The Egyptian Center for Economic Studies

Industrial Barometer

(April - June 1998)

Expectations in the Egyptian manufacturing sector

Industrial Barometer[1]
(April-June 1998)

OVERVIEW

The results of the new ECES survey of industrial expectations, *Industrial Barometer,* paint a promising picture for the Egyptian manufacturing sector in the coming six months. Most indicators of current business activity in the manufacturing sector, relative to the previous six months, reflect continued growth in the overall economy, with the public sector generally more upbeat than the private sector. Even more promising is that expectations for future activity are higher than current levels of activity suggesting increased overall economic growth.

While firms are generally optimistic about future growth and increasing sales and production, they expect lower employment levels. The survey results indicate that a generally stable output/final product price environment is prevailing, although manufacturers expect some wage and input price pressure. This suggests expectations of rising productivity or falling profit margins.

Despite increasing production and sales and high expectations for the coming six months, manufacturers indicate that they will not invest in extra capacity. Results show that for the majority of firms capacity utilization relative to the last six months is currently at normal or below normal levels, implying that the majority of firms still have spare capacity. Therefore, further growth in the manufacturing sector will not be fueled by increases in capital investment; rather, output is expected to grow as firms utilize more of their existing capacity.

Finally, there is little recorded difference between firms' expectations for overall economic growth and expectations for the performance of individual companies, implying that firms expect their fortunes to roughly follow economic growth rates. If anything, firms are marginally more optimistic about firm-level performance than they are about the overall performance of the economy.

[1] The ECES survey discussed here has benefited from the advice, comments and encouragement of Mauro Mecagni, resident representative of the International Monetary Fund in Cairo.

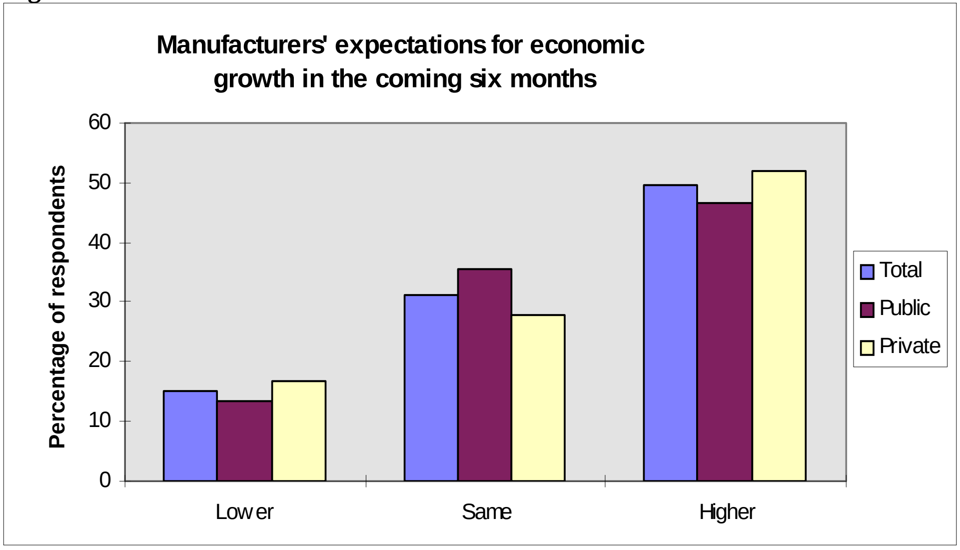
RESULTS[2]

Economic Growth

Results of the ECES survey of industrial trends show that approximately half of the businesspeople surveyed in manufacturing expect overall economic growth to accelerate over the coming six months (Figure 1). This supports a positive economic prognosis for Egypt in the later half of 1998.

According to industrialists, the pace of economic growth is expected to pick up throughout the rest of this year after stagnating the past six months. A slower pace of growth in the last six months may have been responsible for a lack of obvious price pressure on final goods. The higher growth expected in the next six months, however, should not put any apparent pressure on prices of final goods. This implies that there is still slack in the economy. Evidence of this emerged from the survey with 70 percent of firms reporting that they are operating at normal or below normal capacity.

Figure 1



Levels of Activity

The ECES survey aims to capture trends in sales, production, inventories, investment and capacity utilization in the manufacturing sector. When the surveyed firms were asked about their businesses' performance in the last six months, the results indicated that the net percentage of firms reporting growth in production over those reporting declines was 21 percent (Figure 2). Responses about sales in the last six months also suggest that growth has continued for the manufacturing sector. About 39 percent of those firms surveyed reported increases in sales, compared to 23 percent reporting decreases. More than 50 percent of firms in the food, beverage and tobacco; ready-made garments and transportation equipment sectors reported higher production and sales, and expect even higher growth in the next six months. The printing and shoe manufacturing sectors, however, buck this general trend with more than 50 percent of firms reporting lower sales and production over the past six months. In terms of inventories, the number of firms reporting an increase in stock (25 percent) was only marginally lower than those reporting decreases (26 percent), implying that firms are generally satisfied with their inventory levels and do not plan to meet future growth in sales by reducing their inventories.

[2] Methodology of the survey and a copy of the questionnaire used are included in an appendix following the results.

Despite increasing production and sales and expectations of even higher levels in the coming six months, manufacturers indicate that they will not invest in extra capacity in that period. Seventy percent of firms report that their capacity utilization relative to the last six months is currently normal or below normal implying that the majority of firms still have spare capacity; this will reduce pressure to increase capital investment. Therefore, further growth in the manufacturing sector will not be fueled by increases in capital investment with 67 percent of firms expecting no change in capital investment. Rather, output is expected to grow as firms utilize more their existing capacity.

In line with expectations for faster economic growth in the coming six months, a large percentage of the companies surveyed (48 percent) report that they expect levels of activity to increase. Only 9 percent indicate that they expect production levels to decline. Following this trend, of all of the firms surveyed 40 percent said that they expected sales to international markets to increase in the coming six months whilst 50 percent replied that they expected sales in domestic markets to increase over the same time period.

Figure 2

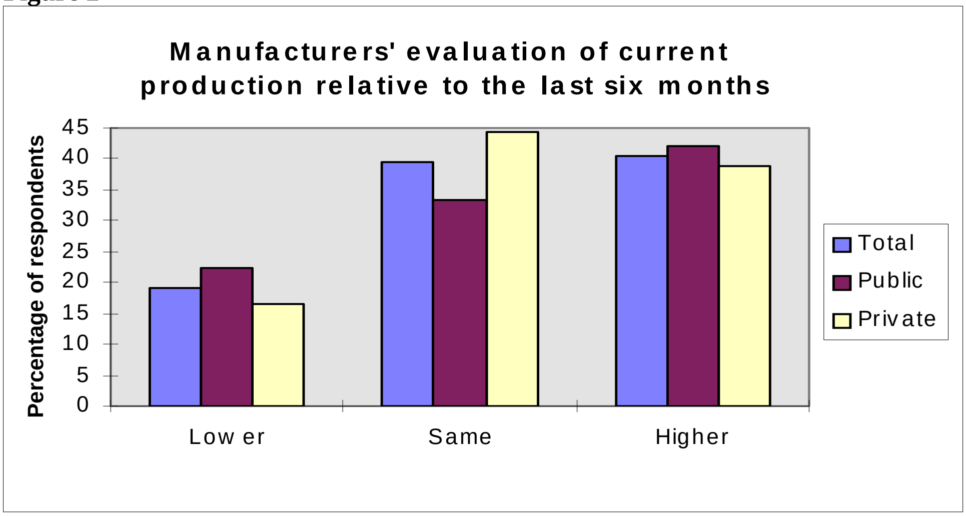


Figure 3

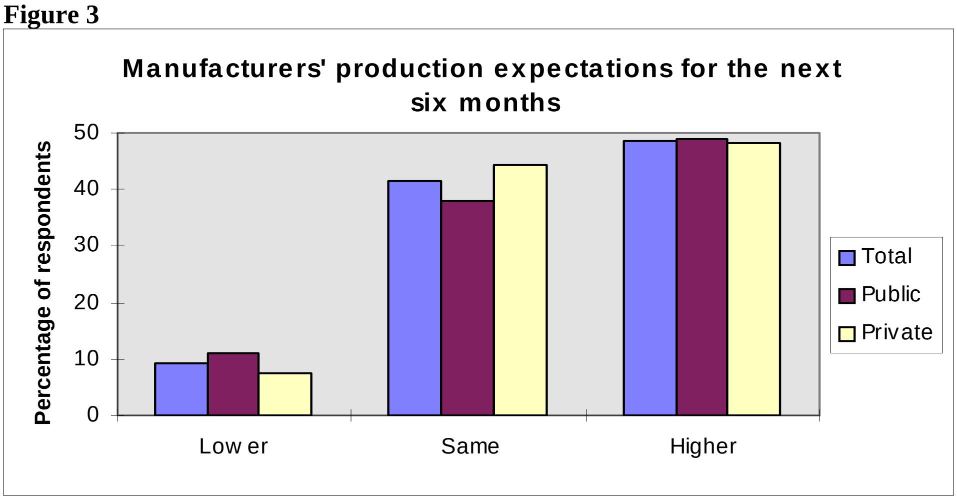


Figure 4

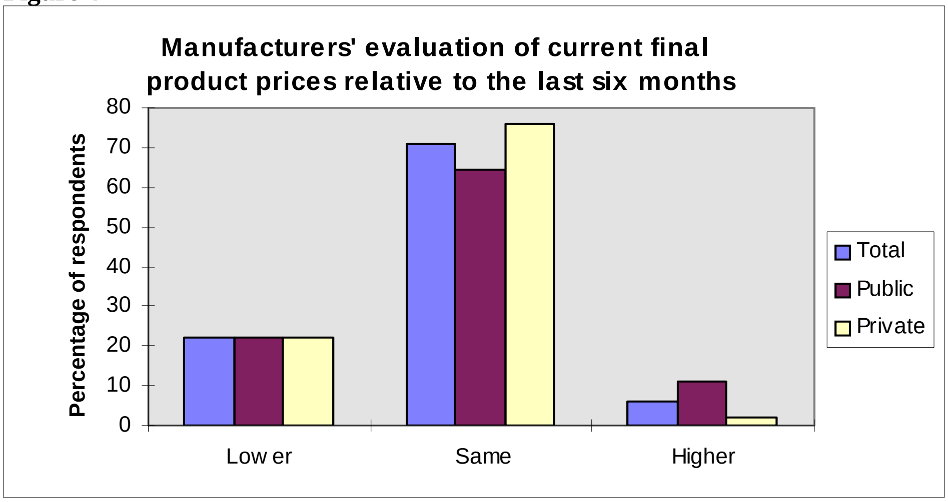
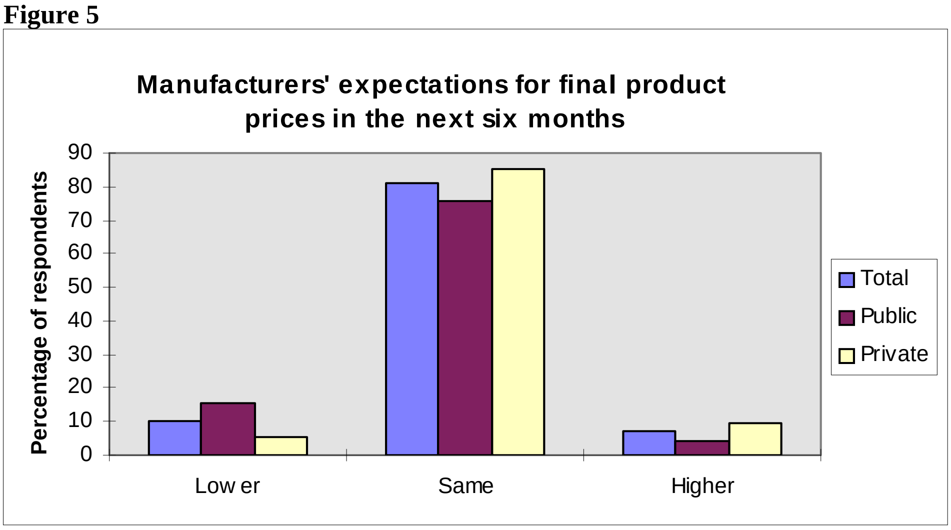


Figure 5



Prices

Over the last six months, there has been downward pressure on output prices, according to the manufacturing sector in ECES' industrial survey. The percentage of firms with declining final product prices (22 percent) was larger than the percentage of those indicating increases (6 percent). In the next six months, final product prices are expected to remain stable according to 81 percent of the firms surveyed. Firms anticipating price increases in inputs and wages (26 and 44 percent respectively), however, outnumber those anticipating declines (13 and 4 percent respectively).

Wages and Employment

In contrast to expectations for final product and input prices, a large percentage of the companies surveyed (48 percent) expected wages to rise in the coming six months. More public sector firms (57 percent), than private firms (33 percent), expect wages to rise. In terms of the manufacturing industry's total wage bill, this upward pressure may be offset by the fact that 40 percent of companies surveyed reported that they expect the number of people they employ to fall over the coming six months. The drop in employment may be attributed to a reduction in the number of people employed in public enterprises due to the Early Retirement Scheme (ERS),[3] especially in the food, spinning and weaving,

[3] Recently, Dr. Atef Ebeid, minister of the Public Enterprise Sector, stated that the early retirement scheme will be implemented in 80 public sector companies starting July 1998. He said that these companies will be offered for sale after implementing the early retirement scheme on them. (*Al Akhbar*, 25/6/1998).

printing, chemical and basic metal subsectors. Employment in the private sector is expected to remain — on balance — the same in the coming six months. Fifty-six percent of the surveyed firms reported that employment levels will stay the same, 22 percent expected higher employment levels, and another 22 percent reported lower expected employment. The private sector industries that expect to increase their employment are the beverage and tobacco, spinning and weaving, and non-metal mining sectors.

According to the survey results, rising wages are not expected to translate into inflationary pressure but rather rising productivity, especially in public sector companies that are rationalizing employment through ERS schemes and reducing underemployment. Some of the expected wage increases are due to rising competition for skilled labor in manufacturing subsectors such as food, chemicals, and transportation equipment.

Wage pressures were reported in all subsectors, but especially in spinning and weaving, non-metal mining products, and the transportation equipment subsectors. These are generally the same sectors that are expecting to increase employment. Plans to increase wage levels are, in many cases, accompanied by plans treduce the number of people employed in the public sector. As noted above, while the reduced number of employees may be attributed to the ERS, increased wages are believed to be adjustments to real wage levels that declined throughout the 1990s.[4] In the private sector, the expected rise in wage levels suggests that certain subsectors, especially in the food sector, which have expanded production and expect this expansion to continue, are facing increased competition for skilled personnel.

Constraints

The ECES survey focused on constraints to production and did not address general constraints to business (see questionnaire). The purpose of this focus was to determine if certain factors of production were causing bottlenecks, and thereby help us to anticipate changes in price levels and employment. This survey did not address some of the most often cited constraints, such as tax laws.

A large number of firms (46.9%) reported that they face no constraints to production at the current time. While this may seem to contradict other business surveys which have highlighted a number of constraints to businesses, including the constraints included in our list (see questionnaire), a closer look at the results and at the sample shows that these results are not in fact out of line with other research. First, the ECES survey relied on the largest firms in each industry in order to capture as much of the trends in production as possible. Since large firms tend to have less constraints than small firms, the sample is biased. Furthermore, the incidence and severity of constraints are not uniform across sectors and do not mirror results of other formal and informal surveys.

The constraints most often cited are: lack of skilled labor force, poor market demand, and limited access to credit. The sectors that are facing the severest constraints in the public sector are spinning and weaving and ready-made garments businesses, while in the private sector, the companies that are facing the most stringent constraints are the food; spinning and weaving; shoe, leather and leather products; and transportation equipment manufacturers.

Since this is the first ECES *Industrial Barometer*, there is no benchmark against which to measure whether the severity of constraints has changed in the face of new government policies and procedures. Future surveys will gauge the progress being made in alleviating some of these constraints.

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[4] Radwan, Samir "Towards Full Employment: Egypt into the 21st Century," ECES Distinguished Lecture Series no. 10, January 1998.

TABLE 1: ECES INDUSTRIAL BAROMETER RESULTS, APRIL - JUNE 1998

Evaluation of present levels of activity relative to last six months[1]

(In percent of total responses, n=99)

	Public and Private Companies				Public Companies				Private Companies			
	Higher	Same	Lower	Net Balance[3]	Higher	Same	Lower	Net Balance[3]	Higher	Same	Lower	Net Balance[3]
Sales	39	37	23	16	38	40	22	16	41	35	24	17
Production	40	39	19	21	42	33	22	20	39	44	17	22
Final product prices	6	71	22	-16	11	64	22	-11	2	76	22	-20
Inventories	25	45	26	-1	20	49	27	-7	30	43	26	4
Level of capacity utilization[2]	23	49	21	2	27	44	22	4	20	54	20	0

Manufacturers' expectations for the next six months[1]

(In percent of total responses, n=99)

	Public and Private Companies				Public Companies				Private Companies			
	Higher	Same	Lower	Net Balance[3]	Higher	Same	Lower	Net Balance[3]	Higher	Same	Lower	Net Balance[3]
Economic growth	49	31	15	34	47	36	13	33	52	28	17	35
Output												
Domestic sales	51	32	16	34	60	27	13	47	43	37	19	24
International sales	40	34	15	25	49	33	11	38	33	35	19	15
Production	48	41	9	39	49	38	11	38	48	44	7	41
Prices												
Final product prices	7	81	10	-3	4	76	16	-11	9	85	6	4
Input prices	26	60	13	13	31	56	11	20	22	63	15	7
Wages	44	52	4	40	58	36	7	51	33	65	2	31
Inputs												
Employment	13	44	42	-29	2	31	67	-64	22	56	22	0
Investment	27	68	0	27	20	78	0	20	33	59	0	33

1. Items may not add up to 100 percent because of omission by respondents.
2. Higher = approaching full capacity, Same = normal capacity utilization, Lower = below normal capacity utilization.
3. Net balance represents the percentage of respondents indicating an increase minus the percentage of respondents indicating a decrease.

APPENDIX

Methodology

In an effort to track and monitor trends in the Egyptian economy, ECES discovered that data on the financial side of the economy was widely available and its timeliness and accuracy had improved dramatically over the last few years. There is, however, a lack of timely real-side data reflecting trends in individual sectors. In order to gather information on entrepreneurs' perspectives of industrial trends, ECES sought to provide this data by conducting a survey targeted at certain sectors/industries. This will ultimately aid ECES in developing output indices for a number of sectors based on information gathered about past and present demand and supply elements, expectations about future orders, prices, and so on.

The survey concentrated on the industrial sector, mainly manufacturing, and excluded construction, petroleum, agricultural and service activities which can be monitored by other means. Selecting the sample was broken down into three stages. First, the value-added contribution of each major subsector to manufacturing was calculated, including the relevant public/private split within each subsector. Secondly, the number of public and private firms needed from each subsector was calculated, based on an initial sample size of 165, in order to complete our sample.[5] Finally, large firms were chosen on the assumption that they contribute the most value added to the industrial sector as a whole across different subsectors.

Ninety-nine firms, out of an original sample of 165 in 11 industrial sectors, responded between April and June of 1998.[6] The survey elicited responses on current levels of activity, prices, inventories and capacity utilization relative to the previous six months, and expectations about output and input prices, final product demand, wage and employment trends, the changing nature of constraints on business as well as overall economic growth. Firms were requested to indicate an increased, decreased or unchanged level of activity for each indicator. Of all the firms that responded, the response rate was above 90 percent for all but one indicator, international sales, due to the fact that some firms are not engaged in external trade.

The *ECES Industrial Barometer* was conducted as a means of gaining information to make assessments and predictions about the Egyptian economy. As a new industrial survey of input and output expectations of its kind in Egypt, it has certain methodological weaknesses. In future surveys, ECES will improve the rigor of the overall approach and increase the sample size to ensure greater coverage of the manufacturing sector and industrial sector.

[5] The initial survey size of 165 firms was selected as a realistic and relevant initial sample.

[6] Using the same classification categories of the Ministry of Planning, the manufacturing sectors covered were: food; beverages and tobacco; spinning and weaving; ready-made clothes; printing; shoes; leather and leather products; chemicals and chemical-related products; non-metal mining products; basic metal products; and transportation equipment.

Questionnaire

Business Survey

Enterprise name: ---------------------- **Year of foundation:---------------**
Nature of Activity: -------------------- **Number of Employees: ----------**
Date of interview: ---------------------

1. Relative to the last six months (the last six months refers to October through March),

are your sales: ☐ higher ☐ normal ☐ lower
is your production: ☐ higher ☐ normal ☐ lower
did prices for your products: ☐ rise ☐ stay the same ☐ fall
did your inventories: ☐ rise ☐ stay the same ☐ fall
has your capacity utilization been:
☐ below normal ☐ normal ☐ approaching full capacity

2. Is your production currently constrained: ☐ yes ☐ no

If yes, please rank on a scale from 0 to 4 the following constraints to your production process, where 0 indicates not a constraint and 4 refers to severe constraints.

	0	1	2	3	4
insufficient demand					
insufficient capital					
insufficient access to imports					
insufficient skilled workforce					
insufficient access to credit					
other factors (please specify)					

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3. In the next six months expect (the next six months refers to April through October) , do you expect,

your sales in the domestic market to: ☐ rise ☐ stay the same ☐ fall
your sales in international markets to: ☐ rise ☐ stay the same ☐ fall
your production to: ☐ rise ☐ stay the same ☐ fall
prices for your products to: ☐ rise ☐ stay the same ☐ fall
prices for your inputs to: ☐ rise ☐ stay the same ☐ fall
wages to: ☐ rise ☐ stay the same ☐ fall

4. In the next six months (the next six months refers to April through October), are you planning to:

☐ increase your work force ☐ maintain your workforce unchanged
☐ decrease your workforce
☐ increase capital investment ☐ maintain capital investment unchanged

5. In the next six months expect (the next six months refers to April through October), do you expect the economy to grow:

☐ faster ☐ at the same rate ☐ slower