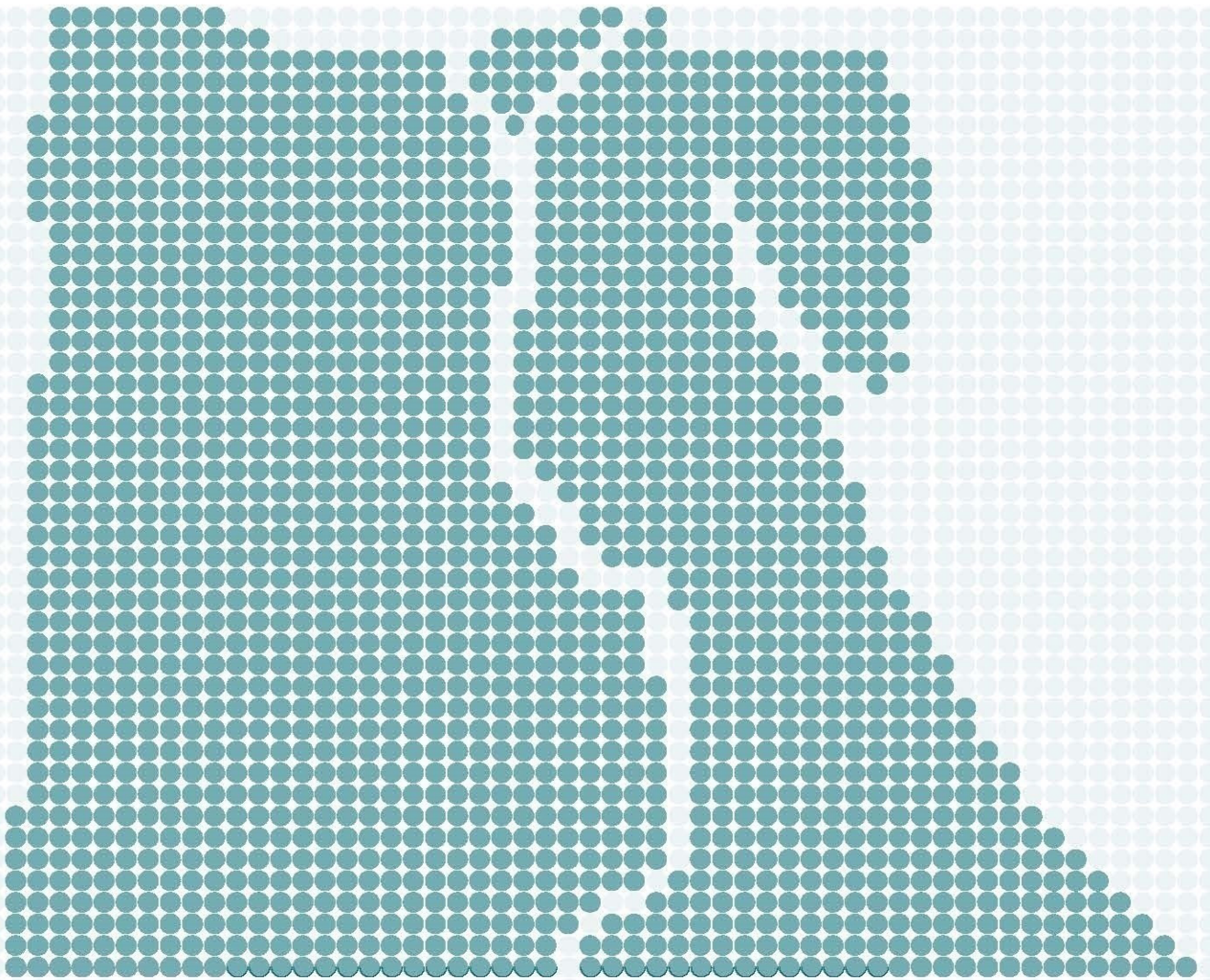




المركز المصري للدراسات الاقتصادية
The Egyptian Center for Economic Studies

Business Barometer

Issue 46 2018



Performance & Expectations of the Egyptian Business Sector

About the Egyptian Center for Economic Studies

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.

Strategic Direction

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.

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Business Barometer

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About the Business Barometer

About the Business Barometer

The Egyptian Center for Economic Studies (ECES) publishes its Business Barometer (BB) survey quarterly as part of its role in providing timely information about the developments of the economic activity in Egypt based on macroeconomic indicators. The survey covers firms' assessment of economic growth and results of own operations during the quarter under study as well as their outlook for the Egyptian economy and in terms of own production, domestic sales, exports, commodity inventories, capacity utilization, prices, wages, employment and investment.

The surveyed firms cover manufacturing (50 percent), financial services (13 percent), construction (12 percent), transportation (10 percent), tourism (9 percent) and telecommunications (7 percent). The survey is conducted on a number of micro, small, medium and large firms as defined by the Central Bank of Egypt (CBE). ECES launched its first Business Barometer in 1998.

This edition of BB covers firms' assessment of economic growth and results of their operations in the second quarter of FY2017/2018 (October-December 2017). It also summarizes their expectations for overall economic performance as well as their own activities for the third quarter of FY2017/2018 (January-March 2018).

Methodology

The BB Index is a simple average of the sub-indices of surveyed variables (production, domestic sales, exports, inventory, capacity utilization, prices, wages, employment and investments). The Index is calculated once for large firms and once for SMEs, both for evaluation and expectations.

Index Value	Index Definition
50 points	Same (no change in firms' performance and expectations)
Above 50 points	Higher (improvement in firms' performance and expectations)
Below 50 points	Lower (decline in firms' performance and expectations)

The index is calculated for each variable using the following equation:

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

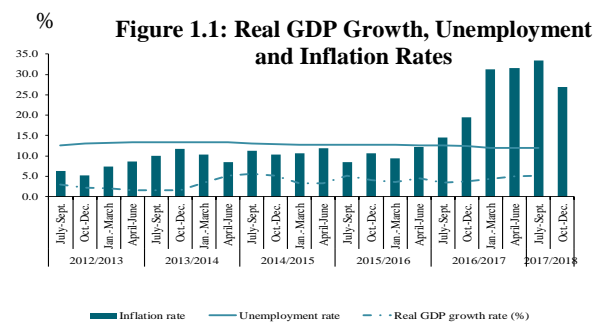
Where *I* is the share of firms reporting an increase and *S* the share of firms reporting "same."

The index is designed to have a maximum of 100 points 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 neutralized 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 in these two variables reflect an adverse business climate for firms.

Overview

The quarter under study saw a continuation of reforms adopted by the government over the past years. Most importantly, issuing the executive regulations of the investment law, launching the first map of industrial investment, lifting caps on deposits and withdrawals imposed on importers of non-essential goods, resuming direct flights between Moscow and Cairo, receiving the third tranche of the IMF loan, and the onstreaming of Zohr gas field. Following the economic reforms initiated by Egypt, S&P revised its outlook for Egypt from stable to positive.

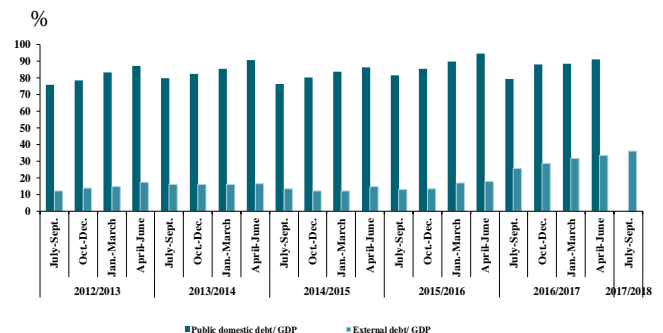
These efforts were reflected in the continued recovery of a number of macro indicators, including the GDP growth rate, which rose to 5.2 percent in the first quarter (July-September) of FY2017/2018, compared to 3.4 percent during the corresponding period of the previous fiscal year. The higher growth rate was reflected in a slight decrease in unemployment to 11.98 percent in Q1 of FY2017/2018 compared to about 12.6 percent during the corresponding quarter of FY2016/2017 the lowest level in the last two years. Inflation also fell in the quarter under review to 26.9 percent on average, from 33.4 percent in the previous quarter (Figure 1.1).



Sources: MoF, Monthly Statistical Bulletin, various issues; CAPMAS.
* Data for real GDP growth rate for the period (January- March 2016/ 2017) is preliminary and may be revised.
* Data for real GDP growth rate for (April-May 2016/ 2017 and July-September 2017/ 2018) is based on a press release.

On the fiscal side, recent economic reforms adopted since 2016 led to further improvement in some fiscal indicators, including decline in the percentage of overall deficit to GDP to 2 percent during July-September 2017 compared to 2.2 percent during the corresponding period last year. This decline is mainly due to increased public revenues at a rate higher than that of spending. The government policy of financing this deficit by issuance of bonds and T-bills in domestic or foreign currency continued, raising domestic debt to about LE 3160.9 billion at end of June 2017 (93 percent of GDP). External debt also rose to \$80.8 billion by end of Q1 of FY2017/2018 compared to \$79 billion at end of Q4 of FY2016/2017 (Figure 1.2).

Figure 1.2: Public Debt (% of GDP)

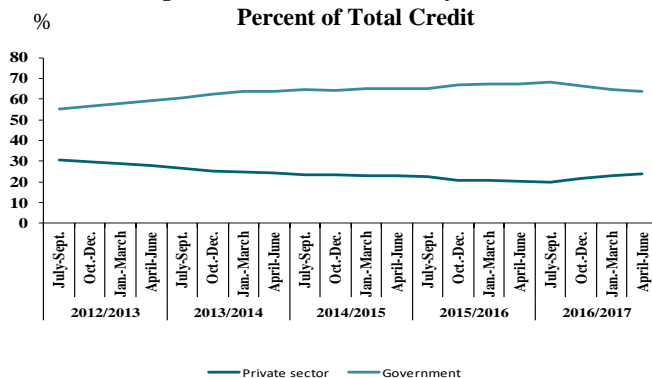


Source: Central Bank of Egypt (CBE), Monthly Statistical Bulletin, various issues.
External debt/ GDP in Q1 of FY2017/ 2018 is preliminary.

Increased debts and continued borrowing negatively affect the competitiveness of the Egyptian economy, exercise more pressure on state finances and limit its ability to meet the constitutional entitlements that require increased spending on education, health and scientific research.

Government dependence on external debt has recently increased, leading to a slight improvement in the amount of credit available to the private sector since late 2016. It is worth noting that lower credit availability to the private sector to finance economic activities may lead to further economic recession and the consequent decline in public revenues (Figure 1.3).

Figure 1.3: Domestic Credit by Sector as a Percent of Total Credit

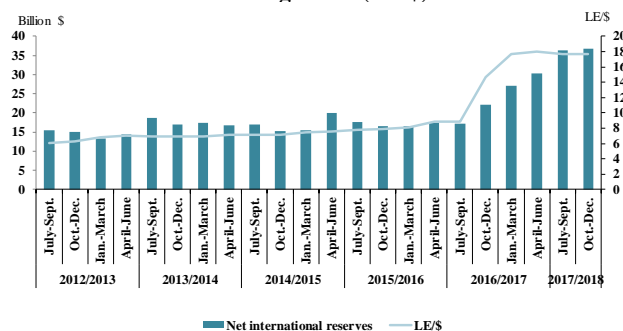


Source: Central Bank of Egypt (CBE), *Monthly Statistical Bulletin*, various issues.

Net international reserves increased slightly on average in the quarter under review (October-December 2017) to \$36.8 billion compared to \$36.2 billion in the preceding quarter of the same fiscal year. This increase is due to the decline in trade deficit and the increase in tourism and Suez Canal revenues. However, a closer look into the structure of international reserves shows that a large portion thereof is from direct loans and foreign investments in T-bills. Foreign investments in T-bills rose by \$7.4 billion on a net basis in Q1 of FY2017/2018, while the proceeds from exports, Suez Canal transit fees, and remittances combined amounted to \$4.3 billion during the same period. This reflects the instability of the sources of these reserves, which may exit the economy suddenly, and the need to increase sustainable sources of international reserves.

It should also be noted that the average exchange rate against the dollar appreciated slightly in the relevant quarter to LE 17.65 compared to LE 17.73 in the previous quarter (Figure 1.4).

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



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

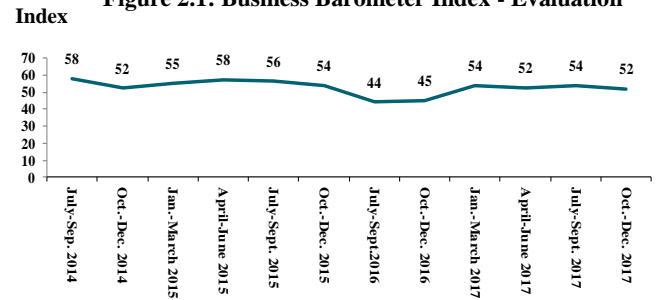
Business Barometer Index (BBI)

Higher outlook index and continued improvement of past performance

The overall performance of businesses continued to improve during the relevant quarter, with the evaluation index reaching 52 points. Though lower than the previous quarter, this index is higher compared to the corresponding quarter of the previous fiscal year (Figure 2.1). The survey results also reflect more optimistic expectations for the third quarter (January-March 2018) compared to the previous quarter, recording 59 points (Figure 2.2).

The survey results reflect improved performance of large firms during October-December 2017, as the evaluation index for large firms rose during the relevant quarter compared to the previous quarter (July–September 2017). The performance of SMEs remained unchanged, registering lower performance (see the Methodology) compared to the previous quarter. The diverging performance may be attributed to the better ability of large firms to cope with ramifications of the economic measures compared to SMEs. This highlights the need to support SMEs to help them continue in business. The outlook is optimistic for both large firms (Figure 2.3) and SMEs (Figure 2.4) for the next quarter (January-March 2018).

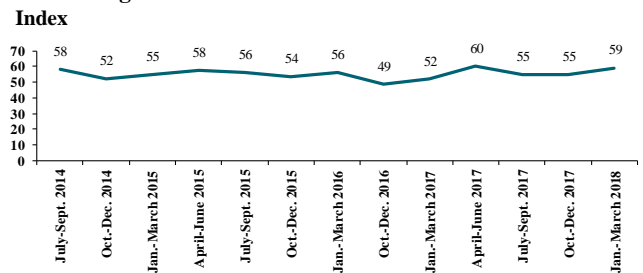
Figure 2.1: Business Barometer Index - Evaluation



Source: Survey results.

** Data for the two quarters of January-March and April-June 2016 are unavailable.

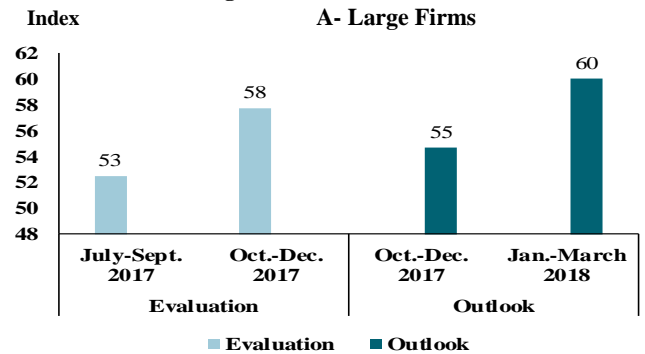
Figure 2.2: Business Barometer Index - Outlook



Source: Survey results.

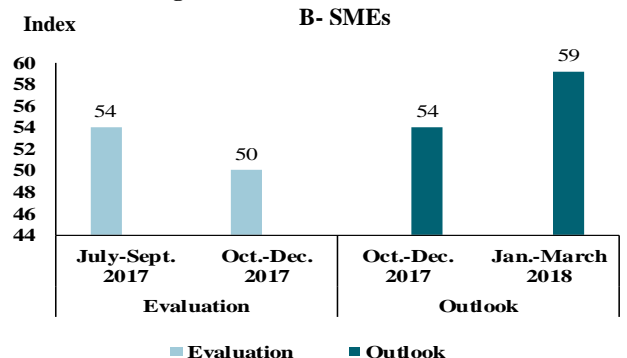
* Data for the two quarters of April-June, and July-September 2016 are unavailable.

Figure 2.3: Business Barometer Index A- Large Firms



Source: Survey results.

Figure 2.4: Business Barometer Index B- SMEs



Source: Survey results.

Past Performance of Businesses

Improved economic activity for large firms and SMEs

At the economic activity level, large firms reported high domestic sales and exports during the quarter under review (October-December 2017), leading to an increase in production and capacity utilization, and reflecting positively on the economic growth index. These results are consistent with the official data released by the Ministry of Planning, which show increased real GDP growth rate. However, the inventory rose during the quarter under review, indicating firms' concern about possible changes in the exchange rate or trade policy, thus maintaining higher inventory (Figure 3.1).

Past performance indicators for SMEs were lower compared to large firms, with the former reporting positive views regarding domestic sales and exports during the period October-December 2017, though lower than the previous quarter, resulting in a slightly higher production index and unchanged capacity utilization. This was reflected in unchanged inventory for SMEs (see the Methodology), asserting the need to revisit government measures in support of these enterprises (Figure 3.2).

Sectorally, the service sector reported better performance than the manufacturing sector, as shown in Appendix Table 1. Within the service sector, communications recorded the best performance, which may be attributed to increased production and domestic sales of the surveyed firms, followed by the construction sector due to increased investments, financial intermediation, tourism due to increased tourist arrivals during the

quarter under review, and transportation. The manufacturing sector, however, saw a slight improvement in overall performance due to increased production in the quarter under review.

Figure 3.1: Economic Activity
 A. Evaluation: Large Firms

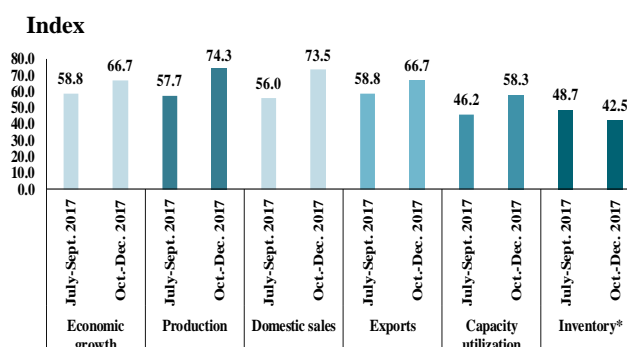
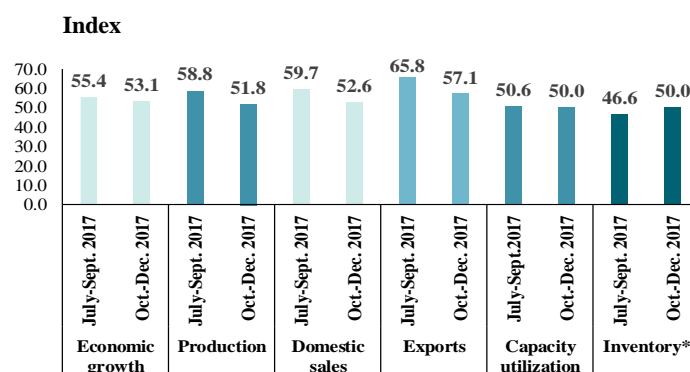


Figure 3.2: Economic Activity
 B. Evaluation - SMEs



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 inventory and vice versa.

Increased input and final product prices

The past performance assessment of large firms and SMEs showed a continued rise in the prices of inputs and final products as well as in wages, though slightly lower than the previous quarter. The inputs index dropped below 50 points for all firms, indicating higher prices of their products during the quarter under review. However, a comparison of prices with those of the previous quarter shows that small firms suffer more than large firms from higher input prices (Figures 3.3 and 3.4).

Improved investment and unchanged employment indices

The investment index improved during the quarter under review for large as well as medium and small firms. This can be attributed to optimism resulting from the serious reform measures taken by the government to improve the investment climate, such as issuance of the executive regulations of the investment law and those of the law on facilitating industrial licensing procedures. Comparing the index values in the quarter under review with those of the previous quarter shows that the investment index for large firms improved, but fell by two points for SMEs. The results also show that the employment index for both large firms and SMEs remained unchanged (Figures 3.5 and 3.6).

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

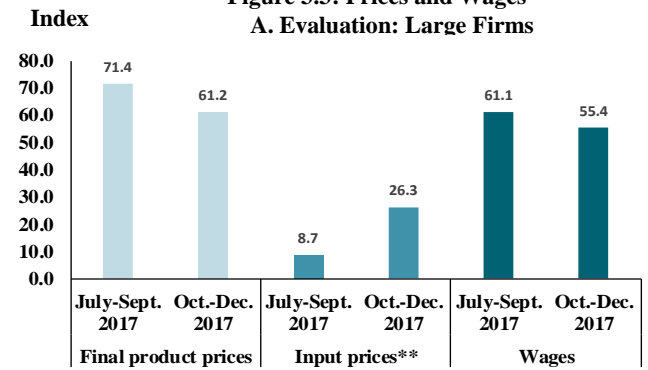


Figure 3.4: Prices and Wages
B. Evaluation: SMEs

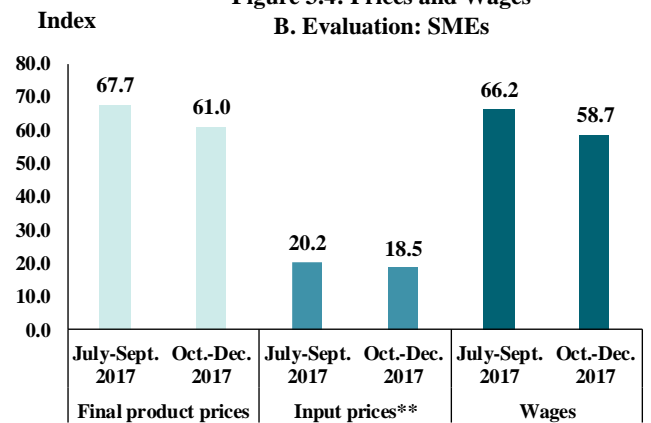


Figure 3.5: Investment and Employment
A. Evaluation: Large Firms

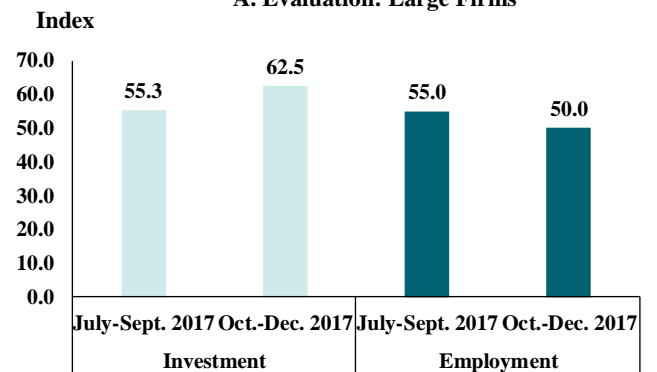
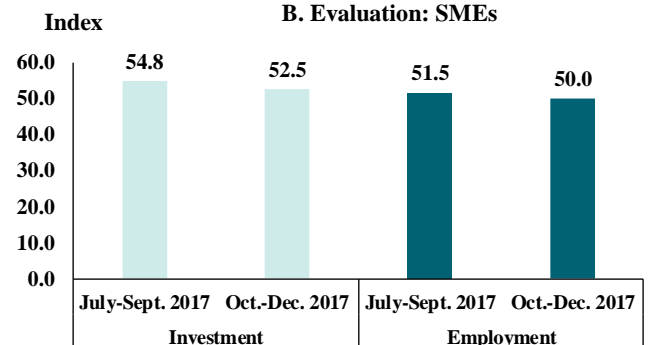


Figure 3.6: Investment and Employment
B. Evaluation: SMEs



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.

Business Strategy Going Forward

Expectations of improved economic activity for businesses

Survey results for SMEs were similar to those of large firms in the quarter under review for all economic indicators. Businesses expect increased domestic sales, exports, production and capacity utilization. This may be attributed to continued positive perceptions regarding the economic growth compared to the previous quarter and commitment of the sample firms to their future production plans (Figures 4.1 and 4.2).

Sectorally, Appendix Table 2 shows that expectations of services and manufacturing firms for the coming quarter are positive in general. However, the highest expectations came from firms operating in financial services, followed by telecommunications and tourism, then the construction sector. The lowest expectations came from the manufacturing and transportation sectors, which may be attributed to continued problems faced by both sectors, leading to limited future contractual engagements.

Figure 4.1: Economic Activity
 A. Outlook: Large Firms

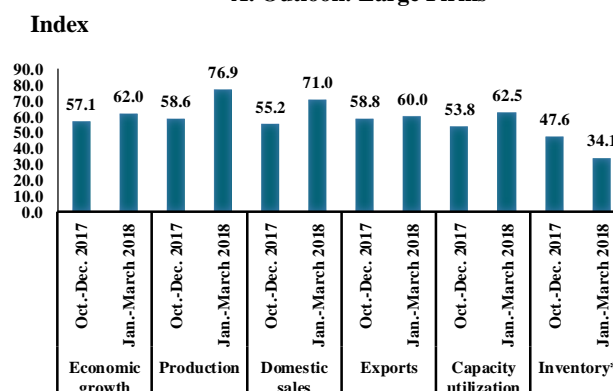
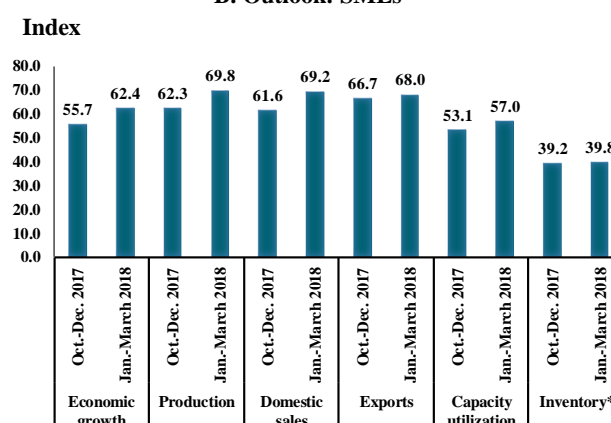


Figure 4.2: Economic Activity
 B. Outlook: SMEs



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.

Expectations of continued rise in the prices of final products and inputs, and in wages

Most large firms expect final product prices and wages to continue rising, exceeding the previous quarter. They also expect a similar trend for input prices, albeit slightly less than in the previous quarter (Figure 4.3), which can be explained by expectations of further reduction in petroleum subsidies and continued rise in energy prices. SMEs results were similar to those of the large firms (Figure 4.4).

Expectations of higher investment and employment indices

Most large firms and SMEs expect higher investment during the quarter January-March FY2017/2018 compared to the previous quarter. However, large firms expect employment to remain unchanged, while SMEs expect higher employment, which is in line with their expectations for economic activity (Figures 4.5 and 4.6).

Figure 4.3: Prices and Wages
A. Outlook: Large Firms

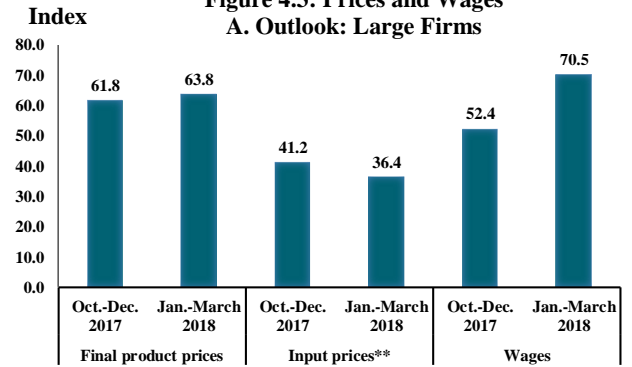


Figure 4.4: Prices and Wages
B. Outlook: SMEs

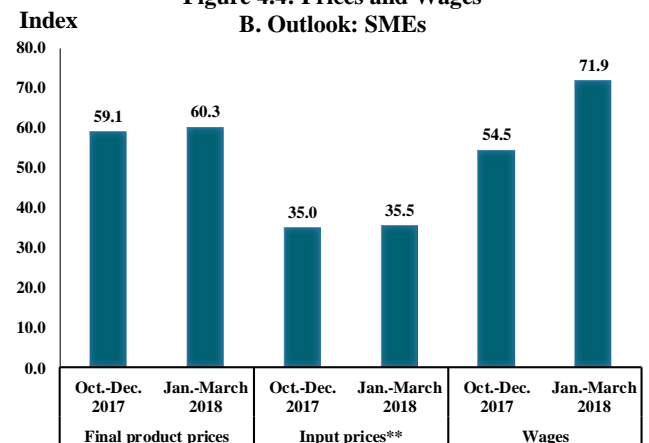


Figure 4.5: Investment and Employment
A. Outlook: Large Firms

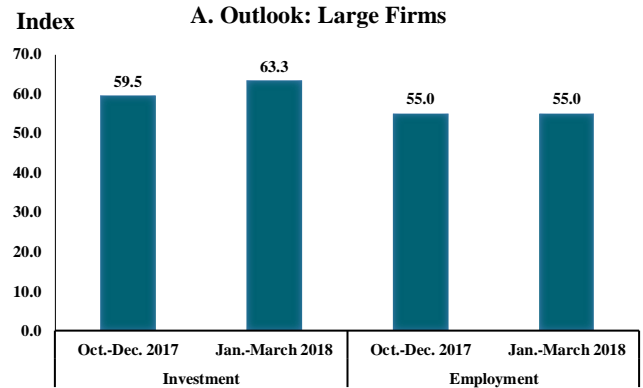
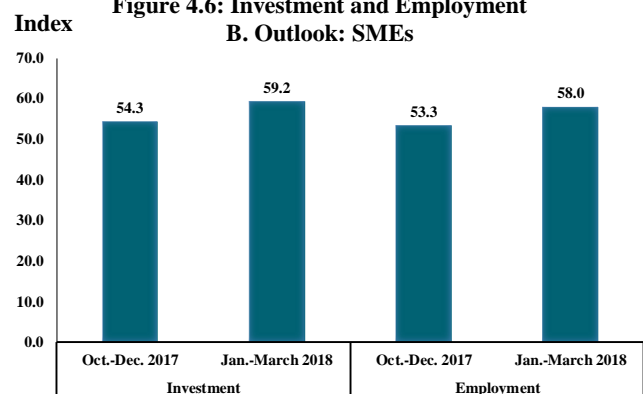


Figure 4.6: Investment and Employment
B. Outlook: SMEs



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.

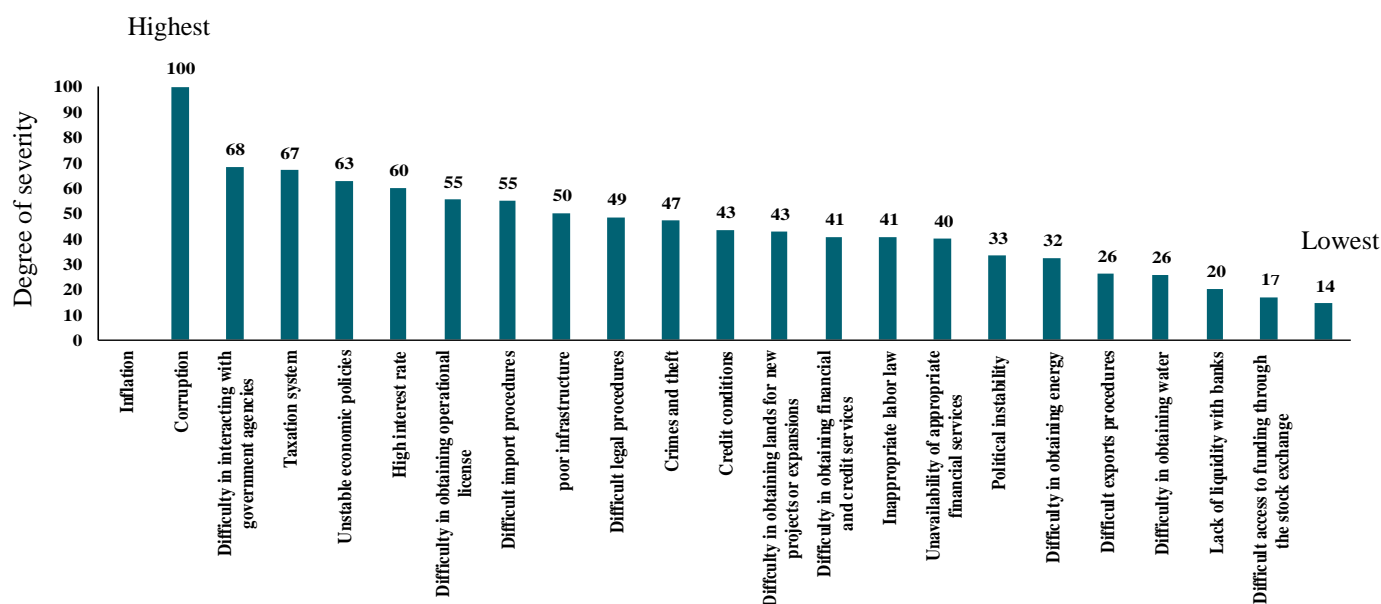
Business Constraints

Major constraints facing the business sector:

Major constraints: inflationary pressures, corruption, difficulty in interacting with government authorities and the tax system

Figure 5 shows the major constraints that faced businesses during the surveyed period, arranged in a descending order of severity. In particular, firms expressed concern about rising inflation, corruption, difficulty in interacting with government authorities, and the tax system. It is worth noting that the order of constraints remains relatively similar to that of the previous survey, indicating minimal progress in removing constraints. It is worth noting that obtaining funding from the stock market was ranked as the least constraint.

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



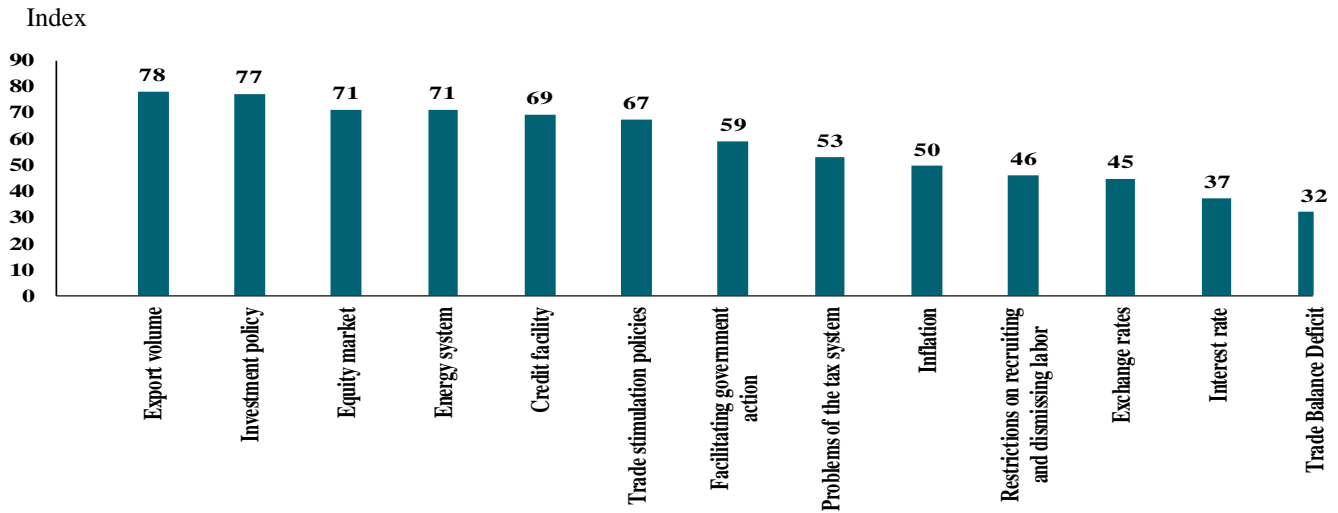
Source: Survey results.

Policy Expectations

Expected improvement in exports, investment policy, stock market and energy system

According to Figure 6, most firms expect improvements in exports in the coming quarter and in investment policy due to availing a more enabling environment to increase foreign direct investments. They also expect improvement in the stock market due to the recent amendments to the capital market law. Firms also expect improvement in the energy system due to the government's efforts in establishing new and renewable energy projects as well as availing an opportunity for investors to invest therein.

Figure 6: Policy Expectations



Source: Survey results.

Table A-1: Survey results - Summary of Past Performance of All Firms (by Sector) October-November-December 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				
	Higher	Same	Lower	51	Higher	Same	Lower	56	Higher	Same	Lower	51	Higher	Same	Lower	51	Higher	Same	Lower	57	Higher	Same	Lower	54
Economic growth	35	38	26	53	46	38	15	61	36	45	18	56	38	50	13	58	38	63	0	62	44	50	6	63
Economic activity																								
Production	43	16	40	51	54	31	15	65	45	18	36	54	63	13	25	67	63	25	13	70	56	25	19	65
Domestic sales	40	19	40	50	62	23	15	69	55	18	27	62	63	13	25	67	63	25	13	70	56	25	19	65
Exports	55	25	20	64	33	33	33	50	50	0	50	50	50	50	0	67	33	67	0	60	0	100	0	50
Inventory	24	50	26	51	23	46	31	53	20	50	30	53	50	50	0	33	50	13	38	44	31	63	6	42
Capacity utilization	12	76	12	50	15	85	0	54	9	82	9	50	25	75	0	57	38	63	0	62	13	81	6	52
Prices																								
Final product prices	39	52	9	60	69	31	0	76	55	36	9	67	25	63	13	54	38	50	13	58	31	63	6	58
Intermediate input prices	75	22	3	21	92	8	0	7	71	29	0	22	100	0	0	0	71	29	0	22	29	71	0	42
Wage level	28	70	1	58	46	54	0	65	36	64	0	61	13	88	0	53	25	75	0	57	13	88	0	53
Primary inputs																								
Investment	21	72	7	54	31	62	8	57	18	55	27	47	25	75	0	57	50	50	0	67	20	80	0	56
Employment	9	76	15	48	31	54	15	55	9	64	27	44	0	100	0	50	25	63	13	54	19	69	13	52

Table A2. Survey Results: Summary of Outlook of all firms (by Sector) January-February-March 2018)¹

Indicator	Manufacturing				Construction				Tourism				Transport				Communications			Financial Intermediaries				
	Percentage			Index ²	Percentage			Index ²	Percentage			Index ²	Percentage			Index ²	Percentage			Index ²				
	Higher	Same	Lower	59	Higher	Same	Lower	60	Higher	Same	Lower	61	Higher	Same	Lower	53	Higher	Same	Lower	61	Higher	Same	Lower	63
Economic growth	44	47	9	62	62	31	8	71	45	55	0	65	38	50	13	58	25	75	0	57	38	63	0	62
Economic activity																								
Production	61	25	13	69	54	38	8	67	64	27	9	71	50	38	13	64	75	25	0	80	56	44	0	70
Domestic sales	64	24	12	71	62	31	8	71	55	36	9	67	50	38	13	64	75	13	13	78	81	19	0	84
Exports	55	20	25	63	33	67	0	60	60	40	0	71	0	100	0	50	67	33	0	75	100	0	0	100
Inventory	38	49	12	41	31	69	0	41	50	50	0	33	50	38	13	36	50	25	25	40	63	38	0	27
Capacity utilization	36	57	7	59	31	62	8	57	36	64	0	61	38	63	0	62	29	71	0	58	13	88	0	53
Prices																								
Final product prices	42	54	5	62	38	62	0	62	45	55	0	65	38	63	0	62	25	75	0	57	25	75	0	57
Intermediate input prices	50	50	0	33	46	54	0	35	0	100	0	50	50	50	0	33	43	57	0	36	33	67	0	40
Wage level	61	39	0	72	54	46	0	68	64	36	0	73	38	63	0	62	50	50	0	67	75	25	0	80
Primary inputs																								
Investment	37	61	1	61	38	62	0	62	27	73	0	58	13	75	13	50	50	50	0	67	31	69	0	59
Employment	31	63	6	58	38	62	0	62	27	73	0	58	0	88	13	47	25	63	13	54	25	69	6	56

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 Methodology.

Table A3. Survey Results: Summary of Past Performance of all Firms (by size) (October-November-December 2017)¹

Indicator	SMEs				Large Firms			
	Percentage			Index ²	Percentage			Index ²
	Higher	Same	Lower	50	Higher	Same	Lower	58
Economic growth	33	42	24	53	52	45	3	67
Economic activity								
Production	41	22	37	52	71	13	16	74
Domestic sales	41	24	35	53	71	10	19	74
Exports	37	47	16	57	64	7	29	67
Inventory	22	56	22	50	45	29	26	43
Level of capacity utilization	8	85	8	50	35	55	10	58
Prices								
Final product prices	42	48	10	61	39	58	3	61
Intermediate input prices	78	21	1	18	66	31	3	26
Wage level	30	68	1	59	19	81	0	55
Primary inputs								
Investment	18	74	9	53	42	55	3	63
Employment	14	72	14	50	10	81	10	50

Table A4. Survey Results: Summary of Outlook of all Firms (by size) (January-February-March 2018)¹

Indicator	SMEs				Large Firms			
	Percentage			Index ²	Percentage			Index ²
	Higher	Same	Lower	59	Higher	Same	Lower	60
Economic growth	45	46	9	62	39	61	0	62
Economic activity								
Production	62	26	12	70	71	26	3	77
Domestic sales	61	27	12	69	61	35	3	71
Exports	60	25	15	68	43	43	14	60
Inventory	40	49	10	40	52	42	6	34
Level of capacity utilization	29	64	7	57	40	60	0	63
Prices								
Final product prices	36	60	3	60	43	57	0	64
Intermediate input prices	45	55	0	36	43	57	0	36
Wage level	61	39	0	72	58	42	0	70
Primary inputs								
Investment	33	65	2	59	42	58	0	63
Employment	32	63	5	58	19	77	3	55

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 Methodology.