ECES
The Egyptian Center for Economic Studies

Business Barometer
Issue 39   2016

Performance & Expectations of the Egyptian Business Sector

About ECES

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 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 (1 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 second quarter of FY 2015/2016 in terms 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 third quarter of FY 2015/2016.

From the ECES Board of Directors

Omar Mohanna, *ECES Chairman, and Chairman, Suez Cement Group of Companies*

Mohamed Taymour, *ECES Vice Chairman, and Chairman, Pharos Holding Co. for Financial Investments*

Tarek Zakaria Tawfik, *ECES Secretary General, and Managing Director, Cairo Poultry Group (CP)*

Alaa Hashim, *ECES Treasurer, and Chairman, Transcendium*

ECES Team

Dr. Abla Abdel Latif, *Executive Director and Director of Research*

Magda Awadallah, *Deputy Director for Finance and Administration*

Mohsen Adel, *Consultant*

Maye Ehab, *Economist*

Markos Magdy, *Research Analyst*

Kadry Sayed, *IT Manager*

Yasser Selim, *Managing Editor*

Fatema Ali, *Translator/Editor*

Contents

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 assessment of their own business for the second quarter of FY15/16 (October-December) and their outlook for the third quarter of FY15/16 (January-March). In this quarter, the Business Barometer Index (BBI) has dropped two points, reflecting the business community's concerns about the Egyptian economy's slow recovery. These concerns are in line with the decline in real GDP growth rate in July-September FY14/15, which reached 3.1 percent from 5.6 percent in the same quarter in the previous year. The results of this edition of BB are also in line with the decline in the previous edition, ringing an alarm for the government to revisit its policies in an effort to stimulate the economy.

Concerning fiscal outturns, the government reported a deficit of 2.8 percent of GDP in the quarter July-September 2015/2016, a decline from 3.64 percent in the previous quarter FY 14/15. Similar to the previous quarter, the deficit was mainly financed domestically through T-bill issuance, crowding out the private sector in the access to credit (Figure 1.3). By securing loans from the World Bank and the African Development Bank, the government will work on reducing the budget deficit by 3-4 percent over the next four years, a decline from a two-digit figure in the previous period, and cut expenditure on fuel subsidies by 30 percent.

At the external front, international reserves declined to reach US$16 billion in October-December 2015/2016 compared to US$18 billion in July-September 2015/2016. The decline has been the result of repayment of US$1.25 billion in September 2015 upon maturity of US dollar denominated notes issued in 2005 (This affected the end of period values for Q1 FY15/16). The Egyptian pound has depreciated to reach LE7.9/$ for the period October to November compared to LE7.8/$ in the quarter July-September 2015/2016. It is noteworthy that the current account balance deteriorated during July-September 2015/2016 to register a deficit of US$3.9 billion compared to US$1.6 billion during the corresponding quarter in 2014/2015.

The exchange rate pass-through effect and higher fruit and vegetable prices were the main drivers of the increase in inflation rate. However, the government managed to control inflation through restricting imports of certain products and providing cheaper substitutes for the basket of goods. The rate increased to reach 10.614 percent in October-December 2015/2016 compared to 10.35 percent in the same quarter in the previous year.

In July-September 2015/2016, implemented investments increased to reach LE 78.077 billion in comparison to LE 64.733 billion in the corresponding period in the previous year. This improvement in investment has resulted in a slight decline in unemployment. The unemployment rate declined slightly to reach 12.7 percent in October-December 2015/2016 compared to 12.9 in the same quarter in the previous year.

**Figure 1.1: Real GDP Growth, Unemployment and Inflation Rates**
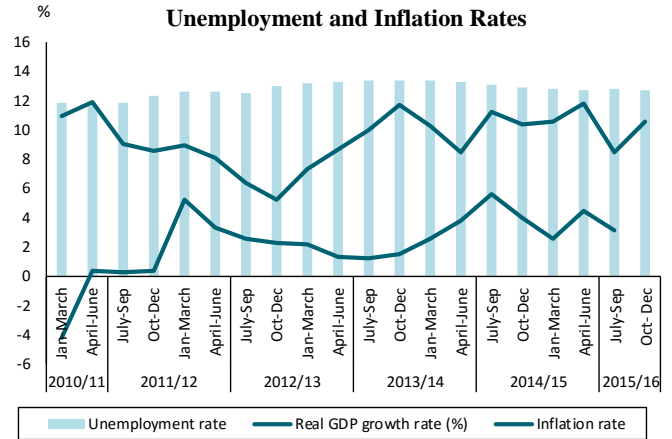
Sources: Ministry of Planning, CAPMAS, and the Central Bank of Egypt (CBE), *Monthly Statistical Bulletin*, various issues.

Figure 1.2: Public Debt and Fiscal Deficit (% of GDP)
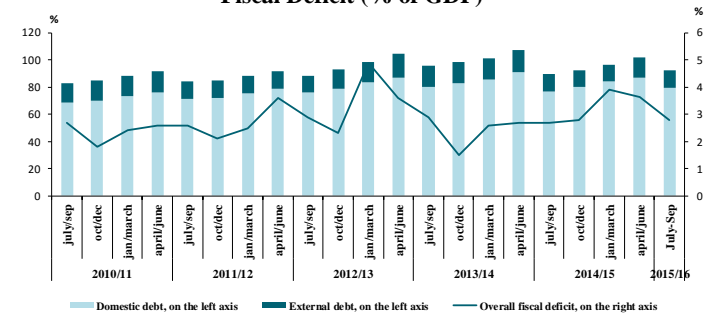
Sources: Central Bank of Egypt (CBE), *Monthly Statistical Bulletin*, various issues, and the Ministry of Finance.
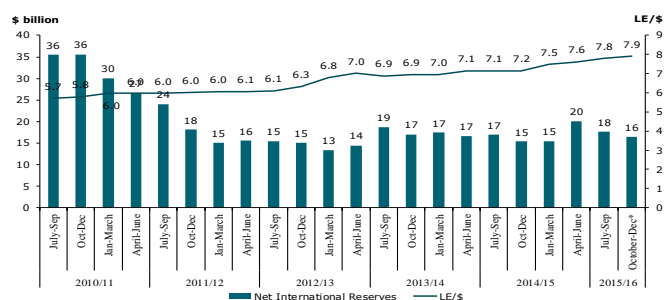

Figure 1.3: Domestic Credit by Sector (% of Total Credit)
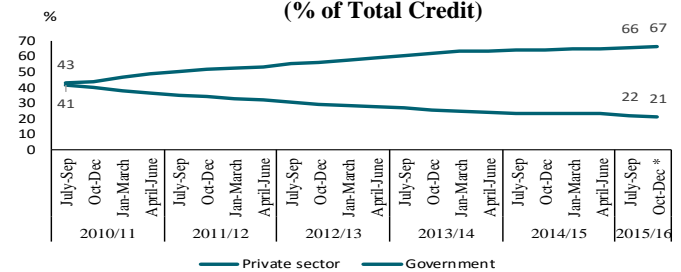
Source: Central Bank of Egypt (CBE), *Monthly Statistical Bulletin*, various issues.
*Data for this quarter is an average for October and November.

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

Source: Central Bank of Egypt (CBE), Monthly Statistical Bulletin, Various Issues.
* Exchange rate for the period October-November.

Past Performance of Businesses

According to the Business Barometer Index (BBI), overall business performance during October-December 2015 witnessed a drop by two points. This is a continuation of the decline that began in the previous quarter. This deterioration in overall performance has been sensed more in the private sector and among small and medium-sized firms.

Firms' evaluation of economic growth declined for the quarter October-December 2015 compared to the previous quarter, but the downturn is modest compared to the decline in the previous quarter. The decline in economic activity has been reflected on firms' performance. Production has decreased by 5 points. Overall Production has shown sluggish trends due to the slowdown of both domestic and international economy. Both domestic and international sales declined in this quarter.

Investment levels are almost similar to last quarter figures. Nevertheless, capacity utilization has witnessed an unprecedented decrease since July-September 2014. It is still higher than the figures observed in 2013 and the second half of 2012. Inventory has reversed its increasing trend declining this quarter by one point.

Output prices declined by two points, which might be the result of decreasing input prices, wages, and declining employment levels for this quarter. This declining trend for both input and output prices can be attributed to government efforts to curb inflation through controlling the prices of ten essential commodities.

Sectorally, all sectors witnessed a decline in performance this quarter except for the manufacturing sector whose performance remained constant compared to the previous quarter. The tourism sector witnessed the sharpest decline in this quarter because of the Russian plane crash over Egypt and the resulting ban of UK flights to Egypt. The manufacturing industries, communications and construction sectors witnessed an increase in their exports during this quarter in light of the depreciation of the Egyptian pound.
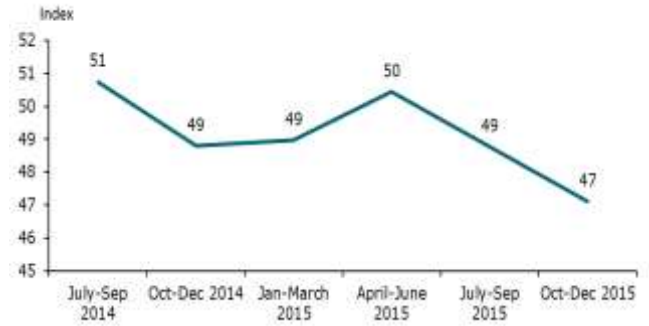
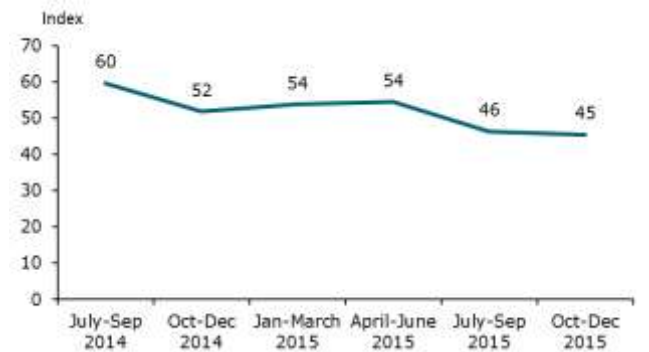**Figure 2.1: Business Barometer Index**

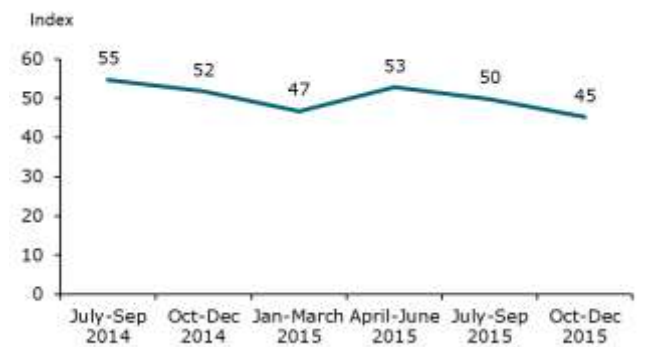

Figure 2.2: Economic Growth

Figure 2.3: Production
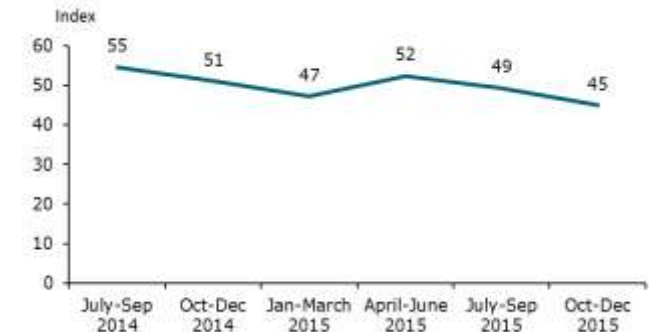

Figure 2.4: Domestic Sales

Figure 2.5: International Sales
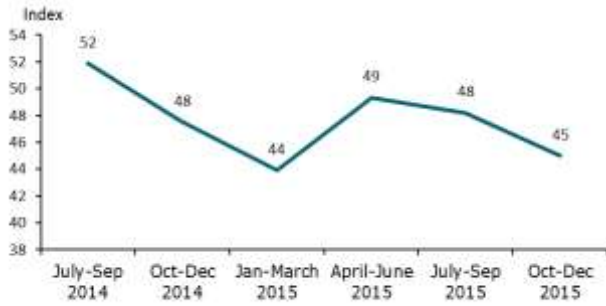
Figure 2.6: Inventory *

Figure 2.7: Capacity Utilization
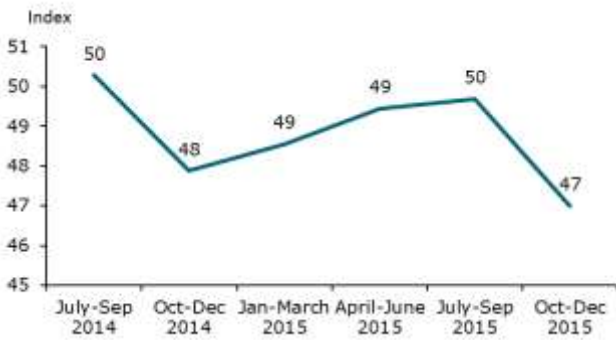
Figure 2.8: Final Product Prices
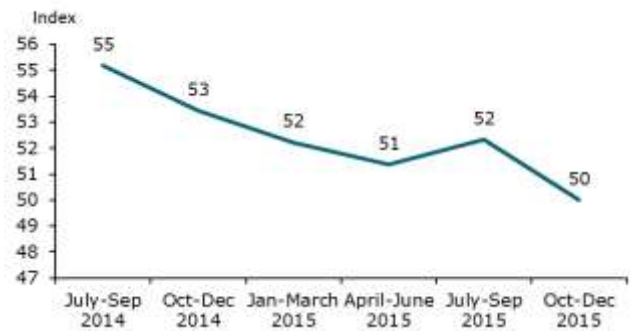
Figure 2.9: Input Prices **
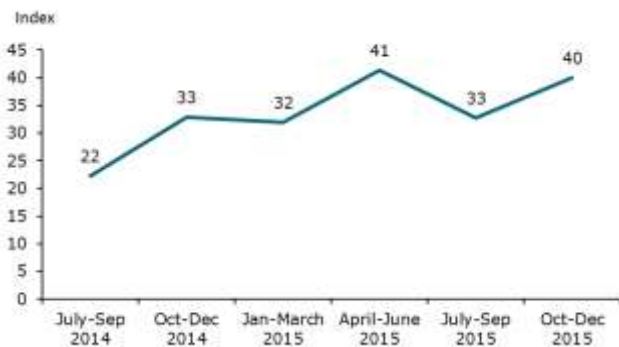
Figure 2.10: Wages

Figure 2.11: Investment

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 in input prices on businesses. Hence, a lower value of this index indicates higher input prices.

Business Strategy Going Forward

Firms' outlook for the upcoming quarter January-March 2016 is more optimistic than their expectations for the previous quarter in contrary to their declining performance in Oct-Dec 2015. Their expectations for economic growth followed the same upward trend in January-March 2016.

Despite a slight decline in international sales, firms expected an increase in production in light of an increase in domestic sales. Expectations of higher production has been reflected on higher wages and employment outlook. Inventory and capacity utilization levels stayed constant. Investments remained unchanged for the third consecutive quarter. Despite fears of further depreciation of the pound, firms anticipate final product prices to remain unchanged in light of an expected decline in input prices. This might be the result of government efforts to control inflation.

Sectorally, the manufacturing industries and the financial intermediation sectors expressed the most optimistic outlook, reporting higher economic growth, production and wages. The worst outlook was reported by the communications sector.

Despite improved competitive advantage due to the depreciated Egyptian pound, exports are expected to decrease for the construction, tourism and transportation sectors. On the contrary, exports are expected to increase only for the manufacturing industries and financial intermediation.

Both SMEs and large firms have an optimistic outlook. Yet, large firms are more optimistic than SMEs. This is the result of expected decline in exports for SMEs. There is no significant difference in outlook between private firms and public firms. However, public firms are more optimistic regarding economic growth, production and domestic and international sales, while privately owned firms reported an expected increase in wages during the upcoming quarter.

Figure 3.1: Business Barometer Index
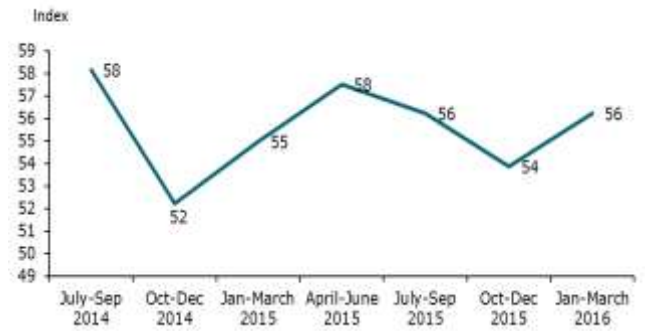
Figure 3.2: Economic Growth
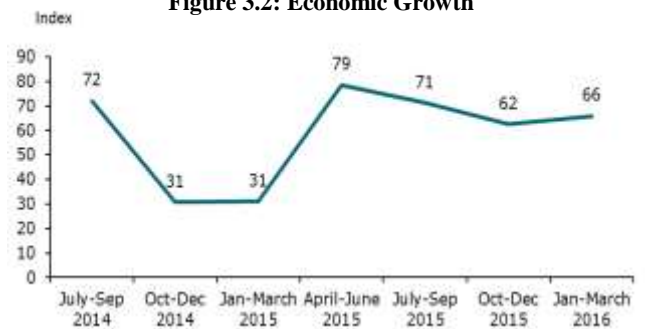
Figure 3.3: Production
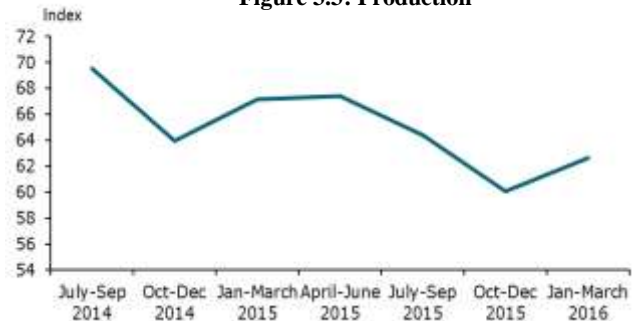
Figure 3.4: Domestic Sales
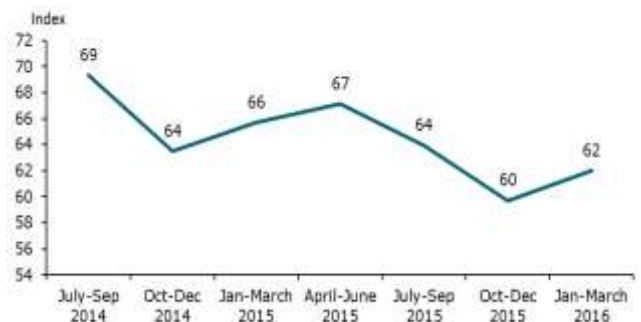
**Figure 3.5: International Sales**
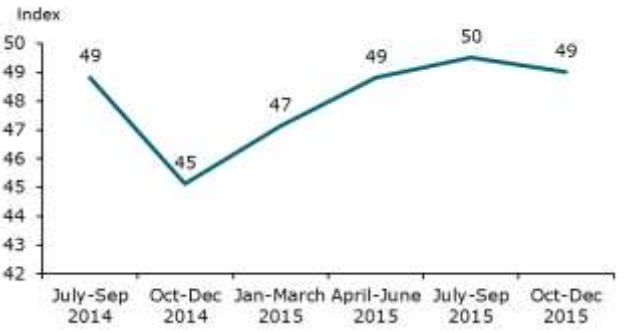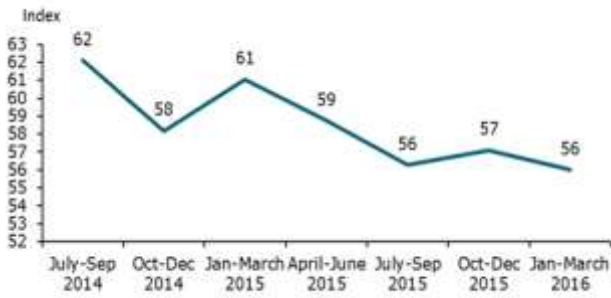

Figure 3.6: Inventory *

Figure 3.7: Capacity Utilization
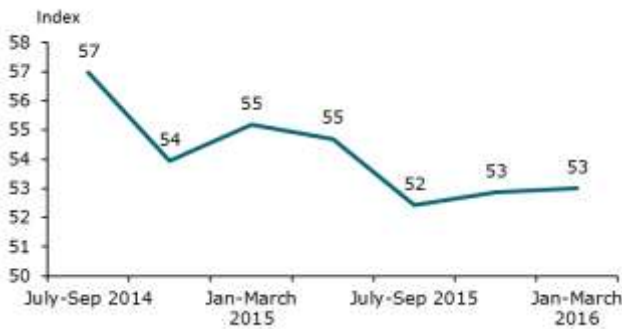
Figure 3.8: Final Product Prices
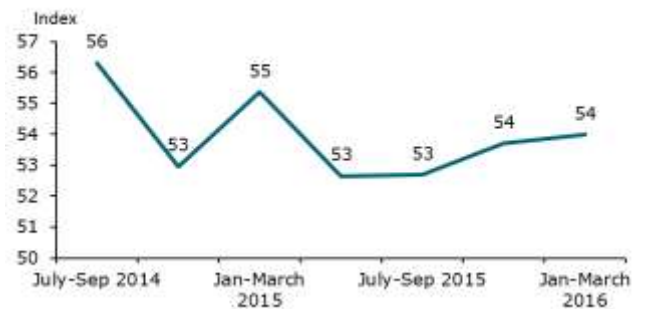
Figure 3.9: Input Prices **
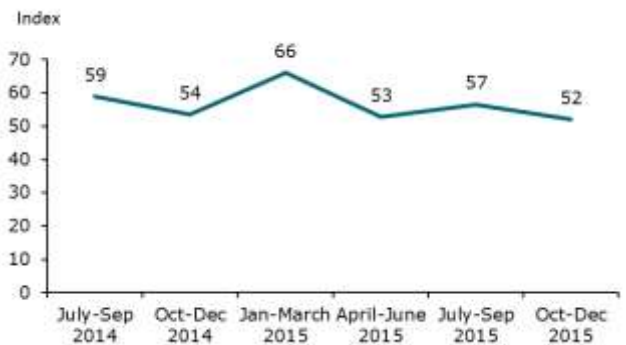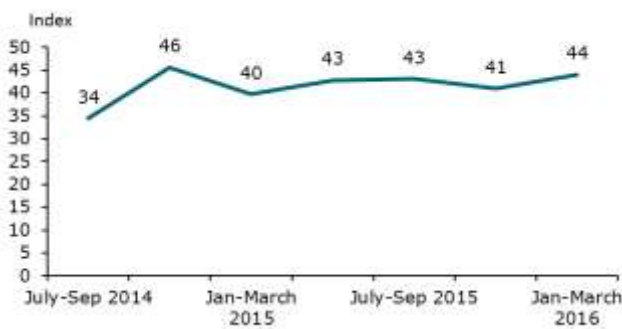

Figure 3.10: Wages
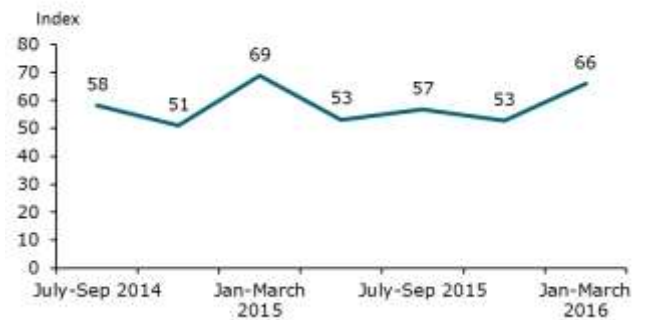
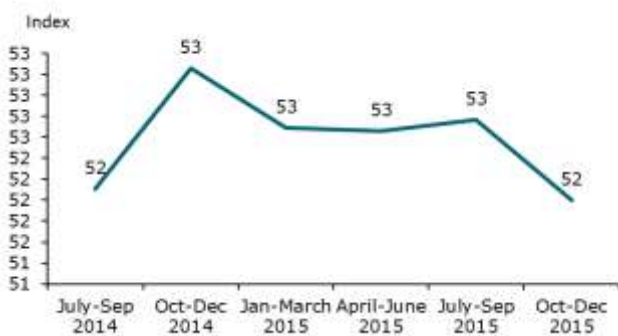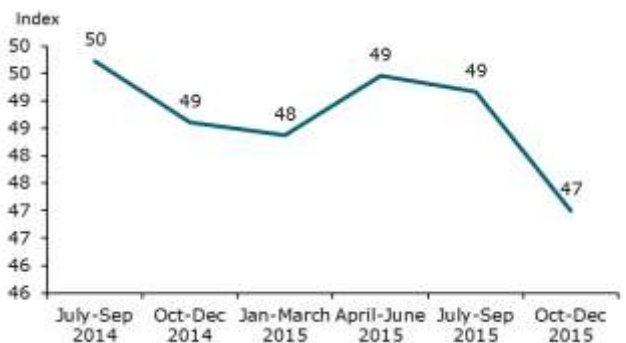**Figure 3.11: Investment**
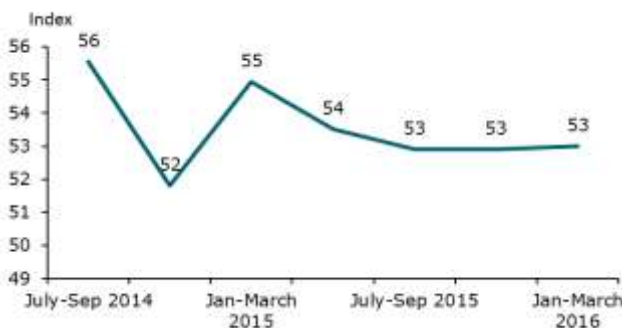
Figure 3.12: Employment
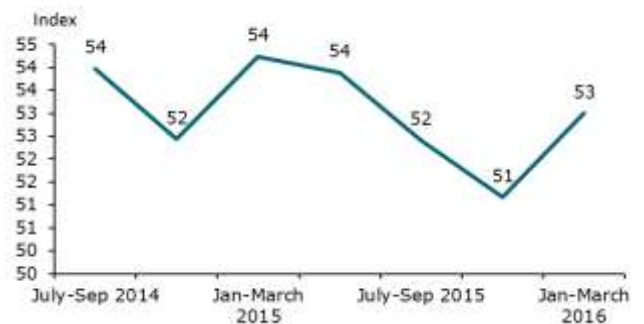
Source: Survey results.

* 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 in input prices on businesses. Hence, a lower value of this index indicates higher input prices.

Business Constraints

Major Constraints: Political and Economic Instability, Red Tape and Poor Infrastructure

Survey respondents were asked to identify areas in which their firms faced a major constraint (Figure 4). Government policies appeared to be more cumbersome to firms in the quarter October-December 2015 compared to the previous quarter. Political instability was a concern for firms in the same quarter in the previous year. In addition, red tape was one of the firms' main concerns. In contrast, inflation changed from being the major constraint facing firms in the last quarter to being the fifth constraint this quarter. This might be partially the result of the CBE's decision to raise interest rates in an effort to control inflation. On the other hand, the rise in interest rates did not hinder firms' performance as it was reported as the least constraint. Furthermore, firms faced minimal constraints with respect to labor laws, obtaining land and gas network infrastructure.

Figure 4: Major Constraints Facing the Business Sector

(Normalized Index of Severity)
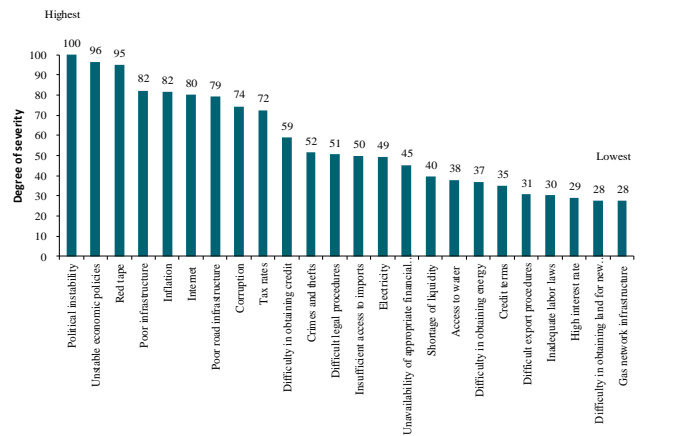
Source: Survey results.

Policy Expectations

Policy Expectations: More Trade Stimulating Policies and Easier Government Red Tape

Figure 5 shows firms' policy expectations. Trade stimulating policies and red tape are on top of the list. As red tape is a persistent constraint facing firms, there is an increasing need to reduce it.

In the previous quarter, the exchange rate policy was the first policy expectation, as the government had taken a number of measures to address the shortage of foreign currency. Such measures started last year with introducing capital control

measures, followed by restricting the imports of some goods, by requiring importers of 23 categories of goods to have their overseas suppliers registered with the General Organization for Export and Import Control (GOEIC) and agree to inspections of their goods.

Figure 5: Policy Expectations
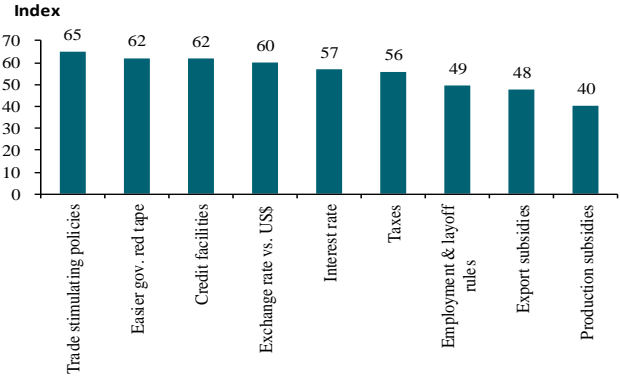
Source: Survey result.

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 Business Sector Past Performance (October-December 2015)[1]

Indicator	Manufacturing			Index[2] 48	Construction			Index[2] 45	Tourism			Index[2] 34	Transportation			Index[2] 42	Communications			Index[2] 45	Financial Intermediaries			Index[2] 44
	Higher	Same	Lower		Higher	Same	Lower		Higher	Same	Lower		Higher	Same	Lower		Higher	Same	Lower		Higher	Same	Lower	
Economic growth	22	43	35	**45**	15	49	36	**43**	10	35	55	**33**	15	52	33	**44**	32	46	21	**53**	31	47	23	**53**
Business activity																								
Production	30	37	34	**49**	16	58	25	**47**	8	18	75	**22**	15	44	41	**41**	21	54	25	**49**	26	35	39	**45**
Domestic sales	28	38	35	**48**	16	58	25	**47**	10	23	68	**27**	15	52	33	**44**	21	54	25	**49**	26	35	39	**45**
International sales	24	60	16	**53**	67	33	0	**75**	3	21	76	**20**	18	33	48	**38**	0	100	0	**50**	0	100	0	**50**
Inventory	17	69	14	**49**	0	0	0	**0**	0	0	0	**0**	0	0	0	**0**	0	0	0	**0**	0	0	0	**0**
Level of capacity utilization	12	67	21	**47**	7	75	18	**47**	5	50	45	**37**	15	74	11	**51**	0	96	4	**49**	15	56	29	**46**
Prices																								
Final product prices	12	82	6	**52**	4	96	0	**51**	3	57	40	**38**	11	74	15	**49**	0	100	0	**50**	2	95	3	**50**
Intermediate input prices	42	55	3	**37**	38	58	4	**39**	20	80	0	**44**	15	81	4	**47**	21	79	0	**44**	26	74	0	**43**
Wage level	11	89	0	**53**	4	96	0	**51**	8	93	0	**52**	9	85	6	**51**	11	89	0	**53**	5	94	2	**51**
Primary inputs																								
Investment	7	91	2	**51**	7	91	2	**51**	5	95	0	**51**	13	83	4	**52**	0	96	4	**49**	16	81	3	**54**
Employment	5	80	15	**47**	4	80	16	**47**	15	65	20	**48**	7	80	13	**48**	7	68	25	**45**	6	84	10	**49**

Table A2. Survey Results: Summary of Business Sector Outlook (Jan.-March 2016)[1]

Indicator	Manufacturing			Index[2] 56	Construction			Index[2] 51	Tourism			Index[2] 51	Transportation			Index[2] 50	Communications			Index[2] 45	Financial Intermediaries			Index[2] 57
	Higher	Same	Lower		Higher	Same	Lower		Higher	Same	Lower		Higher	Same	Lower		Higher	Same	Lower		Higher	Same	Lower	
Economic growth	54	40	6	**67**	45	44	11	**62**	50	30	20	**62**	37	56	7	**60**	54	39	7	**67**	66	31	3	**74**
Business activity																								
Production	45	46	9	**62**	42	56	2	**63**	35	57	8	**59**	35	50	15	**57**	43	46	11	**61**	65	35	0	**74**
Domestic sales	42	49	9	**61**	42	58	0	**63**	33	62	5	**59**	36	49	15	**57**	43	46	11	**61**	65	35	0	**74**
International sales	29	69	2	**58**	14	71	14	**50**	17	72	10	**52**	23	71	6	**55**	0	0	0	**0**	67	33	0	**75**
Inventory	8	87	5	**49**	0	0	0	**0**	0	0	0	**0**	0	0	0	**0**	0	0	0	**0**	0	0	0	**0**
Level of capacity utilization	14	82	4	**53**	20	78	2	**55**	15	80	5	**53**	13	85	2	**53**	0	100	0	**50**	23	76	2	**56**
Prices																								
Final product prices	15	83	2	**54**	25	75	0	**57**	10	90	0	**53**	15	83	2	**54**	21	79	0	**56**	3	95	2	**50**
Intermediate input prices	26	71	2	**43**	27	73	0	**42**	11	89	0	**47**	8	85	8	**50**	29	71	0	**42**	7	93	0	**48**
Wage level	53	47	0	**68**	42	58	0	**63**	55	43	3	**69**	43	56	2	**63**	21	79	0	**56**	50	47	3	**66**
Primary inputs																								
Investment	11	88	1	**53**	7	91	2	**51**	10	90	0	**53**	13	85	2	**53**	11	89	0	**53**	15	84	2	**54**
Employment	14	83	3	**53**	16	82	2	**54**	10	90	0	**53**	11	87	2	**52**	21	68	11	**53**	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) (October-December 2015)[1]

Indicator	SMEs				Large			
	Higher	Percentage Same	Lower	Index[2] 46	Higher	Percentage Same	Lower	Index[2] 49
Economic growth	17	46	37	**43**	26	43	31	**48**
Business activity								
Production	19	38	43	**41**	29	41	30	**50**
Domestic sales	19	38	43	**41**	27	45	28	**50**
International sales	13	48	39	**41**	24	47	29	**48**
Inventory	16	72	12	**49**	18	66	15	**49**
Level of capacity utilization	9	64	26	**45**	12	72	16	**49**
Prices								
Final product prices	8	84	8	**50**	8	83	9	**50**
Intermediate input prices	35	64	1	**40**	35	62	3	**40**
Wage level	11	89	0	**53**	7	91	2	**51**
Primary inputs								
Investment	5	92	3	**51**	12	87	1	**53**
Employment	6	80	13	**48**	6	76	18	**47**

Table A4. Survey Results: Summary of Business Sector Outlook (By Size) (January-March 2016)[1]

Indicator	SMEs				Large			
	Higher	Percentage Same	Lower	Index[2] 55	Higher	Percentage Same	Lower	Index[2] 57
Economic growth	50	41	8	**65**	54	39	7	**67**
Business activity								
Production	40	50	9	**60**	50	44	6	**65**
Domestic sales	40	51	9	**60**	49	46	5	**65**
International sales	23	71	6	**55**	27	69	4	**57**
Inventory	7	88	5	**49**	10	85	5	**49**
Level of capacity utilization	13	83	4	**52**	17	81	2	**54**
Prices								
Final product prices	14	85	2	**54**	16	83	1	**54**
Intermediate input prices	20	79	1	**45**	24	74	2	**44**
Wage level	49	50	1	**66**	47	52	1	**65**
Primary inputs								
Investment	8	91	1	**52**	15	83	1	**54**
Employment	12	85	3	**52**	14	83	3	**53**

[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.