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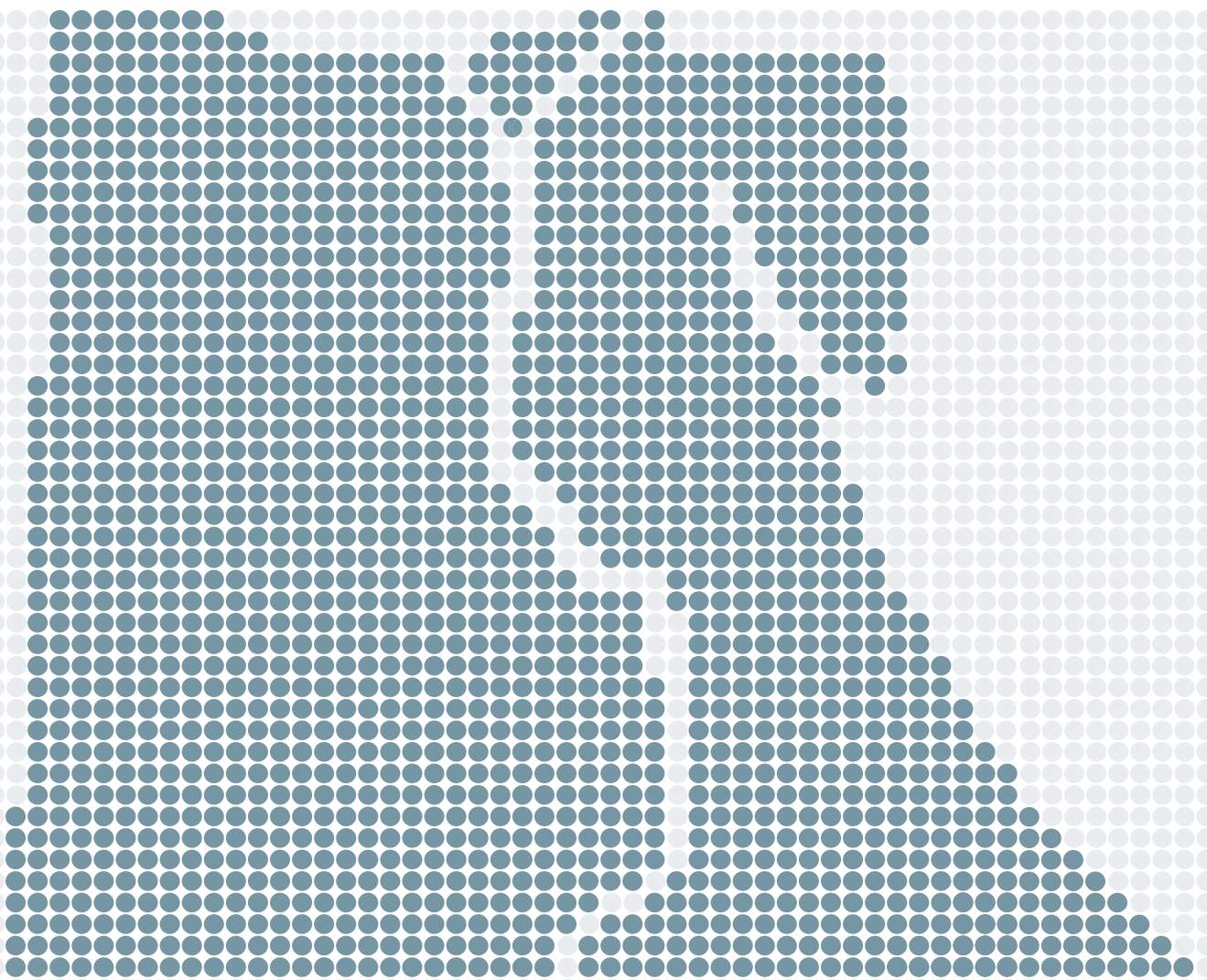
The Egyptian Center
for Economic Studies

COMMITTED TO SHAPING EGYPT'S ECONOMIC FUTURE

Business Barometer

Issue 37

2015



Performance & Expectations of the Egyptian Business Sector

Committed to Shaping Egypt's Economic Future

The Egyptian Center for Economic Studies is an independent Egyptian think tank that promotes sound public and private policymaking through high quality, innovative research and informed public debate, committed to prosperity, social equity, open society and global integration.

About the Business Barometer

In an attempt to provide timely information about the state of economic activity in Egypt, ECES published the first issue of the Industrial Barometer in 1998. The periodical reported the results of a biannual survey of 165 firms fully drawn from the industrial sector. However, to improve the depth of the report, the survey was expanded in the July 2000 issue to include 35 firms from the construction sector. This step converted the former Industrial Barometer into today's Business Barometer. The survey was further expanded in the July 2002 issue to include 10 firms from the tourism sector. In July 2006, the survey was expanded again to include a total of 320 firms (from 210). In July 2007, another 154 firms were added to the sample. These firms cover the transportation, communications and financial sectors. The new sample includes a total of 474 firms. Starting July 2011, the Business Barometer is based on a modified sample survey in terms of firm size, comprising 218 large firms, 57 medium firms and 199 small firms. Firm size is determined by the number of employees as per CAPMAS classification, with the number of employees in small firms ranging between 5-49; in medium firms between 50-99; and in large firms more than 100. Starting January 2013, the Business Barometer includes an index aimed at summarizing the results of the survey and tracking business environment changes over time. The index is calculated for large firms as well as SMEs, once for evaluation of performance and once for expectations. Starting with Issue No. 34, the Business Barometer reports quarterly results for the firm sample.

This edition of the Business Barometer reports the results of a stratified sample of 474 public and private firms. The surveyed firms cover manufacturing (50 percent), financial intermediation (13 percent), construction (12 percent), transportation (11 percent), tourism (8 percent), and communications (6 percent). The survey is conducted across a number of small, medium and large enterprises (42, 12 and 46 percent, respectively). The survey covers their assessment of economic growth and the results of their operations over the last quarter of FY2014/2015 in terms of production, sales, capacity utilization, inventories, prices, wages, employment and investments. It also summarizes their expectations for overall future economic performance as well as their own activities for the first quarter of FY2015/2016.

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Business Barometer

Issue No. 37 - 2015

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List of Abbreviations

BB	Business Barometer
BBI	Business Barometer Index
FY	Fiscal Year
1HFY	First Half of Fiscal Year
2HFY	Second Half of Fiscal Year
Q1FY	First Quarter of Fiscal Year
Q2FY	Second Quarter of Fiscal Year

Overview

This edition of the *Business Barometer* (BB) presents the survey results of a stratified panel of 474 firms regarding their perceptions about the performance of the Egyptian economy and their own business for the fourth quarter of FY14/15 (April-June 2015) and their outlook for the first quarter of FY15/16 (July-September 2015), respectively.¹ The business community is starting the new fiscal year with high expectations about the recovery of the Egyptian economy, as reflected in their outlook for economic growth for the upcoming quarter July-September 2015. This optimistic outlook is in line with the steady recovery of real GDP growth during 2014 and a meager decline in unemployment (Figure 1.1), in addition to the government's target to achieve a growth rate of no less than 5 percent in FY15/16.

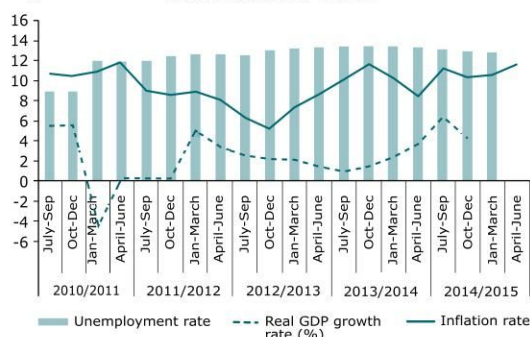
On the fiscal front, despite the increase in tax revenues by 39 percent in January-March FY14/15 compared to the corresponding quarter in the previous year, the fiscal deficit is still high. This can be attributed to lower grants from the Gulf states and increase in expenditures by 17 percent to reach 9 percent of GDP in January-March FY14/15 compared to the same quarter in the previous year. Public debt is declining but remains high, reaching 96.4 percent in the quarter January-March FY14/15 compared to 101.3 percent in January-March FY13/14 (Figure 1.2). The deficit is mainly financed domestically through T-Bill issuance that has been on an upward trend, reaching LE 508.4 million in January-March FY14/15, which crowds out the credit available to the private sector (Figure 1.3).

The government continues to perform fiscal consolidation measures targeting a deficit of 8.9 percent of GDP in FY15/16. These measures include the implementation of the VAT, the gradual phasing out of fuel subsidies and the full implementation of the mining and quarrying law after the issuance of its executive regulations. Accordingly, public debt for FY15/16 is targeted to reach 90-91 percent of GDP.

Externally, the pound witnessed further depreciation against the US dollar to reach LE 7.73 in July 2015—a depreciation of 8 percent since July 2014. While this recent depreciation could support export competitiveness and attract further investments and capital inflows, it may pose inflationary pressures if the import bill increases as a result. It is noteworthy that the current account balance deteriorated during January-March FY14/15 to register a deficit of US\$4.1 billion from a surplus of US\$0.32 during the corresponding period in FY13/14, driven mainly by a decline in oil exports and net official transfers.

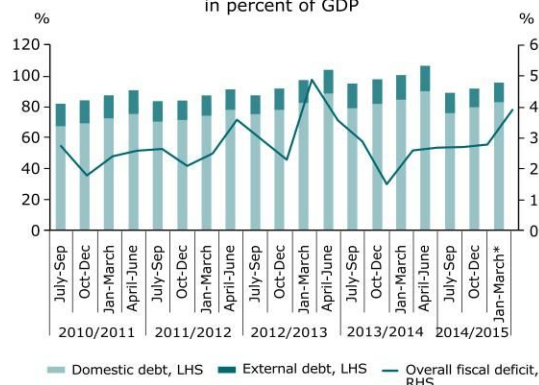
¹ It is important to note that this Business Barometer survey was conducted before the assassination of the chief state prosecutor on June 29th and the multiple simultaneous assaults on Egyptian security checkpoints in northern Sinai on July 1st.

Figure 1.1: Real GDP Growth, Unemployment and Inflation Rates



Sources: Ministry of Planning; CAPMAS and Central Bank of Egypt (CBE), Monthly Statistical Bulletin, Various Issues.

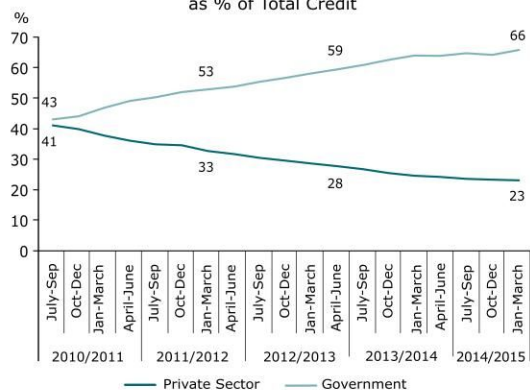
Figure 1.2: Public Debt and Fiscal Deficit in percent of GDP



Source: Central Bank of Egypt (CBE), Monthly Statistical Bulletin, Various Issues.

* Provisional data for domestic and external debt.

Figure 1.3: Domestic Credit by Sector as % of Total Credit



Source: Central Bank of Egypt (CBE), Monthly Statistical Bulletin, Various Issues.

Figure 1.4: Net International Reserves and Exchange Rate (LE/\$)



Source: Central Bank of Egypt (CBE), Monthly Statistical Bulletin, Various Issues.

Past Performance of Businesses

According to the Business Barometer Index (BBI), overall business performance during April-June FY14/15 witnessed an improvement by only one point, mainly among large firms while the performance of SMEs stayed the same. Firms' performance was mainly characterized by a wait-and-see strategy preceding the approval of the budget of the upcoming fiscal year and consequent economic policies and measures.

Despite the recovery of real GDP growth and improved business sentiment in recent months, firms' assessment of economic growth remains constant during April-June FY14/15 compared to the previous quarter. On the contrary, an increase in production has been reported thanks to an improvement in domestic and international sales accompanied by a modest decline in inventory. This pattern has been witnessed by both large firms and SMEs. Firms' capacity utilization and investment remained similar to the last quarter, which was reflected on the employment level that was kept more or less unchanged. This indicates that firms have not yet benefited from the steady economic recovery and real GDP growth achieved during the previous period. Lower oil prices have led to a decline in energy costs, which translated into lower input prices and final product prices during the quarter under study. SMEs reported a larger decline in intermediate input prices compared to large firms.

Sectorally, the tourism sector registered the best performance followed by the transportation and construction sectors. The tourism sector reported the highest capacity utilization in April-June FY14/15—an increase of six points compared to the previous quarter. This improved performance is due to the increase in the number of tourist arrivals and number of tourist nights, registering a growth of 11 percent and 26 percent, respectively in April 2015 compared to March 2015.

In the manufacturing sector, the food industry witnessed an improvement in the overall business performance due to an increase in the domestic sales during the period of Ramadan. This has been reflected on an increase in the food production level. Conversely, the textiles sector has seen a decline in its overall performance in light of decreased levels of domestic and international sales, which have been reflected on lower production levels.

Figure 2.1: Business Barometer Index



Figure 2.2: Economic Growth

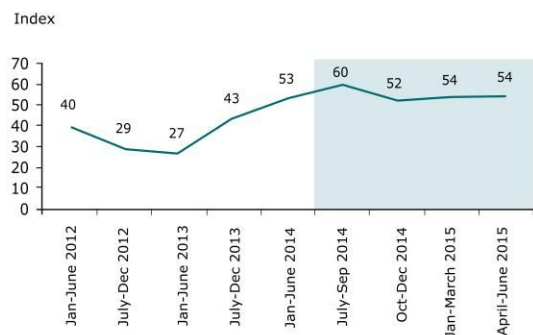


Figure 2.3: Production



Figure 2.4: Domestic Sales



Source: Survey results.
 The shaded area refers to quarterly data, while the plain area refers to bi-annual data.

Figure 2.5: International Sales

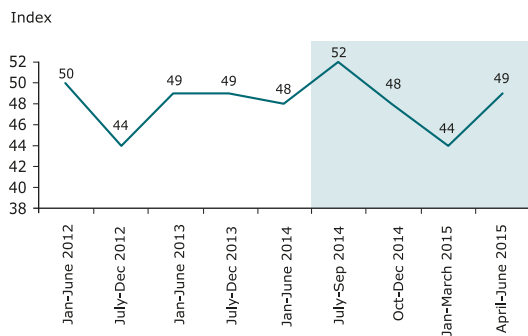


Figure 2.9: Input Prices**

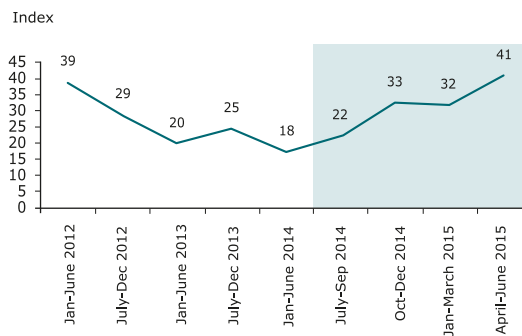


Figure 2.6: Inventory*

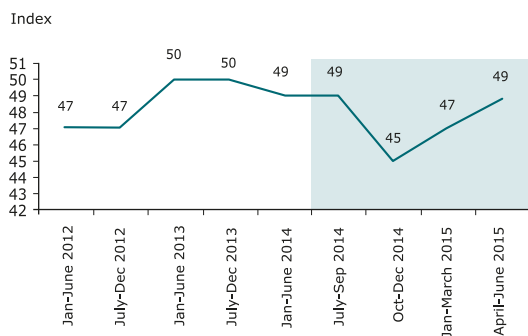


Figure 2.10: Wages

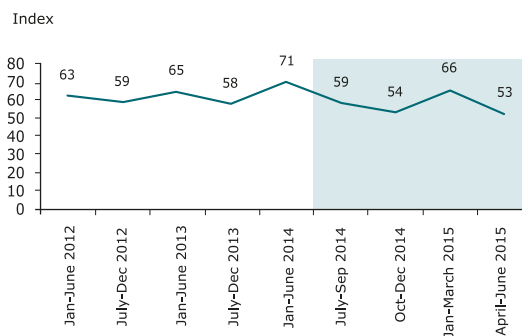


Figure 2.7: Capacity Utilization

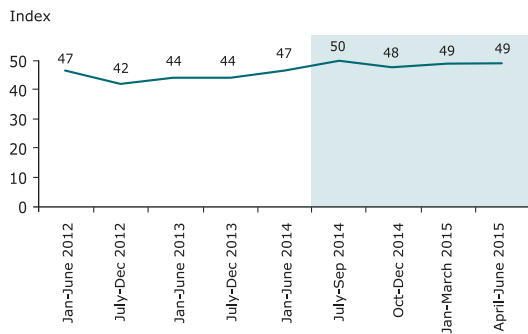


Figure 2.11: Investment

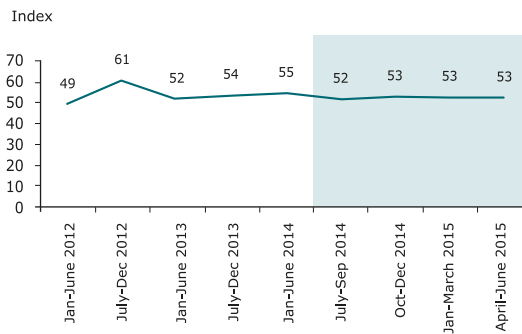


Figure 2.8: Final Product Prices

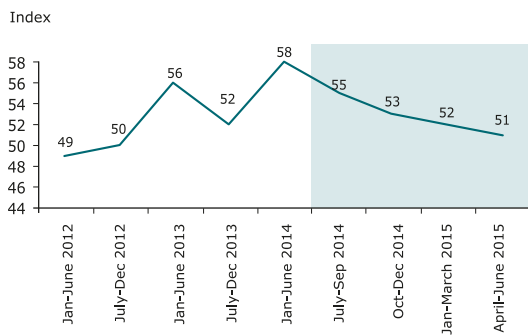
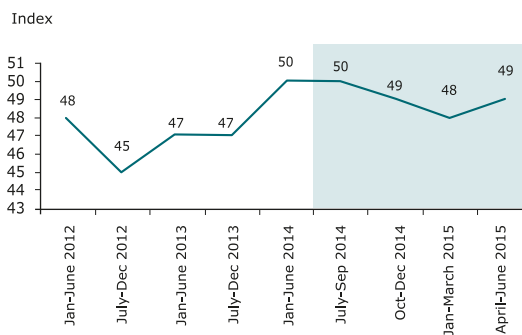


Figure 2.12: Employment



Source: Survey results.

* The index for inventory is inverted to indicate the negative impact of its increase on businesses. Hence, a higher inventory index indicates lower inventory.

** The index for input prices is inverted to indicate the negative effect of the increase of input prices on businesses. Hence, a lower value of this index indicates higher input prices.

■ The shaded area refers to quarterly data, while the plain area refers to bi-annual data.

Business Strategy Going Forward

Firms' outlook for the coming quarter July-September FY15/16 is high, yet generally lower than the outlook for the previous quarter. Firms still have confidence in the economy's ability to rebound, evidenced by their high expectations for economic growth. Ongoing economic reforms, the newly approved budget and the inauguration of the new Suez Canal in August have been manifested on firms' optimism regarding economic growth. On the micro level, although firms' outlook is lower than in the previous quarter, firms still plan to increase production to meet expected domestic demand, in favor of a decrease in inventories.

Firms are not planning to increase their exports in the upcoming period due to difficulty in importing the necessary raw materials— a result of difficulties encountered in opening a letter of credit for imports due to the CBE enforced cap on dollar deposits to curb the black market. Firms anticipate no change in input prices, which induces also similar expectations for final product prices. For the third consecutive quarter, firms' outlook for investment remains unchanged (or declined slightly), which reflected on their employment outlook as well. In other words, their general optimism has not yet been manifested on their investment levels. Among all sectors, firms in the tourism sector expressed the most a positive expectations for the coming quarter. Such optimism was reported prior to the terrorist attacks. Contrary to their performance in the previous quarter, financial intermediaries expressed a positive outlook with the government decision to suspend the controversial capital gains tax for two years. On the other hand, recent government plans to reduce internet prices may have affected communications firms' outlook, expressing the least optimism. Manufacturing firms, especially in the textile sector, were also more conservative regarding the coming quarter than the previous one.

Generally, there are no significant differences in outlook between large firms and SMEs. However, for economic growth, SMEs outlook seems to be less optimistic than that of large firms, in line with SMEs moderate past performance. Also, SMEs expect less inventory and better capacity utilization for the coming quarter.

Figure 3.1: Business Barometer Index



Figure 3.2: Economic Growth

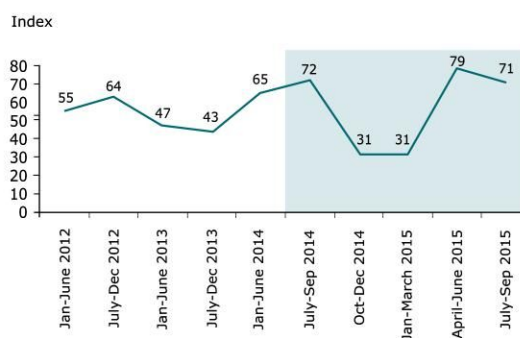


Figure 3.3: Production

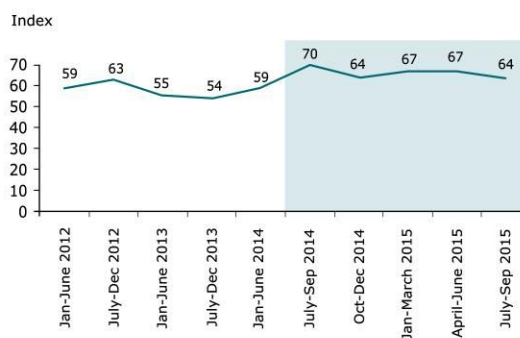
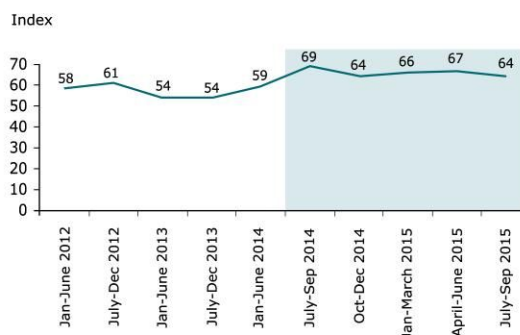


Figure 3.4: Domestic Sales



Source: Survey results.
 The shaded area refers to quarterly data, while the plain area refers to bi-annual data.

Figure 3.5: International Sales

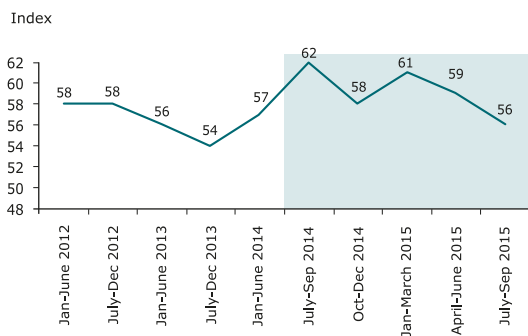


Figure 3.9: Input Prices**

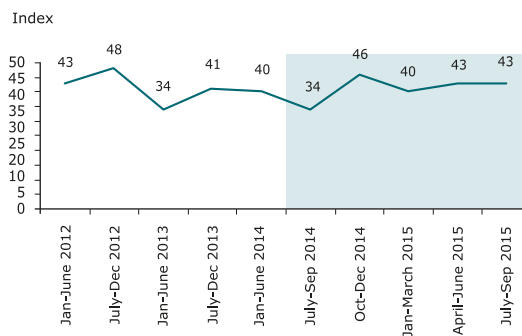


Figure 3.6: Inventory*

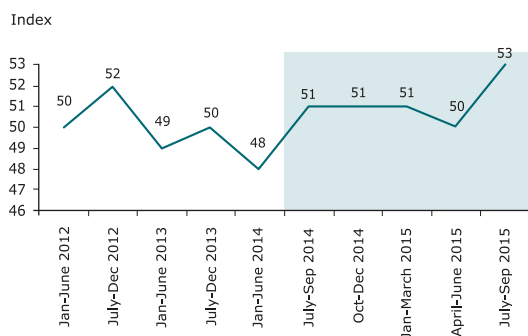


Figure 3.10: Wages

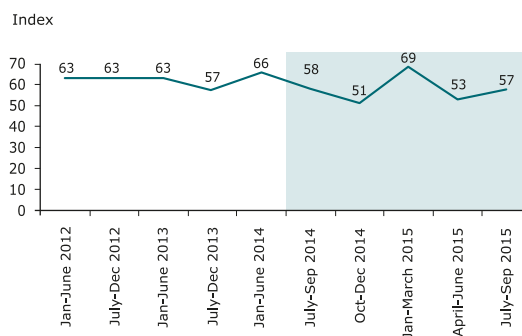


Figure 3.7: Capacity Utilization

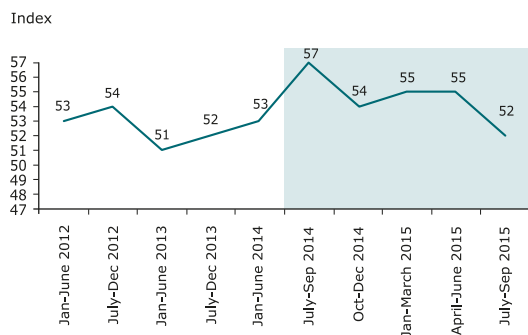


Figure 3.11: Investment

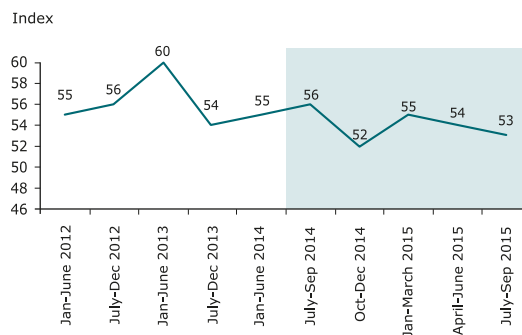


Figure 3.8: Final Product Prices

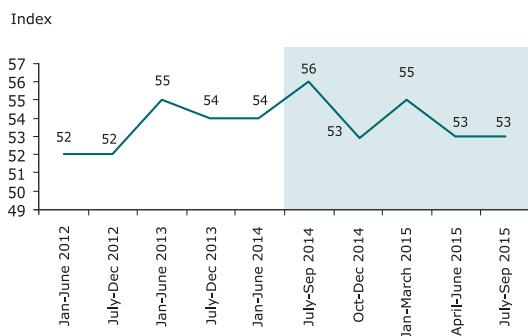
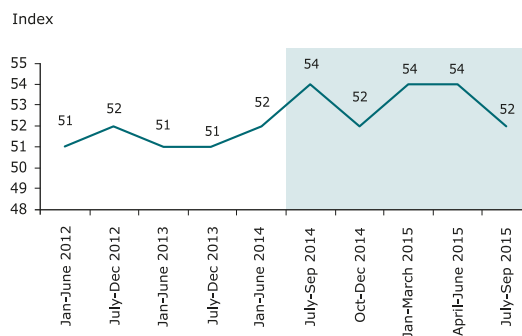


Figure 3.12: Employment



Source: Survey results.

* The index for inventory is inverted to indicate the negative impact of its increase on businesses. Hence, a higher inventory index indicates lower inventory.

** The index for input prices is inverted to indicate the negative effect of the increase of input prices on businesses. Hence, a lower value of this index indicates higher input prices.

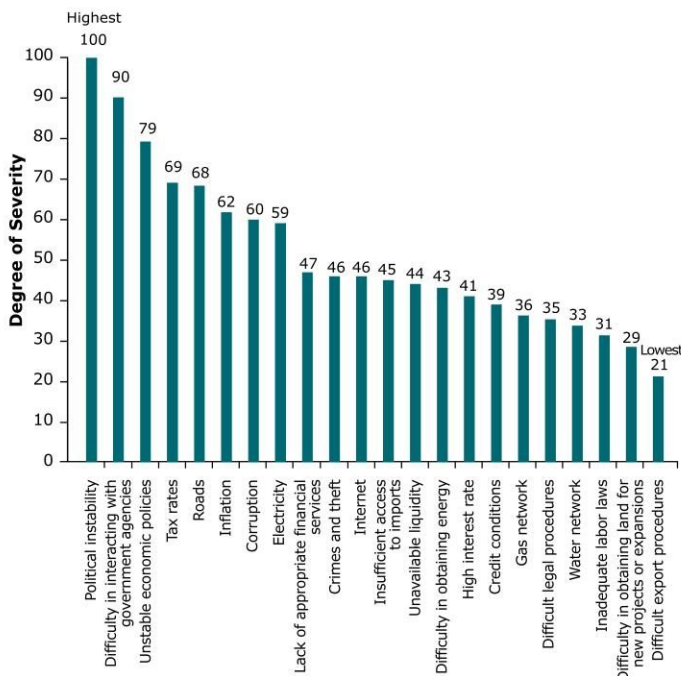
■ The shaded area refers to quarterly data, while the plain area refers to bi-annual data.

Business Constraints

Major Constraints: Political instability, dealing with government agencies, unstable economic policies and tax rates

As shown in Figure 4, government policies are by far the most severe business impediments, followed by poor infrastructure (roads, electricity and the internet). Unstable economic policies and tax rates are deemed significant business constraints due to hesitance of the government in taking economic decisions. Access to imports has become a modestly severe business constraint after being the least severe in October-December 2014. Insufficient access to imports might be the result of curbing the black market of the US dollar and the depreciation of the Egyptian pound.

Figure 4: Major Constraints Facing the Business Sector (Normalized index of severity)



Source: Survey results.

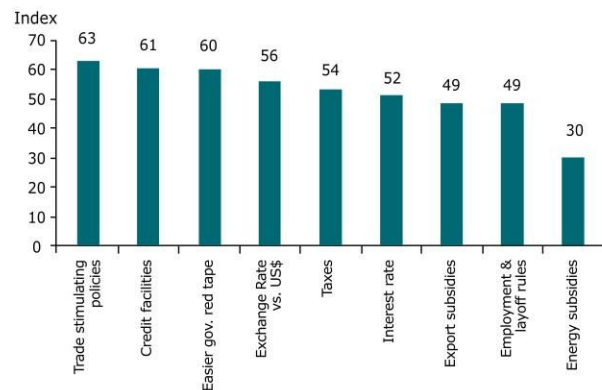
Policy Expectations

More trade stimulating policies and easier government regulations

As revealed by Figure 5, firms tend to anticipate that policies would remain unchanged in the upcoming quarter compared to the previous quarter. However, the index shows that firms expect more credit facilities and trade stimulating policies. This expectation coincided with the increase in budgeted export subsidies to reach LE 5 billion in the new budget of FY15/16, up from LE 2.6 billion in the previous year. As

firms cited difficulty in dealing with government agencies as a major business impediment, easier government regulations is highly expected. In contrast, firms expect lower energy subsidies, which is in line with the government's new target to cut the budget deficit to 8.9 percent in FY15/16.

Figure 5: Policy Expectations



Source: Survey results.

Appendix

Following an elaboration of the methodology used in calculating the index, this appendix will present tables that give a numerical representation of survey results.

Methodology of the Index

The index aims at calculating a single figure for the responses of firms on each variable.

The index's equation is:

$$X = \frac{I+S}{100+S} \times 100,$$

where *I* is the share of firms reporting an increase and *S* the share of firms reporting same.

The index is designed to have a maximum of 100 when all firms report an increase, a minimum of 0 when all firms report a decrease and a middle value of 50 when all firms report no change. Between 0 and 100, the index grows proportionally with larger shares of "increase," and inversely with larger shares of "decrease," while the change in "same" is given less effect by including it in the numerator and the denominator. A higher index thus reflects a better business climate and vice versa. It is worth noting that the index is inverted for inventories and input prices as increases of these two variables reflect an adverse business climate for firms. The Business Barometer Index is a simple average of the variables' indexes, calculated once for large firms and once for SMEs, both for evaluations and expectations.

Table A1. Survey Results: Summary of all Firms Past Performance by Sector (April-June 2015)¹

Indicator	Manufacturing Sector			Construction Sector			Tourism Sector			Transportation			Communications			Financial Intermediaries									
	Percentage Higher 35	Percentage Same 43	Percentage Lower 22	Index ² Higher 50	Percentage Higher 44	Percentage Same 51	Percentage Lower 23	Index ² Higher 63	Percentage Higher 48	Percentage Same 30	Percentage Lower 23	Index ² Higher 60	Percentage Higher 26	Percentage Same 56	Percentage Lower 19	Index ² Higher 53	Percentage Higher 25	Percentage Same 54	Percentage Lower 21	Index ² Higher 51	Percentage Higher 27	Percentage Same 44	Percentage Lower 29	Index ² Higher 47	
Economic growth	35	43	22	55	44	51	5	63	48	30	23	60	26	56	19	53	25	54	21	51	27	44	29	49	
Business activity																									
Production	34	44	22	54	35	49	16	56	48	20	33	57	39	43	19	57	14	61	25	47	19	32	48	39	
Domestic sales	34	44	22	54	35	49	16	56	41	33	26	56	34	45	21	54	14	61	25	47	19	32	48	39	
International sales	18	55	26	47	0	80	20	44	43	24	33	54	30	53	18	54	0	100	0	50	14	71	14	50	
Inventory	18	69	13	49	0	100	0	-	0	100	0	-	0	100	0	-	0	0	0	0	0	0	0	0	-
Level of capacity utilization	9	77	14	49	4	93	4	50	15	83	3	54	0	94	6	48	0	96	4	49	11	73	16	49	
Prices																									
Final product prices	11	83	6	51	4	89	7	49	15	75	10	51	28	67	6	57	0	89	11	47	6	90	3	51	
Intermediate input prices	35	62	3	40	35	64	2	40	38	60	3	39	11	89	0	47	43	57	0	36	25	75	0	43	
Wage level	12	87	1	53	5	95	0	51	13	88	0	54	15	83	2	54	29	71	0	58	8	87	5	51	
Primary inputs																									
Investment	11	88	1	53	15	84	2	54	10	90	0	53	4	93	4	50	7	86	7	50	15	85	0	54	
Employment	6	84	10	49	11	80	9	51	15	78	8	52	7	85	7	50	11	79	11	50	2	90	8	48	

Table A2. Survey Results: Summary of all Firms Outlook by Sector (July-September 2015)¹

Indicator	Manufacturing Sector			Construction Sector			Tourism Sector			Transportation			Communications			Financial Intermediaries									
	Percentage Higher 63	Percentage Same 29	Percentage Lower 8	Index ² Higher 56	Percentage Higher 64	Percentage Same 29	Percentage Lower 7	Index ² Higher 72	Percentage Higher 80	Percentage Same 18	Percentage Lower 3	Index ² Higher 83	Percentage Higher 50	Percentage Same 39	Percentage Lower 11	Index ² Higher 64	Percentage Higher 50	Percentage Same 39	Percentage Lower 11	Index ² Higher 64	Percentage Higher 68	Percentage Same 23	Percentage Lower 10	Index ² Higher 57	
Economic growth	63	29	8	71	64	29	7	72	80	18	3	83	50	39	11	64	50	39	11	64	68	23	10	74	
Business activity																									
Production	47	46	8	64	47	51	2	65	60	25	15	68	46	52	2	64	39	54	7	60	52	48	0	68	
Domestic sales	48	44	7	64	47	51	2	65	51	32	16	63	38	60	2	61	39	54	7	60	51	49	0	67	
International sales	22	68	10	54	0	100	0	50	55	45	0	69	28	69	3	57	0	100	0	50	20	80	0	56	
Inventory	9	74	17	52	0	100	0	50	0	83	17	55	0	100	0	50	0	0	0	0	0	100	0	50	
Level of capacity utilization	17	78	5	53	4	96	0	51	13	83	5	52	2	98	0	51	0	100	0	50	11	87	2	52	
Prices																									
Final product prices	9	89	3	52	22	78	0	56	20	75	5	54	19	81	0	55	7	93	0	52	6	94	0	52	
Intermediate input prices	25	74	1	43	45	55	0	35	23	75	3	45	0	100	0	50	54	46	0	32	21	79	0	44	
Wage level	25	75	0	57	35	65	0	61	28	73	0	58	9	91	0	52	14	86	0	54	24	76	0	57	
Primary inputs																									
Investment	11	88	1	53	22	78	0	56	8	93	0	52	2	98	0	51	11	89	0	53	11	87	2	52	
Employment	11	86	3	52	15	84	2	54	13	88	0	54	6	94	0	52	21	75	4	55	8	92	0	52	

¹ Numbers represent percent of total responses. Higher, same and lower may not add up to 100 due to rounding.

² Equal to the simple average of the variables' indexes. The index's method of calculation is provided in the appendix.

Table A3. Survey Results: Summary of Business Sector Past Performance (By Size)(April-June 2015)¹

Indicator	SMEs			Large				
	Percentage Higher	Percentage Same	Percentage Lower	Index ²	Percentage Higher	Percentage Same	Percentage Lower	Index ²
Economic growth	27	45	28	50	43	46	11	61
Business activity								
Production	24	41	36	46	44	43	13	61
Domestic sales	23	41	36	45	42	46	12	60
International sales	16	55	29	46	28	51	21	52
Inventory	19	72	9	47	15	68	17	51
Level of capacity utilization	6	80	14	48	10	84	6	51
Prices								
Final product prices	13	77	9	51	8	89	3	51
Intermediate input prices	34	65	2	41	29	69	2	42
Wage level	16	83	2	54	8	91	1	52
Primary inputs								
Investment	9	88	2	52	12	87	1	53
Employment	6	83	11	49	8	85	7	50

¹ Numbers represent percent of total responses. Higher, same and lower may not add up to 100 due to rounding.

² Equal to the simple average of the variables' indexes. The index's method of calculation is provided in the appendix.

Table A4. Survey Results: Summary of Business Sector Outlook (By Size)(July-September 2015)¹

Indicator	SMEs			Large				
	Percentage Higher	Percentage Same	Percentage Lower	Index ²	Percentage Higher	Percentage Same	Percentage Lower	Index ²
Economic growth	59	33	9	69	67	25	8	74
Business activity								
Production	45	48	7	63	52	43	5	66
Domestic sales	45	49	7	63	50	45	5	66
International sales	25	70	5	56	28	65	7	56
Inventory	6	76	18	53	11	74	14	51
Level of capacity utilization	13	84	4	53	11	87	2	52
Prices								
Final product prices	12	85	3	52	12	88	0	53
Intermediate input prices	28	71	1	42	23	76	0	43
Wage level	18	82	0	55	31	69	0	59
Primary inputs								
Investment	8	92	0	52	15	84	1	54
Employment	11	88	1	53	11	86	2	52