

Executive Summary

Key Highlights...

On the fiscal side, budget deficit continued to ease during the period July-April 2013/2014, reaching LE 163.3 billion, which represents 8 percent of GDP, compared to 10.5 percent a year earlier. This was mainly due to an increase in tax revenues and exceptional grants, accompanied with a slower rate of implementation in investments during the period of study. Moreover, total government debt (domestic and external) reached LE 1746 billion (85.9 percent of GDP) in December 2013, compared to LE 1644 billion (94 percent of GDP).

As for the external debt, it is important to highlight that:

§ **External debt service to exports of goods and services ratio** has been unchanged since 2008/2009 till 2012/2013 stabilizing at an average of 6.2 percent. Furthermore, this ratio declined at end of December to reach 5 percent, thus indicating a safer level to meet debt service obligations.

§ **Short-term debt to total external debt ratio** decreased from 17.1 percent at end of December 2012 to 6.2 percent at end of December 2013. This could be explained mainly for redeeming Qatari short-term deposit worth US\$ 2 billion by end of December 2013, in addition to another matured deposit worth US\$ 1 billion.

As for the monetary developments, M2 annual growth continued to decelerate slightly for the third month in a row, reaching **16.3** percent at end of March 2014 compared to 17 percent recorded in February 2013, and compared to an average of **18.3** percent during the first 8 months of the year 13/14. Such deceleration did have a proportional impact on Headline Urban inflation, which declined to 8.9 percent in April 2014 (the lowest inflation recorded since May 2013), compared to 9.8 percent in March 2014.

Moreover, during its **Monetary Policy Committee** meeting held on May 29, 2014, CBE decided to keep **overnight deposit rate, overnight lending rates, and CBE's main operation**, and the **discount rate** unchanged at its current levels. Meanwhile, during April 2014, **Net International Reserves (NIR)** increased merely by US\$ 0.08 billion to record US\$ 17.49 billion, up from US\$ 17.41 billion in March 2014, thus recording a y-o-y growth of 21.3 percent.

With regards to the real sector, real GDP growth came at a 1.2 percent in H1-FY13/14, compared to 2.4 percent a year earlier, mainly in light of security reasons and political developments during this period. **Concerning lead indicators, EGX-30 increased by 5.8 percent to record 8256 points in April 2014**, compared to the previous month. However, latest figures show the industrial production index have decreased by 6 percent to record 168.1 points in March 2014, compared to the previous month, however, this is still higher than the December 2013 level of 151.6.

Fiscal Sector:

Budget Deficit continued to decline during the first 10 months of FY 2013/2014 in value and as percent of GDP, compared to the same period last year. This was mainly due to an increase in tax revenues and exceptional grants, with a slower rate of implementation in investments.

Budget Deficit
continued its
decelerating
trend...

July- April 13/ 14 Budget Deficit	July- April 12/ 13 Budget Deficit
LE 163.3 billion (8 percent of GDP)	LE 184.8 billion (10.5 percent of GDP)
Revenues	Revenues
LE 314.8 billion (15.5 percent of GDP)	LE 240.1 billion (13.7 percent of GDP)
Expenditure	Expenditure
LE 471.8 billion (23.2 percent of GDP)	LE 423.1 billion (24.1 percent of GDP)

Source: Ministry of Finance, Macro Fiscal Policy Unit

Both Tax and Non-Tax Revenues increased during the period of study...

On the revenue side,

- Total revenues increased significantly during July-April 2013/2014 by 31 percent, recording LE 314.8 billion (15.5 percent of GDP), mainly due to the increase in both tax revenues by 9.9 percent (9.6 percent of GDP), and non-tax revenues by 91.4 percent (5.9 percent of GDP).

Tax Revenues increased due to:

Taxes on Income, Capital Gains and Profits increased by LE 15.7 billion (21 percent growth) to reach LE 90.4 billion (4.4 percent of GDP)

Mainly on the back of an increase in:

- Taxes on domestic salaries by LE 2.1 billion
- Taxes on industrial & commercial profits by LE 1.5 billion
- Receipts from EGPC by LE 14.9 billion to reach LE 30.6 billion (1.5 percent of GDP), after including the first settlement in December 2013, and the second settlement in January 2014.
- Receipts from Other Companies by LE 1.8 billion.
- Receipts from Suez Canal by LE 0.2 billion.

Taxes on Property increased by LE 2.1 billion (15 percent growth) to reach LE 15.9 billion (0.8 percent of GDP)

Mainly as a result of an increase in Taxes on T-bills and bonds payable interest by 17.4 percent y-o-y to LE 13.1 billion (0.6 percent of GDP)

Taxes on International Trade increased by LE 0.5 billion (3.6 percent growth) to reach LE 13.6 billion (0.7 percent of GDP)

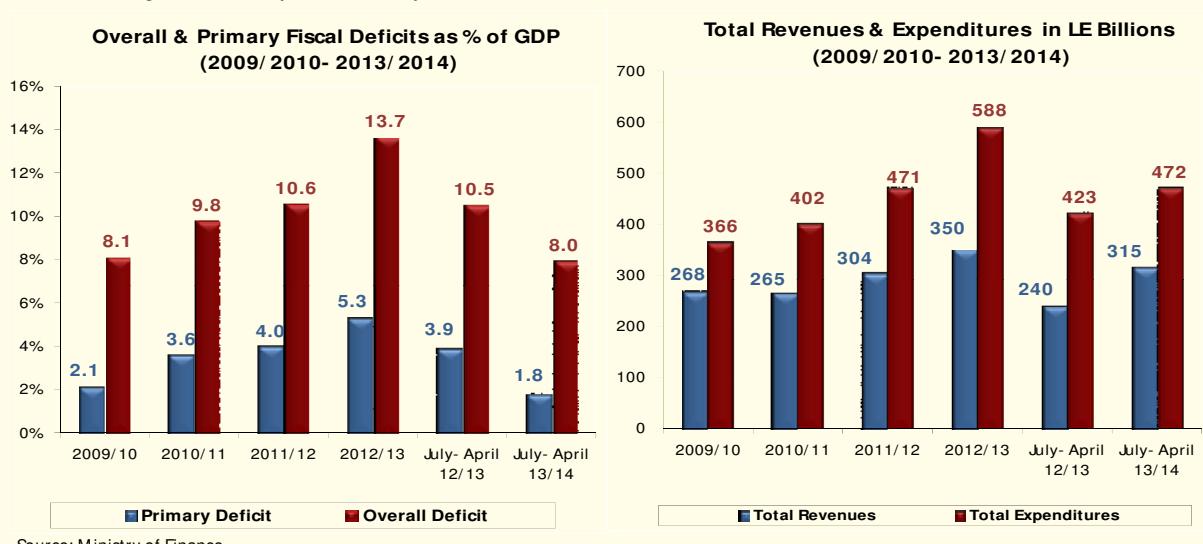
In light of an increase in taxes on valued customs by 6.3 percent y-o-y to LE 13 billion (0.6 percent of GDP)

- The abovementioned increase came despite of;

- o The decline of excises on domestic commodities by 17 percent (particularly the decline in sales tax on petroleum products)
- o The decline in general sales tax on services by 7.2 percent (particularly the decline in tax receipts from hotel and restaurant, communication services and operating services).

Moreover, the significant increase in non-tax revenues could be explained in light of the following:

- Increase in grants to reach LE 51.4 billion during July-April 2013/2014 (2.5 percent of GDP), mainly due to:
 - a) LE 29.7 billion increase in grants—half of the dollar denominated deposits at the central bank- to be allocated to finance the first stimulus package related to the presidential decree no. 105, 2013.
 - b) LE 21 billion (the equivalent of US\$ 3 billion) cash grants from Gulf countries.
- Increase in dividends collected from EGPC by LE 7 billion, dividends collected from Central Bank by LE 1.8 billion, and dividends collected from Suez Canal by LE 1.8 billion.
- Increase in revenues from sales of goods and services by 35 percent y-o-y to LE 17 billion (0.8 percent of GDP) due to the increase in revenues from special accounts and funds¹ by LE 3.8 billion to record LE 13.8 billion in the period of study compared to LE 10 billion during the same period last year.



¹ The increase comes in light of the law number 19 for the year 2013, which stipulated that budget entities should pay to the Ministry of Finance 10 percent of the revenues from special accounts and funds; additionally, 25 percent of the outstanding balance was repaid to the treasury in 30/6/2013.

On the Expenditures Side:

Total expenditures increased during July- April 2013/2014 by 11.5 percent, recording LE 471.8 billion (23.2 percent of GDP), mainly due to:

- The increase in wages and compensation of employees by LE 26.2 billion to LE 139 billion (6.8 percent of GDP).
- The increase in subsidies grants and social benefits by LE 2.6 billion to LE 128 billion (6.3 percent of GDP) in light of the following:-
- **Payments to pension funds increased by LE 13.6 billion** during July-April 13/14 (of which an increase of LE 2.4 billion only in April 2014), to reach LE 26.8 billion, compared to LE 13.2 billion during the same period last year.
- The increase in subsidies to electricity to record LE 11 billion, compared to LE 1 billion only during the same period (due to the increase in fuel subsidies which is used in power generation).
- The increase of Social insurance Pension to record LE 4.1 billion compared to LE 3.2 billion increasing by 28 percent.
- The increase in interest payments by LE 10 billion to LE 126.5 billion (6.2 percent of GDP).
- The rise in other expenditures by LE 3.8 billion to LE 30.1 billion (1.5 percent of GDP).
- The increase in purchases of non-financial assets (investments) by LE 6.4 billion (1.5 percent of GDP). It is worthy to note that some LE 30.3 billion were disbursed as purchases of non-financial assets (investments) during the first 10 months of 2013/2014, increasing by 26.6 percent compared to the same period last year, while investments are expected to increase further during the coming period.

Going forward, the government's strategy to lower budget deficit, and achieve social justice consists of two pillars: First, on the revenue side, restructuring the tax system to allow for a fair distribution of the tax burden. In addition, other strategies that include countering tax evasion, widening the tax base will be implemented. Meanwhile, other revenues boosters include the introduction of the new Property Tax Law, and the new mining law.

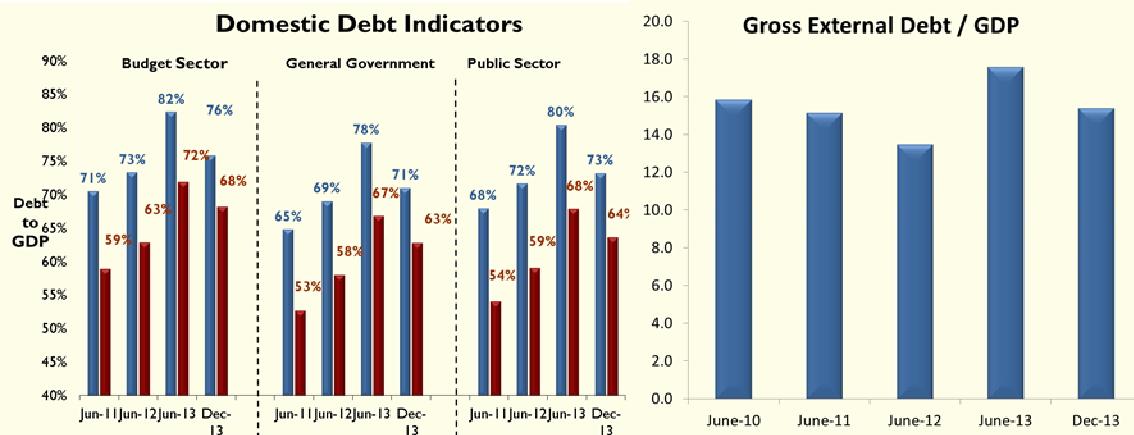
The second pillar envisages expenditure side reforms, that focus on re-prioritize public spending in favor of protecting the poor and most vulnerable groups, with specific focus on energy subsidies reform.

Meanwhile, the Ministry of finance approved disbursements to be allocated to the ministries and public institutions, for the aim of improving the services provided to citizens, and providing them with basic commodities. Furthermore, additional spending will be allocated to important social programs, such as, supporting women-headed households, and supporting children at the pre-school level.

*Increase in
Domestic Debt...*

Domestic budget sector debt recorded LE 1544 billion (75.9 percent of GDP) by end of December 2013, compared to LE 1294 billion (73.8 percent of GDP) by end of December 2012.

It is worth mentioning that the total government debt (domestic and external) reached LE 1746 billion (85.9 percent of GDP) in December 2013, compared to LE 1644 billion (94 percent of GDP) at end of June 2013, and LE 1459 billion (83.2 percent of GDP) in December 2012.



Source: Ministry of Finance

External debt stock² (government and non-government debt) recorded US\$ 45.8 billion by the end of December 2013 compared to US\$ 38.8 billion by the end of December 2012 (most of the increase represented aid from the Gulf Countries with concessional and preferential terms). External debt as percent of GDP recorded 15.5 percent by the end of December 2013, which is relatively low if compared to the average of peer countries (Middle East and North Africa countries recorded an average of 25.5 percent of GDP during the year 2013).

Main External debt indicators are as follows:

§ **External debt service to exports of goods and services ratio** has been unchanged since 2008/2009 till 2012/2013 stabilizing at an average of 6.2 percent. Furthermore, this ratio declined at end of December to reach 5 percent, thus indicating a safer level to meet debt service obligations.

§ **Short-term debt to total external debt ratio** decreased from 17.1 percent at end of December 2012 to 6.2 percent at end of December 2013. This could be explained mainly for redeeming Qatari short-term deposit worth US\$ 2 billion by end of December 2013, in addition to another matured deposits worth US\$ 1 billion.

2 The notable increase in non-government external debt during the first half of the fiscal year 2013/2014 can be explained in light of a net increase of nearly US\$ 4.4 billion in external debt on the monetary authorities compared to end of December 2012/2013. The breakdown of inflows is as follows: US\$ 2 billion from UAE, US\$ 2 billion from Saudi Arabia and US\$ 3 billion from Kuwait. Meanwhile the Qatari short term deposit worth US\$ 2 billion was cancelled and a Qatari deposit worth US\$ 1 billion was converted into T-bonds during the period of study. Moreover, it is important to highlight that Egypt has returned another matured deposits worth US\$ 1 billion to Qatar during the period of study.

Monetary Perspective:

M2 reached an annual real growth rate of 6.5 percent...

According to recent data released by the CBE, M2 annual growth continued to decelerate slightly for the third month in a row, reaching **16.3** percent at end of March 2014 (LE 1438 billion), compared to 17 percent recorded in February 2014, and compared to an average of 18.3 percent during the first 8 months of the year 13/14. The slight decrease witnessed in M2 could be explained from the liabilities side in light of a slower increase in money growth reaching 19 percent during the month of study (LE 388.7 billion), compared to an average of 26.9 percent during the first 8 months of the year. Meanwhile, annual growth of quasi money remained almost unchanged at 15.3 percent (LE 1049.8 billion), compared to an average of 15.4 percent during the first 8 months of the year.

Moreover – on the asset side – **net domestic assets of the banking system** annual growth showed a similar pattern during the month of study recording an annual growth of 18.6 percent (LE 1314 billion), compared to an average of 22.9 percent during the first 8 months of the year, as growth in **net claims on the government** decelerated to 27.7 percent (LE 960 billion), compared to an average of 35 percent during the first 8 months of the year. **This could be partly explained in light of the annual decline witnessed in credit facilities to the government from CBE recording -11 percent during the month of study**, compared to an annual increase of 4.5 percent recorded during the previous month and compared to an average growth of 67.8 percent during the first 8 months of the year. The above mentioned **annual deceleration in credit facilities to the government could be justified on the backdrop of aid flows from the Gulf countries received by CBE since the beginning of the fiscal year 13/14 till May 2014** amounting to US\$ 17.9 billion, of which US\$ 15.9 billion that were refinanced to the government.

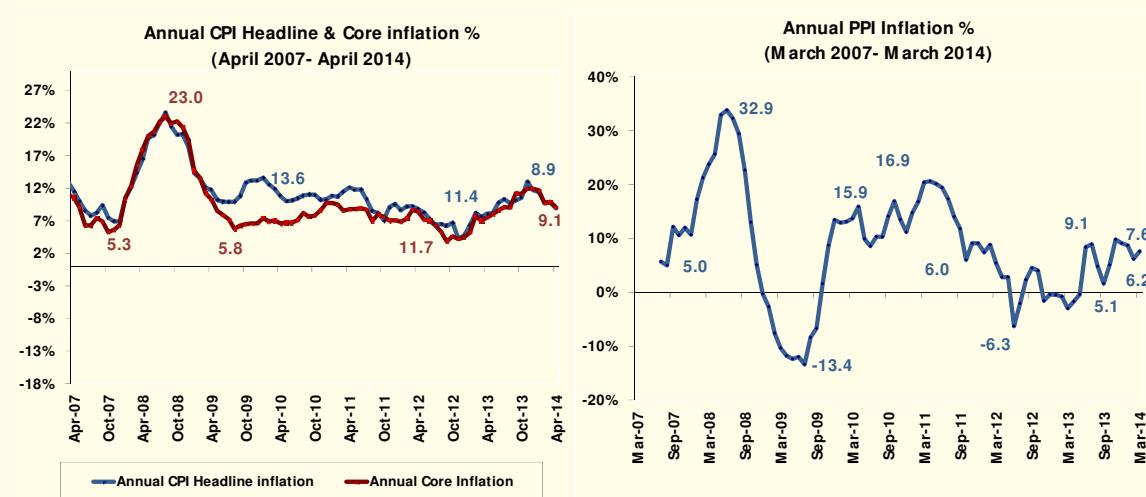
Moreover, **lending to private sector** decelerated slightly reaching 5.3 percent at end of March 2014 to LE 510.9 billion, compared to an average of 7.8 percent recorded during the first 8 months of 13/14. This deceleration comes on the back of the slowdown witnessed in claims on private business sector annual growth reaching 3.1 percent, compared to an average of 6.3 percent during the first 8 months of 13/14, which overcame the 11.9 percent increase in household witnessed during the month of study. Meanwhile, **net foreign assets** annual growth began to show some signs of improvement, with a relatively slower depletion on annual basis reaching only -3.9 percent (LE 124.3 billion), compared to an average of -13.2 percent during the first 8 months of 13/14, partly due to base effect.

Total deposits annual growth – excluding deposits at the CBE – stabilized for the second month in a row at 18.9 percent y-o-y (LE 1341.8 billion) at the end of February 2014, while it increased if compared to 12.9 percent in February 2013. Out of total deposits, 87.3 percent belonged to the non-government sector. Meanwhile, annual growth rate in total lending by banking sector (excluding CBE) increased during the year ending February 2014 recording 4.8 percent (LE 556 billion), compared to 4.6 percent during the previous month, while it decreased if compared to 7.1 percent recorded at end of February 2013. To that end, **loans-to-deposits** ratios decreased at end of February 2014 registering **41.4 percent**, compared to 47 percent in February 2013. (Detailed data for March 2014 is not yet available)

Monthly CPI eased during April 2014 compared to the first 9 months of the FY13/14

CPI annual Urban Inflation increased during the period **July-April 2013/ 2014** recording an average of 10.5 percent, compared to 6.5 percent during the same period of last year. Factors contributing to inflationary pressures include; higher food prices (the largest weight in CPI), and some other seasonal reasons, as well as an unfavorable base effect.

However, it is noteworthy that the annual inflation growth rate declined recording 8.9 percent during April 2014 (the lowest inflation rate since May 2013). This development is mainly attributed to the slower increase in annual inflation rate of “Food and Beverages” group, due to the decline in annual inflation rate of some sub items; “Vegetables”, “Fruits”, “Bread and Cereals”, “Meat”, “Milk Cheese and eggs”, and “Oils and Fats”, and which counterparts the increase in annual inflation of other groups, on the top of which; “Clothing and Footwear”, “Transport”, “Furnishing and Household Equipments”, “Recreation and Culture”, “Restaurants and Hotels”. On the other hand, monthly inflation decreased to 0.6 percent during April 2014 compared to 0.7 percent in the previous month.



Annual core inflation declined during April 2014 to 9.1 percent compared to 9.9 percent during March 2014. Meanwhile, monthly core inflation declined to 0.2 percent compared to 0.7 percent during the previous month. The monthly inflation could be explained in light of the increase in prices of retail items, paid services, and other services, which contributed by 0.36 percentage points to monthly core inflation. Meanwhile, food prices contributing by -0.11 percentage points.

During its **Monetary Policy Committee** meeting held on May 29, 2014, CBE decided to keep the **overnight deposit rate** and **overnight lending rates** unchanged at **8.25 percent** and **9.25 percent** respectively, and to keep the CBE's **main operation** unchanged at **8.75 percent**. The discount rate was also kept unchanged at 8.75 percent. The committee justified that decision in light of balancing upside risks, the inflation outlook, with the downside risks to economic growth at present.

In an attempt to absorb excess liquidity and to protect the domestic currency, the CBE announced the reintroduction of deposit operations. In this context, on May 28, 2014, the CBE introduced LE 40 billion worth of 7-day maturity at a fixed annual interest rate of 8.75 percent.

It is noteworthy that the CBE has offered US\$ 1.1 billion on May 14, 2014 at Foreign Exchange exceptional auction to meet banks import financing needs.

GDP growth rate...

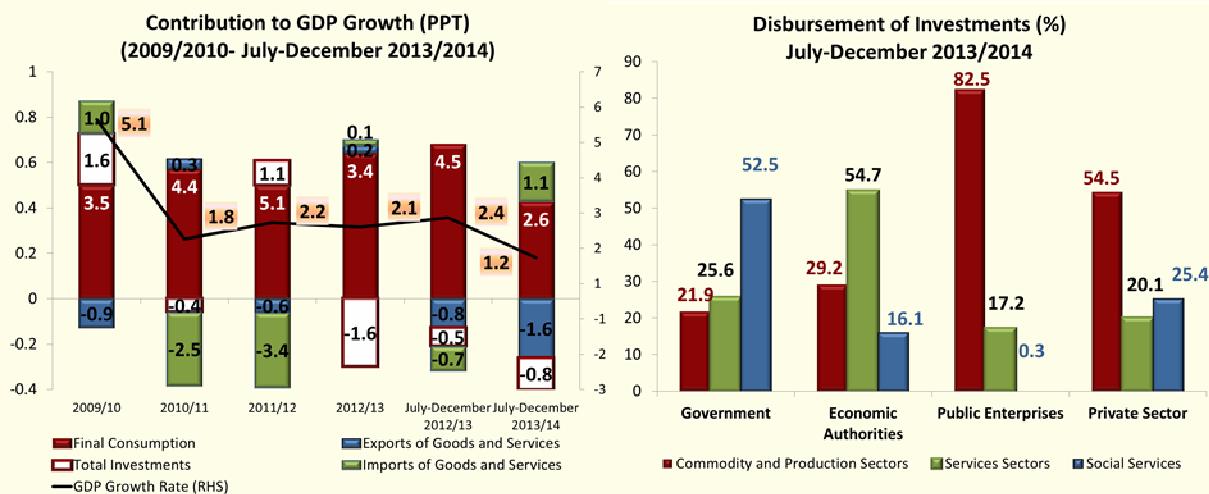
Five key sectors led growth in H1-FY13/14...

GDP Latest figures suggest the economy's recovery pace is still slow. GDP growth came at a humble 1.2 percent in H1-FY13/14, compared to 2.4 percent during the same period last year, mainly due to security reasons and political developments. Moreover, disbursements of the announced two stimulus- packages –that focused on propping up government investments- were not fully captured in GDP growth during the period of study, mainly due to tendering procedures for stimulus related projects. **This suggests that recovery in the second half of FY13/14 would assume a faster pace.**

Going forward, the government's strategy will shift to the second phase of reviving the economy, via preparing an additional stimulus package that will focus solely on removing bottlenecks that hinder private sector investments in key economic sectors, namely; industrial, housing and construction, communications and tourism. This should accelerate the pace of growth, while crowding in the private sector, which is a key contributor to employment.

On the supply side, key sectors that led growth in the first half of FY13/14 were the agricultural sector and the general government, with real growth rates of 3.5 and 5.5 percent respectively, contributing by 0.6 and 0.5 PPT, compared to 0.5 and 0.3 PPT a year earlier. **Wholesale and retail trade** real growth came at 3.2 percent in the same period (0.4 PPT compared to 0.3 PPT a year earlier), while **non-oil manufacturing sector and the construction sector** witnessed growth at 2.3 and 3.9 percent (0.3 and 0.2 PPT) respectively, same as a year earlier. Together, they represented around 56 percent of total real GDP in the period of study.

Meanwhile, Tourism and natural gas extraction sectors continued to subdue growth in the first half. Tourism has been severely hit due to several unfortunate events, falling by 30 percent y-o-y in the first half of FY13/14, while natural gas extraction fell by 8.2 percent in the same period, contributing negatively to growth.



On the demand side, Private consumption grew by only 2.5 percent y-o-y in the period of study, after having accelerated by 4.2 percent y-o-y in Q1-FY13/14, implying that Q2-FY13/14 real growth came at a humble rate of 0.8 percent. Similarly, **public consumption** grew at 4.8 percent in the period of study, compared to 5.6 percent a year

earlier, after having accelerated by 5.9 percent in Q1-FY13/14, implying a slow-down in growth (3.6 percent) in Q2-FY13/14.

Investments continued to hinder GDP growth in the first six months of FY13/14 with a (-ve) real contribution of 0.8 PPT, compared to 0.5 PPT negative contribution in the same period last year.

As for the distribution of total **investments by economic agents** (in nominal terms), public investments (government + economic authorities + public business sector) accounted for 25.6 percent of total investments in Egypt during the period of study, while the private sector accounted for 74.4 percent in the same period, noting that nearly half of government investments were directed towards social services sectors.

Meanwhile, **net exports** posted a negative contribution of 0.5 PPT in the first half, down from -1.6 PPT a year earlier. **Exports** continued to decelerate in the first half of FY-13/14, decreasing by 9.5 percent with a contribution of -1.6 PPT to real GDP growth, compared to -0.8 PPT a year earlier. While **imports** dropped by 4.2 percent in the same period, contributing positively by 1.1 PPT, compared to -0.7 PPT in the same period last year.

Industrial production index declined by 6 percent in March 2014 to 168.1 points, compared to 178.7 points in February 2014. However, this is still higher than the December 2013 level of 151.6.

The EGX-30 index increased by 451 points during April 2014, reaching 8256 points compared to 7805 during March 2014. Moreover, market capitalization increased by 1.7 percent m-o-m during the month of study to reach LE 478 billion (23.5 percent of GDP) compared to a LE 470 billion during the previous month. Meanwhile, the value of traded stocks decreased in April 2014, recording LE 20.4 billion, down 30 percent m-o-m compared to March 2014.

On the External Sector side:

BOP showed a significant improvement during the first half of 2013/2014 **recording an overall surplus of US\$ 2 billion** (0.7 percent of GDP), compared to an overall deficit of **US\$ 0.6 billion** in the same period last year, and compared to an average deficit of US\$ 1.2 billion over the last 5 years. The recorded surplus can be explained in light of the notable decrease in the **current account deficit**, recording US\$ 0.8 billion (0.3 percent of GDP) compared to a deficit of US\$ 4.9 billion in the same period last year. This was mainly driven by the noticeable increase in **public transfers** coupled with the deceleration in **imports**. Moreover, the **capital and financial account** witnessed net inflows of US\$ 3 billion (1 percent of GDP), compared to net inflows of US\$ 6.4 billion during the same period last year, while net errors and omissions recorded an outflow of US\$ 0.2 billion, compared to an outflow of US\$ 2.1 billion during the period July-December 2012/2013 .

§ On a more detailed level, the decrease witnessed in the **current account balance deficit** can be attributed to:

- The significant increase in **public transfers** during the first half of 2013/2014 recording US\$ 6 billion (2 percent of GDP) in light of grants received from Arab countries (US\$ 1 billion from the United Arab Emirates, US\$ 3.7 billion in-kind grants from Gulf countries in the form of petroleum shipments and US\$ 1.3 billion international funding and grants from various countries), compared to US\$ 0.6 billion during the same period last year.
- The decline in **trade deficit** by 16.8 percent to US\$ 15.4 billion during the period of study, compared to US\$ 18.5 billion during the same period last year. This was mainly due to the decrease in imports payments by 7.4 percent and the increase in exports proceeds by 7.5 percent, and thus resulted to the following:
 - Increase in exports to imports coverage ratio to reach 44.9 percent during H1-FY13/14, compared to 38.7 percent during the same period last year.
 - Rise in NIR imports coverage ratio to record 3.6 months of imports during the first half of FY 13/14 compared to 3 months of imports during the same period last year.

§ On the other hand, **services balance** deteriorated significantly by 95.5 percent to record a surplus of US\$ 0.2 billion compared to a surplus of US\$ 3.9 billion during the same period last year. This deterioration was driven mainly by an annual decrease of 66.4 percent and 18 percent in tourism receipts and other receipts, respectively.

§ Meanwhile, the surplus recorded in the **capital and financial account** was due to the following developments:

- The increase in **net foreign direct investments in Egypt** by 14.9 percent, recording a net inflow of US\$ 2.8 billion (1 percent of GDP) during July-December 2013/2014, compared to US\$ 2.5 billion during the same period last year.
- **Portfolio investments in Egypt** recorded a net inflow of US\$ 1.2 billion (0.4 percent of GDP) during H1-FY13/14, compared to a net outflow of US\$ 0.3 billion in H1-FY12/13, due to the government issuance of bonds equivalent to US\$ 1 billion, as a replacement for a Qatari deposit with the same value.
- The decrease in **liabilities of the CBE**, recording a net inflow of US\$ 2.1 billion compared to a net inflow of US\$ 3.4 billion during the same period last year, as CBE reimbursed part of the deposits that have been placed by some Arab countries (of which US\$ 1 billion to Qatar).

Total number of tourists arrivals increased slightly during the month of March 2014, reaching 754.7 thousand tourists compared to 617 thousand tourists in the previous month.

NIR increased for the fourth month in a row..

During April 2014, Net International Reserves (NIR) increased merely by US\$ 0.08 billion to record US\$ 17.49 billion, up from US\$ 17.41 billion in March 2014, thus recording a y-o-y growth of 21.3 percent. The witnessed increase in April 2014 was mainly due to a 0.4 percent increase in foreign currencies (y-o-y growth by 37.4 percent). It is noteworthy that NIR has recorded a positive growth for the fourth month in a row, after a continuous decrease since July 2013.