



المركز المصري للدراسات الاقتصادية
The Egyptian Center for Economic Studies

Business Barometer

Issue 44 2017



Performance & Expectations of the Egyptian Business Sector

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The Egyptian Center for Economic Studies (ECES) is an independent, non-profit think tank that conducts specialized economic research, drawing on international experience and constructive discussions among various stakeholders. ECES's main objective is to propose sound economic policies, and institutional and legislative reforms that contribute to sustainable development in Egypt, all on the basis of combined economic efficiency and social justice.

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Economic efficiency and social justice are of core interest to ECES. Combined, they constitute the Center's strategic direction. ECES research and activities focus on studying past, present and future challenges facing the Egyptian economy, whether they are related to macroeconomic stability, microeconomic efficiency, or political economy aspects both on the internal and external dimensions. In its analysis, ECES is keen on adopting a comprehensive approach that encompasses legislative, institutional, policy and structural aspects of whatever problem or area addressed, not to mention implementation mechanisms. In all its activities, ECES relies on its competent team of in-house researchers, in addition to collaboration with external experts and like-minded think tanks as needed.

About the Business Barometer

This edition of the Business Barometer reports the results of a stratified sample of 120 private firms. The survey covers their assessment of economic growth and the results of their operations over the last quarter (April-June) of FY 2016/2017. It also summarizes their expectations for overall future economic performance as well as their own activities for the first quarter (July-September) of FY 2017/2018.

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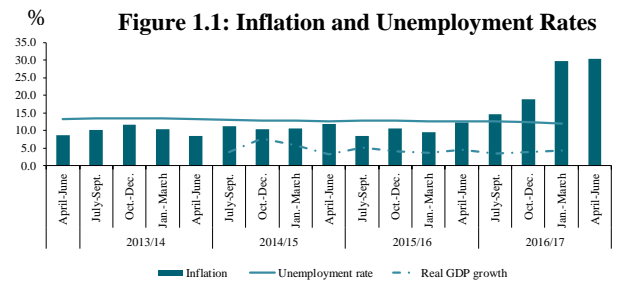
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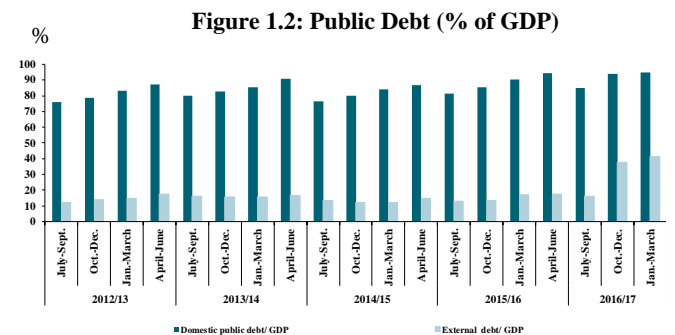
Overview

This edition of the Business Barometer (BB) presents the survey results of a stratified panel of 120 firms regarding their perceptions about the performance of the Egyptian economy and own business during the fourth quarter (April-June) of FY2016/2017 and their outlook for the first quarter (July-September) of FY2017/2018. Firms participating in the survey represent the manufacturing sectors (50 percent), financial services (13 percent), construction (12 percent), transportation (10 percent), tourism (9 percent) and telecommunications (7 percent). The survey also covers a number of small, medium and large enterprises. According to the survey, the business community is starting the new fiscal year with cautious forecasts regarding the recovery of the economy. However, such forecasts are not consistent with the recovery in GDP growth, which rose to 4.3 percent during the third quarter of FY2016/2017 compared to 3.6 percent during the corresponding period of the previous fiscal year. The rising growth rate was reflected in lower unemployment (12 percent) during the third quarter of FY2016/2017 compared to about 12.7 percent in the third quarter of the previous year, registering its lowest level in two years (Figure 1.1).

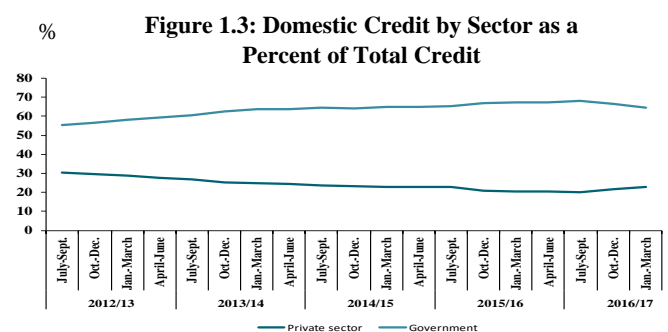
As for macro indicators, the annual inflation rate rose to 30 percent during the quarter under review compared to 29 percent in the previous quarter of FY2016/2017. The annual inflation rate also rose to 34.2 percent in July 2017 compared to 30.9 percent in June 2017. This notable rise came in the



Source: Central Bank of Egypt (CBE), *Monthly Statistical Bulletin*, various issues.



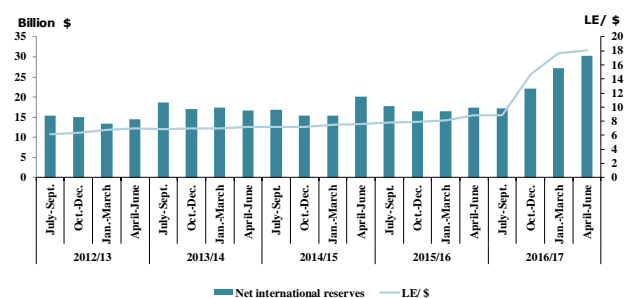
Source: Central Bank of Egypt (CBE), *Monthly Statistical Bulletin*, various issues.



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

* Exchange rate for the period October-November.

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



Source: Central Bank of Egypt (CBE), *Monthly Statistical Bulletin*, various issues.

wake of the decision to raise fuel prices end of last June.

In an attempt to counter inflationary pressures, the Central Bank of Egypt (CBE) raised the deposit and lending rate in May by 200 basis points, the second hike since liberalizing the exchange rate in November 2016. Towards the end of this quarter (June 29, 2017), the government decided to raise fuel prices. As a matter of course, this would reflect on prices, but the impact thereof on corporate performance will materialize over the coming quarter, as costs in the quarter under review were incurred using pre-rise fuel prices.

On the fiscal front, recent economic reforms undertaken since 2016 have led to improvement in some fiscal indicators, including lower overall deficit to GDP (9.5 percent) during July 2016 -May 2017 compared to 11.5 percent in the corresponding period of the previous fiscal year. This decline is mainly due to the growth of public revenues at a rate exceeding the growth of public expenditures (Figure 1.2).

The Government continued to finance this deficit by issuing bonds and Treasury bills in local or foreign currency, thus increasing the size of domestic public debt, which reached about EGP 3158 billion by end of March 2017, accounting for 93 percent of GDP, hence exceeding the safe limit (60 percent of GDP). Moreover, the volume of external public debt rose to \$US73 billion by end of March 2017.

The high and rising indebtedness negatively affect the competitiveness of the Egyptian economy and

its credit rating, and increase pressures on public finances with respect to fulfillment of constitutional entitlements that require increased spending on education, health and scientific research to about 10 percent of GDP. It also translates into lower credit availability to the private sector to finance various economic activities, leading to deeper economic recession and the consequent contraction of public revenues (Figure 1.3).

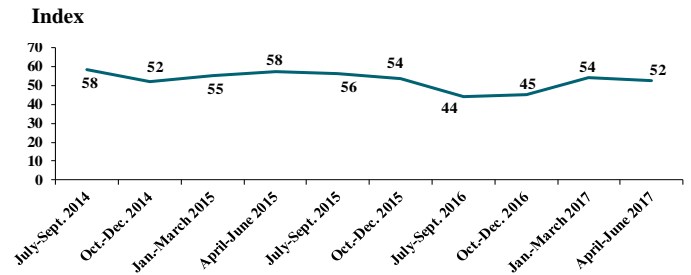
Net international reserves also rose to \$30 billion during the quarter under review from \$27 billion in the previous quarter. They further increased to \$36.03 billion in July, the highest level in seven years, compared to \$31 billion at end of June. The increase in reserves is attributed to higher exports, foreign investment inflows, and receiving the second payment of the first tranche of the IMF loan with a value of \$1.25 billion. It is also noteworthy that the exchange rate witnessed a slight decline during the quarter under review compared to the previous quarter thanks to increased dollar resources in the banking system.

Business Barometer Index (BBI)

Lower BBI for both past performance and outlook

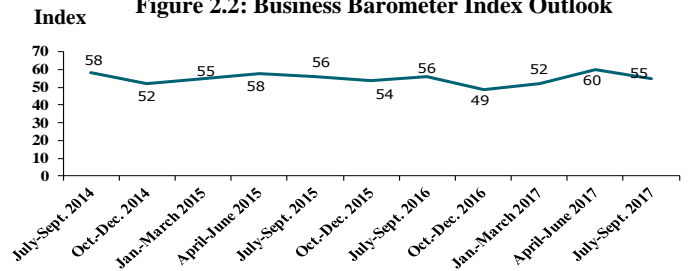
Although the government embarked on several economic reforms, views of the business community have yet to improve. In particular, the past performance BBI declined by two points during the quarter under review led by a rise in input prices (Figure 2.1). The corporate outlook for the first quarter (July-September) of FY2017/2018 is lower than that for (April-June 2017), reflecting uncertainty by the business community regarding economic reforms (Figure 2.2). The BBI for large enterprises showed less positive views with respect to both past performance and expectations, with small and medium enterprises also reporting a decline, albeit lesser than large enterprises.

Figure 2.1: Business Barometer Index Evaluation



*Data for the quarters (Jan-March and April-June 2016) is unavailable.

Figure 2.2: Business Barometer Index Outlook



*Data for the quarters (July-September & October-December 2016) is unavailable.

Figure 2.4: Business Barometer Index
B- SMEs

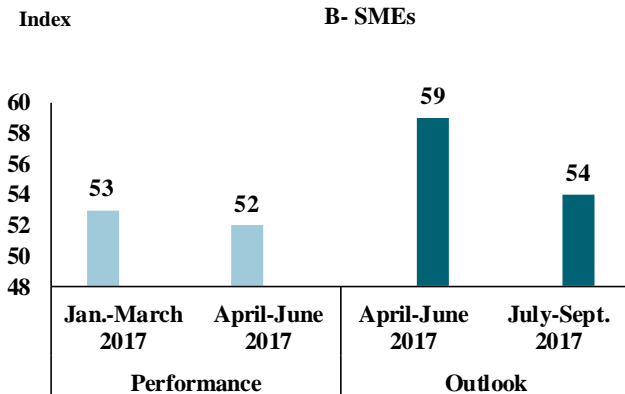
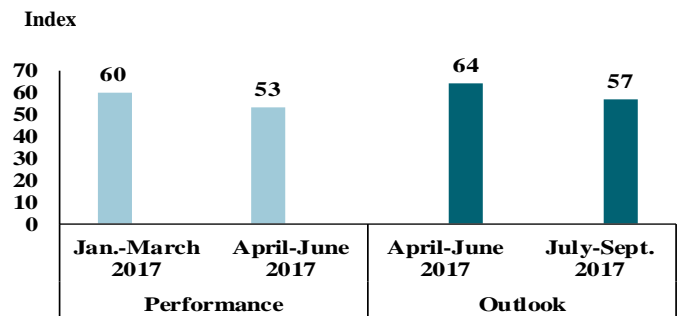


Figure 2.3: Business Barometer Index
A- Large Firms



Source: Survey results.

Past Performance of Businesses

Declining domestic production and sales indices for SMEs

Despite the recovery of real GDP growth and improvement of corporate performance in the previous quarter (January-March 2016/2017), corporate assessment of economic growth in the quarter

Source: Survey results. Over than in the previous quarter. The decline in economic activity negatively affected the performance of large enterprises, with the production index declining by 8 points compared to the previous quarter. Domestic sales witnessed a similar decline, affecting the capacity utilization index, which fell two points from the previous quarter. This indicates continued corporate uncertainty regarding own business and economic environment despite government efforts to boost investment and the impact thereof on the capacity utilization index for large enterprises (Figure 3.1). Past performance indicators for SMEs were better compared to large enterprises, with the former reporting more positive views regarding economic growth, reflecting the government's strategy to introduce new policies for the development of SMEs (Figure 3.2).

Sectorally, the manufacturing sector reported the best performance, with the index posting 53 points in the quarter under review. The business sector's views regarding production were more positive in the quarter under review, with the index rising to 60 points compared to 57 points in the previous quarter. The export index increased to 72 points

Figure 3.1: Economic Activity
 A. Evaluation: Large Firms

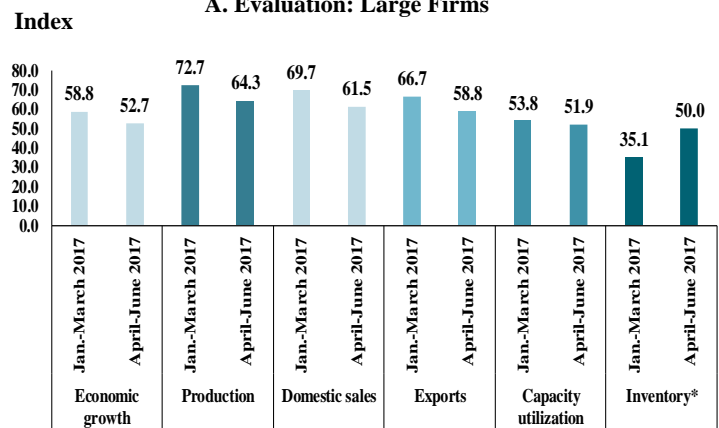
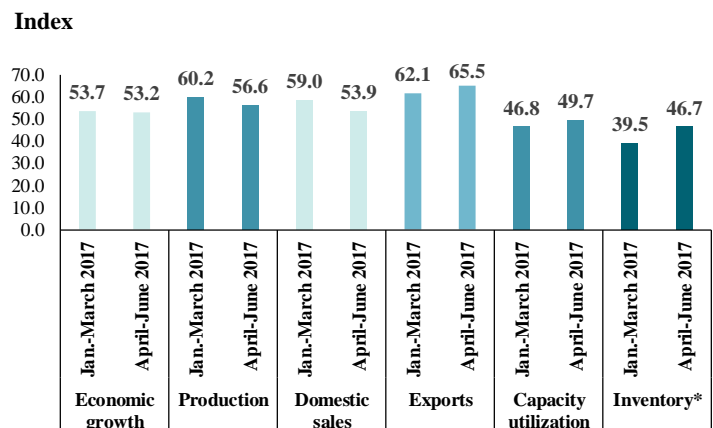


Figure 3.2: Economic Activity
 B. Evaluation - SMEs



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

from 70 points in the previous quarter, followed by the tourism sector (52 points) thanks to increased tourist nights in the third quarter of FY2016/2017, then the telecommunications and transport sectors (Table 1).

Increased input and final product prices

The assessment of past performance of large enterprises showed a continued rise in final product prices, as the index exceeded 50 points (see the methodology) (Figure 3.3), though the index fell to 73.8 points in April-June 2016/2017 from 83.9 in January-March 2016/2017. In April-June 2016/2017, input prices rose to their highest in view of the actions taken by the government in the way of economic reform. While the past performance assessment of SMEs is better than that of large enterprises, the rise in input prices remains a major constraint facing the business community in general (Figure 3.4).

Decline in investment and employment indices

Continuing with the past performance assessment, the employment index for large enterprises fell by 4 points in the quarter under review compared to the previous year. Likewise, the investment index fell to 53.3 points in April-June 2016/2017 compared to 57 points in the previous quarter (Figure 3.5). Contrary to investment and employment indices for large enterprises, survey results showed an increase in the investment and employment indices for SMEs. This confirms the more cautious attitude of large enterprises, and

Figure 3.3: Prices and Wages
A. Evaluation: Large Firms

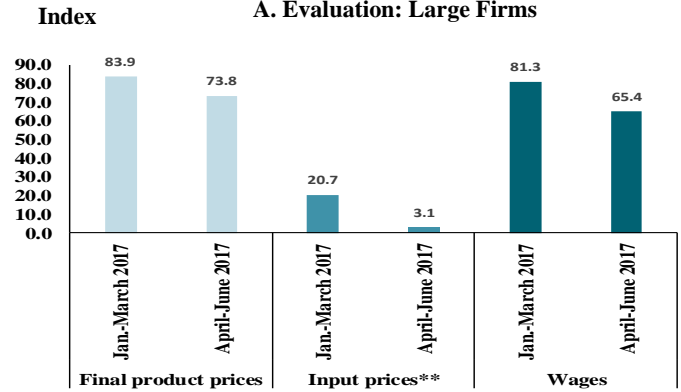


Figure 3.4: Prices and Wages
B. Evaluation: SMEs

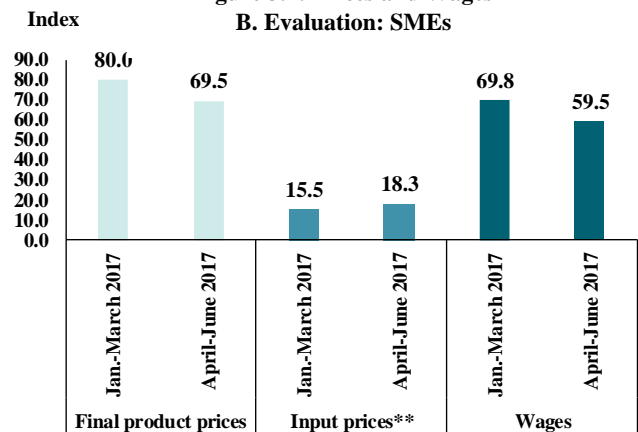


Figure 3.5: Investment and Employment
A. Evaluation: Large Firms

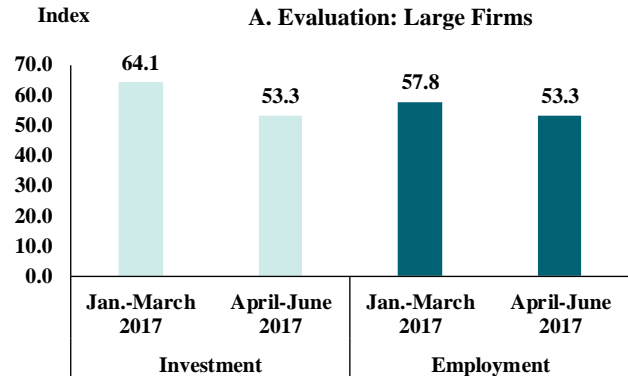
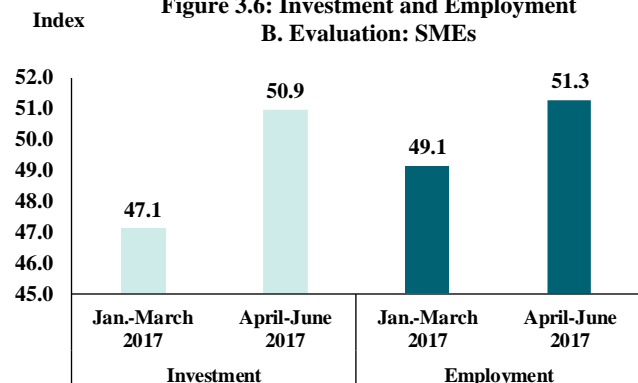


Figure 3.6: Investment and Employment
B. Evaluation: SMEs



Source: Survey results.

** The input price index is inverted to reflect the negative impact of rising input prices on the BBI. In other words, a lower index indicates higher input prices.

reflects the larger negative impact on large enterprises of higher input prices (Figure 3-6).

Survey results regarding investment and employment for SMEs were similar to large firms. The investment index rose from 37 points in the second quarter to 47.1 points in the third quarter, while the employment index rose from 47.9 points to 49.1 points during the same period.

It is noteworthy that this rise in the employment and investment indices is still below the mean (50 points) (see the Methodology in the Appendix). The rise in employment and investment indices can be attributed to rationalization of imports due to their higher prices after liberalization of the exchange rate, as well as to the higher demand on locally produced inputs (Figure 3.6).

Business Strategy Going Forward

Expectations of continued decline in production, domestic sales and capacity utilization

The corporate outlook for the first quarter (July-September) of FY2017/2018 was less optimistic compared to the previous quarter (April-June 2017), suggesting companies are uncertain about the impact of economic reform measures. In particular, the production index fell to 68.2 points in July-September 2017/2018 compared to 83.3 points in the previous quarter. The indices of domestic sales, exports and capacity utilization all edged downward. Results show an increase in the inventory index, reflecting high expectations of demand growth and domestic consumption (Figure 4.1). The outlook of SMEs regarding economic activity was similar to that of large enterprises, albeit more optimistic, reflecting the measures taken by the government to promote the role of SMEs.

Figure 4.1: Economic Activity
 A. Outlook: Large Firms

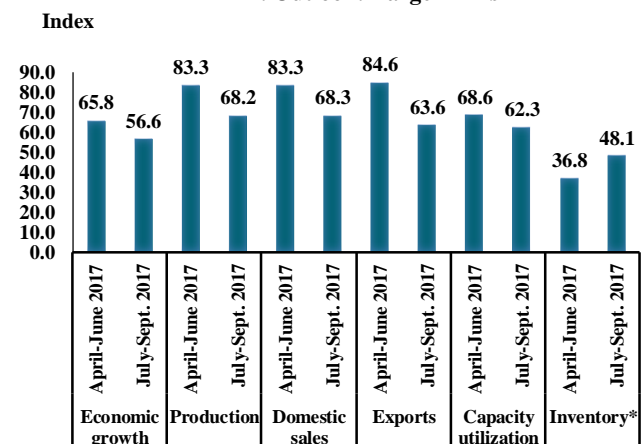
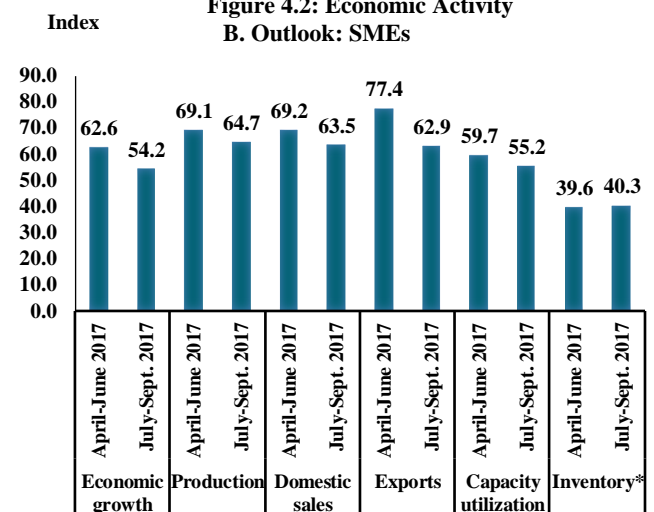


Figure 4.2: Economic Activity
 B. Outlook: SMEs



Source: Survey results.

* The inventory index is inverted to reflect the negative impact of rising inventory on businesses. In other words, a higher index indicates lower inventory and vice versa.

At the sectoral level, the transport sector voiced the most positive outlook, followed by the manufacturing sector (54 points). The business community also reported a positive outlook for construction and tourism in the first quarter of FY2017/2018 (Table 2).

Final product and input prices as well as wages expected to continue rising

Large enterprises expect both input and final product prices to continue rising during the first quarter of FY2017/2018; as the final product price index rose by 14 points and the wage index by 5 points from the previous quarter. This could be attributed to the continued impact of reduced energy subsidies at end of last June (Figure 3.4).

Expectations of SMEs were similar to those of large enterprises, with both expecting input and final product prices and wages to continue rising (Figure 4.4).

Expectations of a slight decline in investment and employment indices

The views of large enterprises with respect to investment and employment were less optimistic than in the previous quarter, due to the multiplicity of constraints facing investment (Figure 4.5). SMEs' views regarding investment and employment were even less positive compared to those of large enterprises, reflecting uncertainty of the business community regarding the policies aimed at incentivizing investment and employment.

Figure 4.3: Prices and Wages

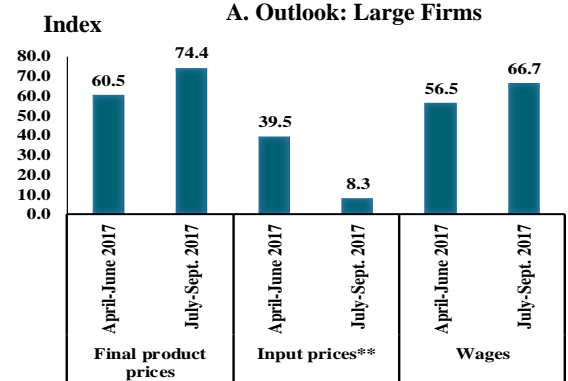


Figure 4.4: Prices and Wages

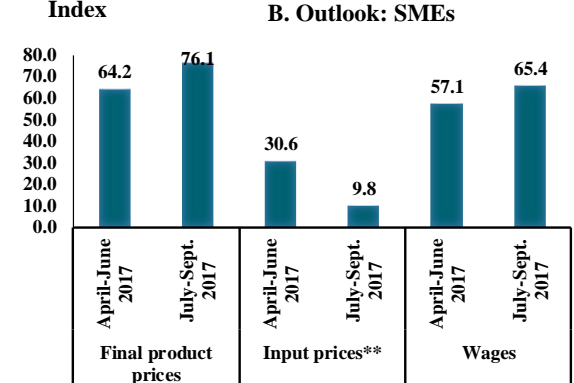


Figure 4.5: Investment and Employment

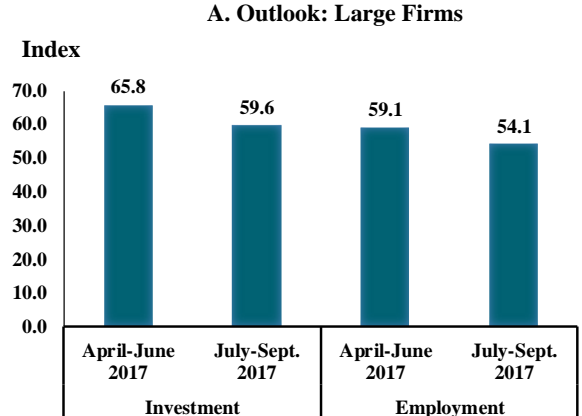
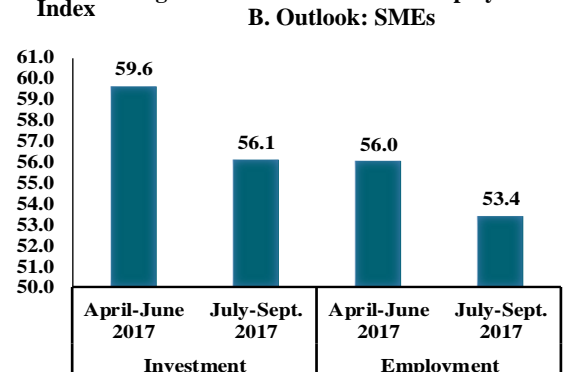


Figure 4.6: Investment and Employment



Source: Survey results.

** 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.

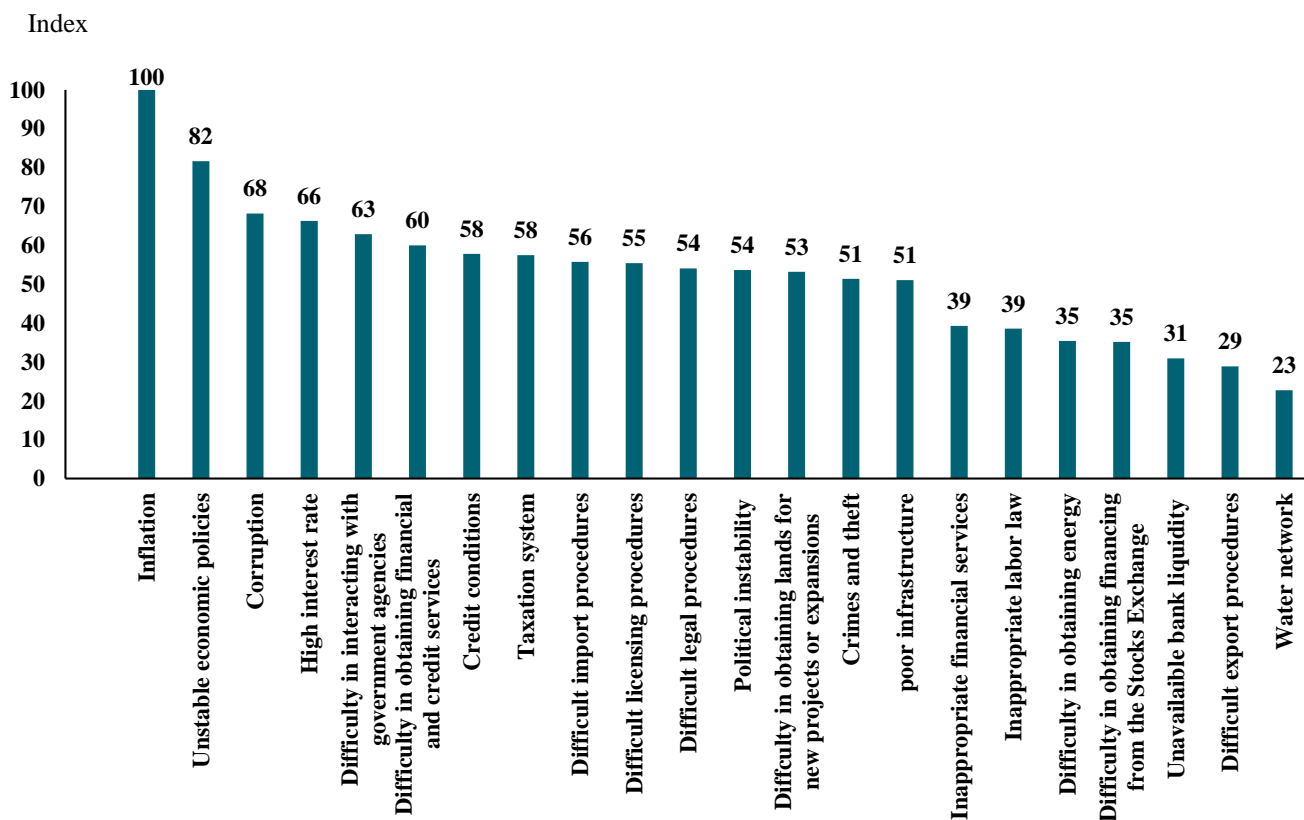
Business Constraints

Major constraints facing the business sector.

Major constraints: inflationary pressures, policy instability, corruption and high lending interest rate

Figure 5 shows the major barriers that constrained businesses during the period under review, arranged in a descending order of severity. In particular, firms expressed concern about inflation, policy instability, corruption, and high lending interest rate. The order of constraints is similar to that of the previous survey, with rising inflation remaining the most severe constraint due to the reduction of petroleum subsidies, the hike in electricity prices and the increase in the VAT rate. In an attempt to control inflation, the government has taken a number of measures, such as raising deposit and lending interest rates, though the business community deemed this decision a severe constraint. Therefore, there is a need to take measures to stimulate investment and production, with a view to increasing national income.

Figure 5: Major Constraints Facing the Business Sector (Normalized Index of Severity)



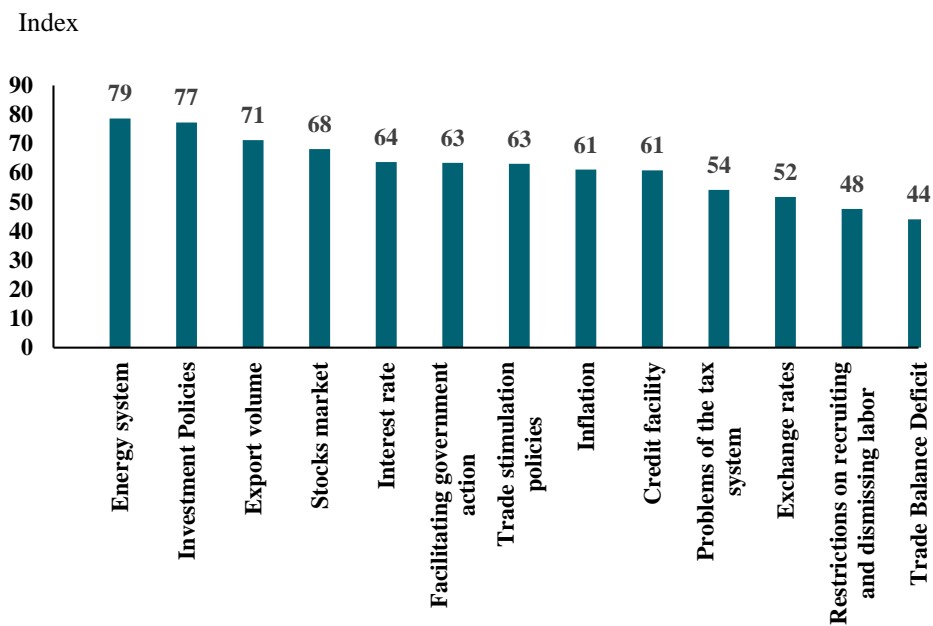
Source: Survey results.

Policy Expectations

Expected improvement in energy and investment policies as well as exports

As shown in Figure 6, firms expect improvements in the energy system due to government efforts in undertaking new and renewable energy projects and availing opportunities for investors to enter this field. Firms also expect improvement in investment policies with the near completion of the executive regulations of the new investment law, which aims to attract more foreign direct investment during FY2017/2018. Firms also expect the volume of exports to increase thanks to the liberalization of the exchange rate, which gives Egyptian products a competitive edge.

Figure 6: 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:

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

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. Summary of Past Performance of All Firms (by Sector) (April-May-June 2017)¹

Indicator	Manufacturing				Construction				Tourism				Transport				Communications				Financial Intermediaries			
	Percentage			Index ²	Percentage			Index ²	Percentage			Index ²	Percentage			Index ²	Percentage			Index ²	Percentage			Index ²
	Higher	Same	Lower		53	Higher	Same		Lower	50	Higher		Same	Lower	52		Higher	Same	Lower		48	Higher	Same	
Economic growth	38	36	25	55	20	60	20	50	27	64	9	56	18	73	9	53	44	33	22	58	25	44	31	48
Economic activity																								
Production	49	28	23	60	53	33	13	65	45	9	45	50	36	45	18	56	33	33	33	50	56	6	38	59
Domestic sales	42	28	30	55	47	40	13	62	50	10	40	55	36	45	18	56	44	22	33	55	50	13	38	56
Exports	63	33	4	72	0	0	0	0	44	22	33	55	14	43	43	40	50	25	25	60	0	0	0	0
Inventory	33	39	28	48	13	60	27	54	36	36	27	47	30	60	10	44	25	38	38	55	64	7	29	33
Capacity utilization	16	72	12	51	27	60	13	54	0	91	9	48	0	82	18	45	0	63	38	38	25	69	6	56
Prices																								
Final product prices	59	36	5	70	93	7	0	94	73	9	18	75	36	64	0	61	63	38	0	73	44	50	6	63
Intermediate input prices	85	15	0	13	100	0	0	0	70	30	0	23	73	27	0	21	83	17	0	14	67	33	0	25
Wage level	36	64	0	61	57	43	0	70	18	82	0	55	9	91	0	52	44	56	0	64	44	56	0	64
Primary inputs																								
Investment	16	74	10	52	0	93	7	48	18	82	0	55	0	100	0	50	11	89	0	53	20	67	13	52
Employment	16	72	11	51	7	80	13	48	18	73	9	53	9	91	0	52	22	78	0	56	13	88	0	53

Table A2. Survey Results: Summary of Outlook of All Firms (by Sector) (July-August-September 20)

Indicator	Manufacturing				Construction				Tourism				Transport				Communications				Financial Intermediaries			
	Percentage			Index ²	Percentage			Index ²	Percentage			Index ²	Percentage			Index ²	Percentage			Index ²	Percentage			Index ²
	Higher	Same	Lower		54	Higher	Same		Lower	54	Higher		Same	Lower	54		Higher	Same	Lower		73	Higher	Same	
Economic growth	28	43	28	50	7	93	0	52	27	64	9	56	55	45	0	69	33	44	22	54	56	38	6	68
Economic activity																								
Production	46	34	20	60	73	20	7	78	45	36	18	60	91	9	0	92	33	56	11	57	69	19	13	74
Domestic sales	47	30	23	59	73	20	7	78	40	40	20	57	82	18	0	85	33	56	11	57	69	19	13	74
Exports	64	32	4	73	0	0	0	0	0	67	33	40	57	43	0	70	0	75	25	43	0	0	0	0
Inventory	24	63	14	47	0	93	7	52	27	55	18	47	90	10	0	9	43	57	0	36	64	36	0	26
Capacity utilization	27	60	13	54	53	40	7	67	27	73	0	58	36	64	0	61	22	78	0	56	25	75	0	57
Prices																								
Final product prices	64	31	5	72	87	13	0	88	73	27	0	79	100	0	0	100	50	50	0	67	56	44	0	70
Intermediate input prices	83	17	0	14	100	0	0	0	100	0	0	0	100	0	0	100	100	0	0	0	83	17	0	14
Wage level	38	62	0	62	27	73	0	58	91	9	0	92	100	0	0	100	44	56	0	64	44	56	0	64
Primary inputs																								
Investment	17	73	10	52	53	40	7	67	9	91	0	52	45	55	0	65	33	67	0	60	53	47	0	68
Employment	10	85	5	51	13	80	7	52	18	82	0	55	27	73	0	58	11	89	0	53	38	63	0	62

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

²Equal 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 Past Performance of all Firms (by size) (April-May-June 2017)¹

Indicator	SMEs				Large Firms			
	Percentage			Index ²	Percentage			Index ²
	Higher	Same	Lower	52	Higher	Same	Lower	53
Economic growth	35	40	25	54	24	62	15	53
Economic activity								
Production	45	27	28	57	56	24	21	64
Domestic sales	40	31	30	54	55	18	27	62
Exports	60	16	24	66	36	55	9	59
Inventory	35	40	26	47	30	39	30	50
Level of capacity utilization	13	74	14	50	19	69	13	52
Prices								
Final product prices	58	39	4	69	68	24	9	74
Intermediate input prices	78	22	0	18	97	3	0	3
Wage level	32	68	0	59	47	53	0	65
Primary inputs								
Investment	11	81	8	51	18	76	6	53
Employment	13	78	9	51	18	76	6	53

Table A4: Survey Results: Summary of Outlook of all Firms (by size) (July-August-September 2017)¹

Indicator	SMEs				Large Firms			
	Percentage			Index ²	Percentage			Index ²
	Higher	Same	Lower	54	Higher	Same	Lower	57
Economic growth	32	49	19	54	32	56	12	57
Economic activity								
Production	47	28	25	59	56	26	18	65
Domestic sales	52	31	17	63	61	24	15	68
Exports	50	35	15	63	45	50	5	64
Inventory	38	54	8	40	19	69	13	48
Level of capacity utilization	26	65	9	55	41	56	3	62
Prices								
Final product prices	69	30	1	76	68	26	6	74
Intermediate input prices	89	11	0	10	91	9	0	8
Wage level	47	53	0	65	50	50	0	67
Primary inputs								
Investment	26	68	6	56	36	58	6	60
Employment	16	81	3	53	18	79	3	54

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

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