



The Egyptian Center for Economic Studies



Industrial Barometer
January 1999

Expectations in the Egyptian Manufacturing Sector

M MARKET RESEARCH & DEVELOPMENT
MARKETEERS

بارومتر الصناعة

يناير 1999

Introduction

This is ECES' second issue of its new *Industrial Barometer*, published in the summer of 1998, building on the success of the first issue. The *Barometer* seeks to provide and analyze real side economic data on the current state of Egypt's industrial sector. For each issue ECES conducts a survey of industrial firms in Egypt to evaluate their business and economic expectations in the coming six months. In this second survey, conducted between October and December of 1998, the sample increased to 200 firms in 11 industrial sectors, of which 138 responded.

In this *Industrial Barometer*, we examine the performance of the Egyptian manufacturing industry over the last six months and look at the prospects for the first half of 1999. Moreover, industrialists' business expectations as polled in last issue's survey are compared to actual economic performance in an effort to gauge how closely expectations were actually realized. In addition, expectations from the last survey are compared to current expectations to see if Egypt's business community has become more or less optimistic about economic performance given recent economic events.

Overview

Latest results paint a robust picture of the Egyptian manufacturing sector.

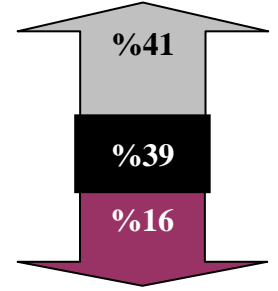
Despite the recent turbulence that has been experienced, especially in global financial and commodity markets, the results of the latest ECES *Industrial Barometer* paint a reasonably robust picture of the Egyptian manufacturing sector over the latter half of 1998. According to the manufacturing firms surveyed, economic growth in Egypt continued to advance in the last half of 1998, but at a slower pace than firms had previously expected. Nevertheless, a large percentage of manufacturers (41.3 percent) expect economic growth to accelerate in the coming six months, whereas a much smaller percentage (15.9 percent) expect lower growth rates.

Current performance indicators are up but short of previous expectations

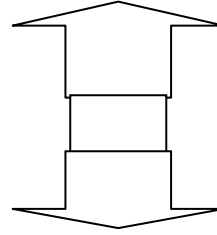
In general, manufacturers reported positive developments in most performance indicators over the last half of 1998, although as reported in the April-June 1998 survey, there were marked differences compared to manufacturers' expectations for the last half of 1998. In this second survey, evaluations of sales activity over the last six months show that, on balance, sales activity was lower

التوقعات ليناير - يونيو 1999

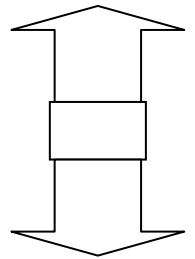
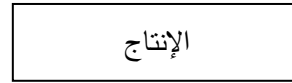
النمو الاقتصادي



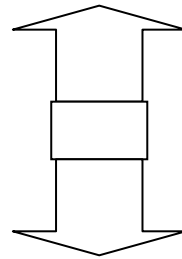
المبيعات في الأسواق العالمية



الإنتاج



أسعار السلع النهائية



than expected in both domestic and international markets with the public sector faring worst. When the surveyed firms were asked about their production levels over the last six months, the net percentage of those reporting increases over those reporting declines was 25.4 percent compared to a net balance of 39 percent of respondents in the April-June survey who expected production to rise.

Private sector employment prospects turn optimistic

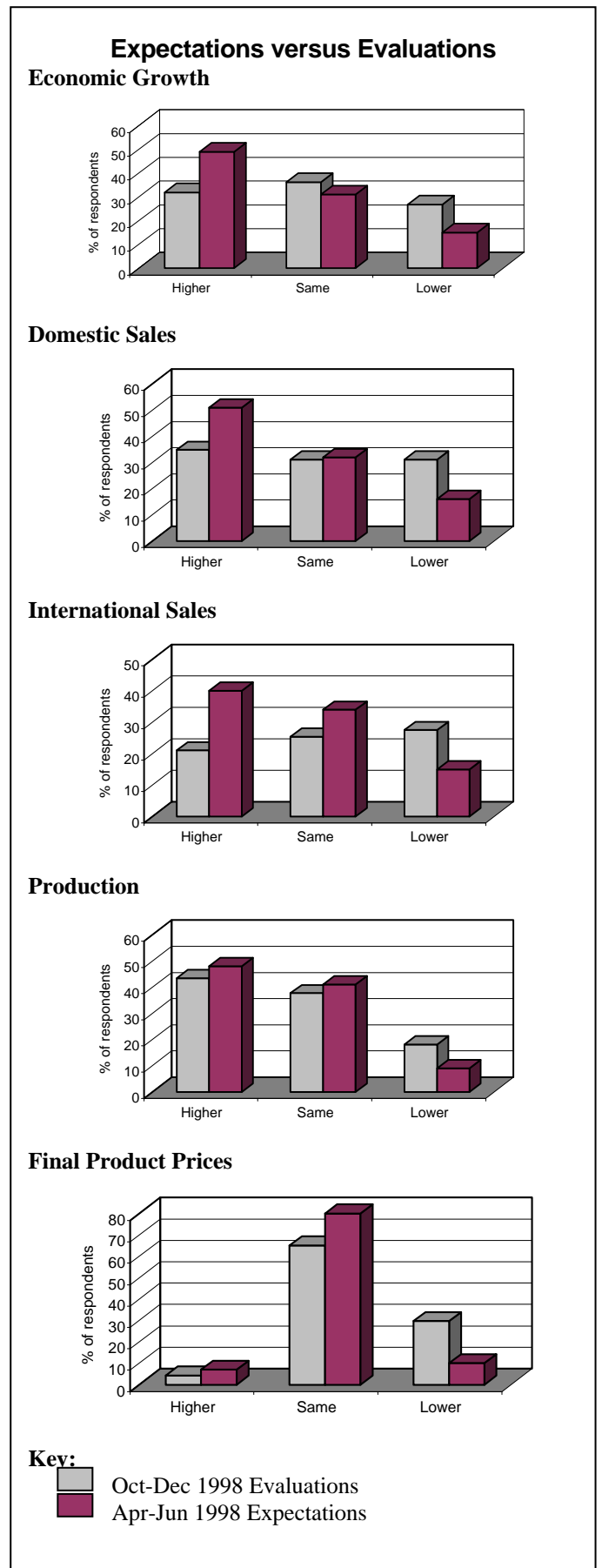
According to the manufacturing firms polled in the second survey, there is a stable price environment in Egypt, despite the fact that wage costs continue to rise. Although firms are expecting to pay higher costs for wages in the first half of 1999, not all firms are expecting to reduce or maintain their workforce at current levels. Over the coming six months, public sector firms are forecasting reductions in their workforces, while the private sector, which was forecasting no changes in employment in the previous survey, is now, on balance, expecting to increase employment over the coming six months.

Economic Growth

Economic growth over the second half of 1998: slower than expected

One of the most interesting findings of this edition of the *Industrial Barometer* is the difference between what actually occurred on the economic scene and what manufacturers previously expected for the second half of 1998 as measured in the previous survey. Evaluations of economic growth over the second half of 1998 show that manufacturers' expectations as recorded in the previous survey fell well short of actual end of year evaluations which are reported in this new survey. While close to half the respondents (49 percent) expected the pace of economic growth to increase over the second half of 1998 only 31.9 percent report that it actually has increased (See data tables for more detail about the spread of responses).

Interestingly, ECES' most recent survey shows that firms' current expectations for the first half of 1999 are generally lower than their expectations were for the latter half of 1998 (Expectations for the latter half of 1998 were published in the April-June survey). This is because a large number of companies' expectations have shifted and they are now expecting the Egyptian economy to continue growing at its present rate, rather than at any faster or slower rate. Nevertheless, expectations for economic growth over the coming six months are still positive. The net balance of firms expecting higher economic growth is



25.4 percent (41.3 percent of firms that responded expect higher economic growth in the first half of 1999, while nearly 16 percent indicated that they expected lower growth levels), with public sector firms slightly more optimistic than the private sector. Therefore, there are few signs of the manufacturing sector predicting recession or slowdown in growth; rather industrialists expect steady growth rates over the course of the coming year.

Levels of Activity

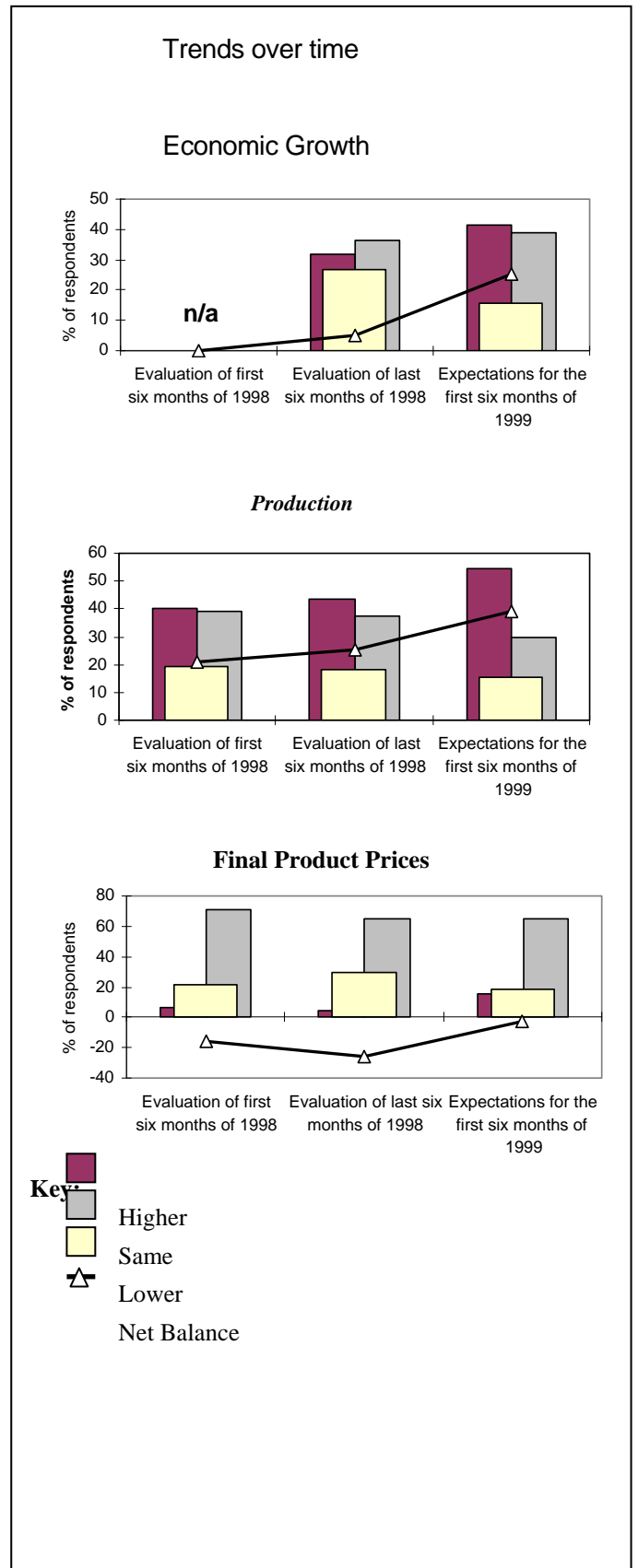
Production: an upward trend

ECES' evaluation of sales activity over the last six months shows that, on balance, sales activity was lower than firms expected six months ago in both domestic and international markets with the public sector faring worst. Moreover, when surveyed firms were asked about their production levels over the last six months, the net percentage of those reporting increases over those reporting declines was 25.4 percent compared to a net percentage of 39 percent of respondents in the April-June 1998 survey who expected increases in production. Among the industries surveyed, the food, beverage and tobacco industries reported a much higher than average increase in production and sales and are optimistic about growth in the coming six months. Conversely, the spinning and weaving, shoe and leather industries are reporting more negative results and are generally pessimistic about the prospect of any improvement in their market outlook over the coming six months.

Reflecting general production trends over the final six months of 1998, more firms (43.5 percent) reported increases in production than those reported decreases (18.1 percent). This is similar to results from the previous survey which showed a similar spread of responses (40 percent of firms reported increases compared to 19 percent reporting decreases) implying that growth in production over the past six months has been similar to growth in the first part of 1998. Over the second half of 1998, production gains were stronger in the private sector whose net balance was 36.6 percent compared to a net balance of 13 percent in the public sector. The increase in production relative to sales has led to increased inventories in the private sector and a slight increase in the level of capacity utilization.

Domestic and international sales activity: lower than expected

Despite their increasing production, firms reported that overall domestic sales have, on balance, grown marginally over the second half of 1998, while international sales have dropped. This is understandable given the turbulence in the global economy over the last few months, and



supports the fact that economic growth has continued in Egypt, though at a similar rate of growth to the previous period.

Breaking down the survey results into public and private components sheds more light on the prevailing economic climate in Egypt and shows that the private sector has been performing much better than the public sector in terms of sales to both domestic and international markets. In the public sector, the number of firms reporting increases in domestic and international sales (26.9 and 17.9 percent respectively) was significantly lower than those reporting decreases (35.8 and 25.4 percent respectively) relative to six months ago. Meanwhile, in the private sector, 42.3 percent of the firms report higher domestic sales compared to 26.8 percent indicating decreases over the last six months of 1998. Possibly due to prevailing global economic conditions, sales to international markets did not fare as well as those to domestic markets with the number of private firms reporting decreases in sales (29.6 percent) being larger than those reporting increases (23.9 percent).

Sales and production: expected improvements

Looking forward to the coming six months of 1999, higher sales and production levels are expected with a large percentage of all firms surveyed (54 percent) reporting that they expect production to increase. Only 15 percent of the companies polled indicated that they expect production levels to decline.

Investment: tempered by spare productive capacity

Despite these positive expectations, the majority of manufacturers (67 percent) indicate that they will not invest in extra capacity in the first half of 1999. New investment will continue to be tempered by excess productive capacity with 71 percent of the firms surveyed indicating that the current capacity utilization is normal or below normal. Therefore, as discussed in the last *Industrial Barometer*, further growth in the manufacturing sector will not necessarily be fueled by expansionary capital investment (67 percent of firms expect no change in capital investment). Rather, any growth in investment is expected in the form of new projects primarily.

Prices

Lower prices for final goods, moderate increase in input costs

The survey results indicate a strong downward trend in the price of final goods, marking an increasingly competitive environment in Egypt. At the same time, there remains

upward pressure on the price of inputs which, in combination with lower-than-expected sales, implies that profit margins have been slimmer over the past six months. The chemicals sector witnessed the largest fall in final product prices with a full 59 percent of firms surveyed reporting declining prices, compared to a sample average of 29.7 percent indicating that final product prices have fallen. It seems that falling final product prices in the chemical sector have been aided, in general, by declining prices of raw materials.

Wage costs continue to rise

Survey results indicate that wages continued to rise over the last six months at a rate faster than previously expected. Wages are expected to continue to rise in the first half of 1999 with close to 57 percent of companies expecting to pay higher wages. This trend is more prominent in the private than the public sector with 71 percent of private firms expecting to pay higher wages over the first six months of 1999 compared to only 40 percent of public firms. Higher wages in the private sector could be explained by forecast increases in employment.

Private sector employment: forecasts turn optimistic

Tempered optimism is also evident in firms' forecasts for employment growth in their companies. Although firms are expecting to pay higher costs for wages over the coming six months, not all firms are expecting to reduce or even just maintain their workforce at current levels. In contrast, the private sector, which was forecasting no change in employment in the previous survey, is now expecting to increase employment over the coming six months (31 percent of the private firms expected employment to increase in the coming six months, compared to only 8.5 percent that expected to reduce their workforce). Bucking this trend in the private sector is the chemicals industry, which expects no increase in employment. Continuing a trend observed in the April-June 1998 *Industrial Barometer*, public sector firms are still forecasting similar reductions in their workforce in the coming six months.

Constraints

Weak market demand: a common constraint to production

A high percentage of the surveyed firms (63.8 percent) reported facing at least one constraint to production. This is a much higher percentage than in the previous survey, where slightly less than half of the firms reported experiencing some constraints. Overall, more public (69

percent) than private (59 percent) sector firms face constraints, although the private sector firms that do face constraints to production report more severe constraints.

Over the past six months, the most commonly cited constraint to production has been low market demand. This was the only constraint consistently cited by both public and private firms. Some firms blamed dumping by foreign producers and increasing competition from imports for the lack of demand for Egyptian products. This is consistent with the survey results showing lower sales and slower economic growth compared to the last half of 1998.

The sectors that are facing acutely insufficient market demand are spinning and weaving, shoe, leather and leather products, and non-metal mining products. The chemical industry, especially the private sector, is suffering from lack of skilled labor and having access to credit, this in addition to weak market demand.

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 data on entrepreneurs' perspectives of industrial trends, ECES conducted 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.

Both the first and second surveys concentrated on the industrial sector, mainly manufacturing, and excluded construction, petroleum, agriculture, and service activities, which can be monitored by other means. Selecting the sample was done in 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 the sample size, in order to complete our sample. 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.

In the current survey, out of a sample of 200 firms in 11 industrial sectors, 138 responded between October and December of 1998. Using the same classification categories of the Ministry of Planning, the manufacturing sectors surveyed 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. 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 of 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 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 in the process of anticipating changes in price levels and employment. Therefore, this survey did not address some of the most often-cited constraints in the general business environment, such as tax laws.

Additionally, the ECES survey relies on the largest firms in each industry, in terms of employment, in order to capture as much of the trends in production as possible. Since large firms tend to have fewer 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 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. ECES is committed to improving the rigor of the overall approach and increasing the sample size in each subsequent survey to ensure greater coverage of the manufacturing sector and industrial sector. The next *Industrial Barometer* survey will take place in the months of April-June 1999 with the results due to be published in July 1999. ECES would like to thank all the companies that participated and those readers who sent their comments and suggestions. ECES has tried to incorporate their feedback into this survey and would welcome any further comments or suggestions.

Questionnaire

Data Tables