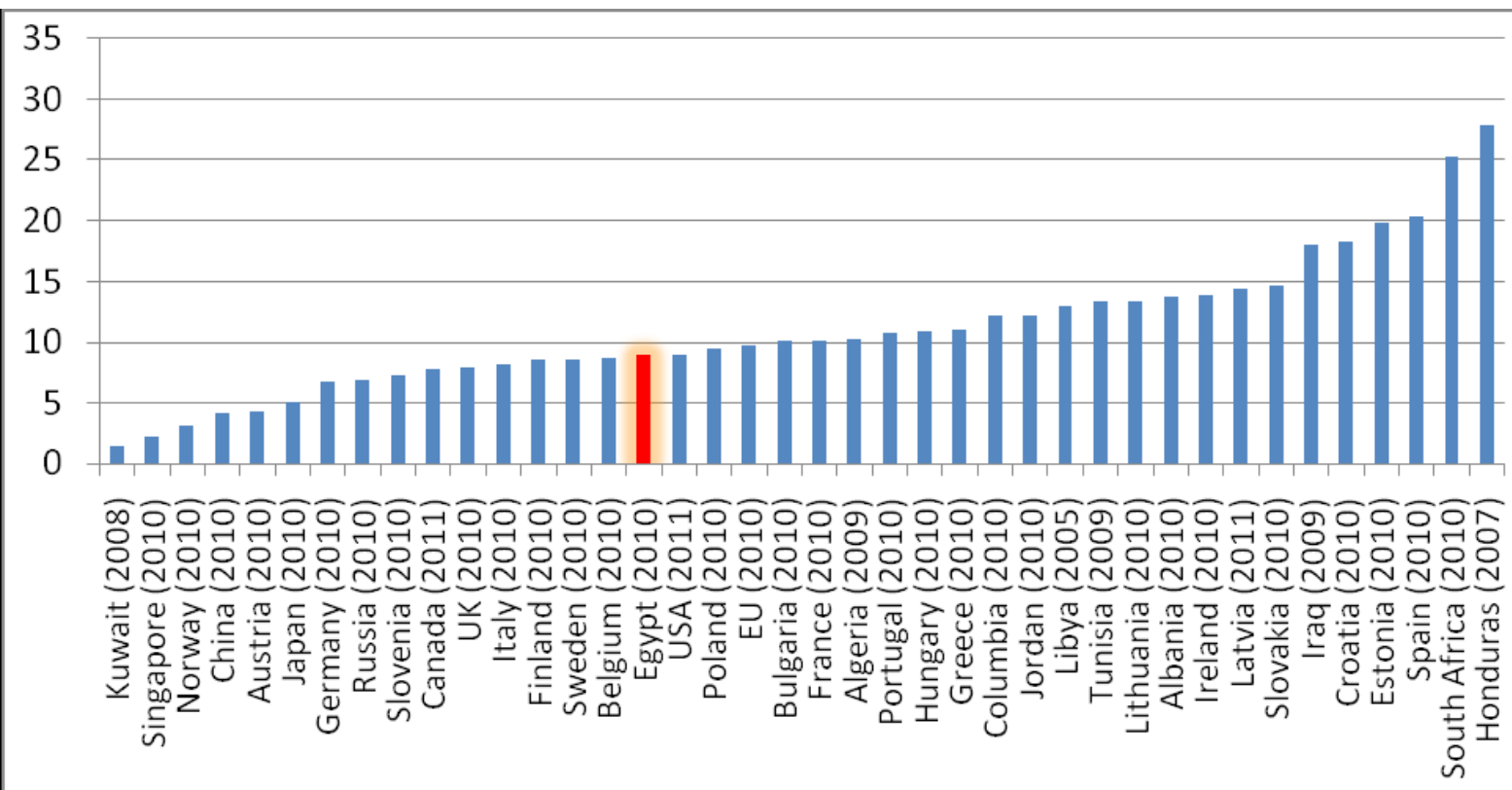
Source: Ministry of Finance.

youth (15-24 year old) is 30%, more than double the national average according to official data.

There really is a time bomb ticking here.

Figure (1)

Unemployment in Some Countries



(iii) Poverty: Measured by the national poverty line, poverty increased from 22% in 2010 to 25% in 2012. According to the World Bank poverty line of a dollar a day, the poverty rate has reached almost 40%.

The observed increase in the poverty rate after the January 25 revolution is the result of lower GDP growth rate, higher unemployment and higher inflation. Poverty is more widespread and intense in rural areas. About two thirds of the poor live in rural areas; most of those are in Upper Egypt. In Assiut, one of the governorates of Upper Egypt, the poverty rate is officially estimated at a staggering 58%. These facts underscore the significance of the spatial dimension of social justice in the case of Egypt. In essence, poverty means the lack of basics of life. Bread is the number one preoccupation of the poor. This is why the huge masses in Tahrir square on January 25 cried: “Breads... Freedom ...Social Justice”.

(iv) FDI inflows: Inflows of FDI to Egypt plunged by 90% in the first four months of 2011 immediately following the start of the revolution compared to the same period in 2010, as a result of the deterioration of the investment climate. In spite of government efforts to attract foreign investment inflow, it remains very low, against the backdrop of continued political instability.

III- Major Challenges:

1- Social Justice: In Tahrir square, the big cry was “social justice”. Consecutive governments grappled with conflicting approaches to addressing pressures for inclusive growth and demands for social justice.

Social justice does not only mean justice among social groups or classes, but it encompasses three dimensions.

- The horizontal dimension means equality between social groups or classes which live contemporaneously.
- The vertical dimension means equality between various generations or inter-generational equality.
- The spatial dimension means equality among various regions that constitute the country- for example rural and urban, north and south, east and west.

The last two dimensions are often neglected. In Egypt's case, with 52.2% of the population 25 year-old or younger and where poverty is located more in rural areas (especially Upper Egypt), social justice should top the list of public policy objectives. Consecutive governments declare the emphasis on social justice but continue to adopt a free market system. It is doubtful social justice can be achieved in a free market economy.

2- Privatization: Past privatization deals are subjects of debate, and even legal action to undo some of them (Omar Effendi and Steam Boilers companies). Issues of corruption and post-privatization foreign control of basic industries such as cement and banking occupy center stage. In such an environment, we witness a plethora of strikes: steel workers' strike, textile workers' strike, and other strikes are becoming almost daily occurrences.

3- The Rise of Political Islam: The Freedom and Justice Party (the political arm of the Moslem Brothers) and the Nour Party (the political arm of the Salafis Group) won a clear majority in the parliamentary elections which took place in early 2012, and a Moslem Brothers' president was elected in mid-2012. But the Moslem Brothers played factional politics, and failed miserably in running the economy. This sparked popular discontent. Many segments of the population, particularly the youth, were up against them. In the first (and also the last) year of Morsi's presidency, 9427 public protests took place for various reasons in various areas around the country; a historical record by Egypt's standards. Such protests climaxed on June 30th 2013, when at least 10 million Egyptians took to the streets and squares throughout the country, asking Morsi to leave.

Under the pressure of the masses, the army intervened. Morsi was ousted and replaced by the head of the constitutional court as temporary president, and a broad-based government was sworn in and a new road map was announced, stipulating writing a constitution then electing a new permanent president and parliament.

4- Democratic transition: is proving to be very difficult, in the absence of national consensus. Currently, Egypt is fiercely engaged in the task of writing a constitution- the second time around in just one year. A lot depends on the outcome of the referendum of 14-15 January.

5- Law and order: After the collapse of the Mubarak regime, law and order broke down almost entirely. Domestic security

continues to be a serious problem. It is one of the factors arresting economic recovery and holding back investment.

IV-Future Prospects:

It is my judgment that the prospects of the Egyptian economy are rather good, despite the negative aspects analyzed above. This is so for three reasons. First, Egyptians, thanks to the revolution, have been transformed from *subjects* to *citizens*. That should factor positively into economic performance. Second, the Egyptian economy did not suffer destruction as happened in other Arab Spring economies. Productive capacity is there, almost intact. Third, the Egyptian economy only needs recovery, not reconstruction.