REPORT ON THE EGYPTIAN ECONOMY

AND

DEBT REPAYMENT PROSPECTS - 1988

Executive Summary

Egypt's economic reform progress accelerated in early 1987, with approval of an International Monetary Fund Stand-By Arrangement paving the way to a multilateral Paris Club debt rescheduling. The IMF agreement, Egypt's first since 1979, provides a comprehensive framework for economic reform in Egypt. Over the program period, Egypt has committed to undertake exchange rate unification, pursue fiscal and monetary restraint, move toward world energy prices, and further liberalize the agricultural sector. These measures constitute a first step toward a more self-sustaining, market-based economy which should ultimately enhance the country's ability to service its external debts. Phasing of the reform measures will continue to be affected by domestic political considerations focusing on social stability.

By international standards, Egypt's debt load remains heavy. The current Paris Club rescheduling agreement runs only through June 1988: any follow-on reschedulings will be linked to the pursuit of economic adjustment programs supported by annual arrangements with the IMF, and to balance of payments prospects. Unlike most other heavily indebted countries, Egypt's debts are almost entirely extended or guaranteed by foreign governments: the country has relatively little commercial bank debt.

Structural rigidities accumulated over a long period combine with a heavy debt overhang to cloud Egypt's medium-term economic prospects. Rapid population growth, a pervasive system of subsidies, and a structural trade deficit will leave Egypt dependent on extraordinary external assistance to meet its external commitments. With the assistance of the IMF, World Bank, and U.S. Government, Egypt has begun to address these problems in a systematic fashion. Accelerated reform progress is needed to stimulate the support of other creditors and donors necessary to restore economic growth.

II. Introduction

Egypt's adjustment program, as endorsed by the IMF under the Stand-By Arrangement, provides for a substantial reduction in the budget deficit, a phased unification of exchange rates, positive interest rates in real terms, sharp rises in energy prices, reforms in agriculture and tightened monetary policies. Two exchange rates covering over half of all transactions have already been nearly unified, while discussions are still taking place on a schedule for merging the highly subsidized central bank rate. Interest rates were increased slightly in early 1987, but remain well below positive real levels. Electricity tariffs were raised in May 1987 by a weighted average of 29%, while the prices of most petroleum products were raised by over 65%. Energy prices, however, remain well below international levels. Discussions are continuing on the timing of the next increases in energy prices, as well as their magnitude. Area and delivery controls in many crops have been lifted to encourage greater private participation, though cotton prices remain well below world levels. The price of subsidized imported corn was increased on July 1 and again on January 21, 1988. Fertilizer subsidies have not been reduced significantly.

The current Paris Club debt rescheduling provides more than $7 billion in relief to Egypt's balance of payments, including $4.5 billion of rescheduled arrears. Arrears and the bulk of interest payments and principal repayments due from January 1, 1987 to June 30, 1988 have been deferred to the mid and late 1990's. If this breathing space is used to pursue structural reforms in the Egyptian economy, additional resources should ultimately be generated to assist servicing of the growing debt burden. However, negotiations to strengthen the government's reform program were delayed beyond the fall, 1987 First Review specified in the IMF Stand-By Arrangement. As a result, the reforms to be negotiated in the context of the next Stand-by arrangement are especially important. This is even more significant because Egypt's medium term balance of payments prospects remain difficult, and even with strengthened adjustment, extraordinary creditor support will be required.

III. Structural Imbalance: Underlying Basis of Problems

Over the past twenty-five years, the Egyptian economy has undergone a gradual but steady deterioration, due largely to the effects of two main government policy weaknesses. Rigidities in prices of energy, utilities, food and other commodities as well as extensive government controls over production activities have combined to result in major imbalances in the structure of the economy, and costly inefficiencies. Until 1985, the effects of these policies were largely masked by substantial inflows of external resources. In the last three years, however, declining levels of external inflows have combined with rising debt service obligations to place substantial pressure on Egypt's budget, balance of payments, and economic growth performance.

The rapid rate of real economic growth during 1974-82 of 8% annually thus decelerated to about 5% over the 1982/83 to 1984/85 period and then to 2% or less since. The GOE's budgetary deficit climbed from LE 4.7 billion in 1982/83 to a high of over LE 8 billion in 1985/86. As a percentage of GDP, the budget deficit continued to rise to 23% in 1985/86 before gradually falling to perhaps 16% during the current year.

Egyptian subsidies of basic food and energy commodities represent an economic burden to the government of some LE 8 billion per year. Industrial production in some cases produces negative value added due to implicit and explicit subsidies. Increased demand for subsidized goods limits the amount of exportable surplus or creates pressure for more imports, thereby aggravating balance of payments pressures.

A. Energy

Egypt is an energy surplus country, endowed with sizeable oil and gas reserves which are being inefficiently used. Rapidly increasing domestic consumption of all forms of energy, encouraged by low subsidized prices, limits growth of an exportable surplus and distorts the pattern of production and consumption. While the production of crude oil and natural gas has expanded by 9.5% annually from 1981 through 1984, domestic consumption increased by 13.7% annually over the same period, causing exports of Egyptian crude oil to fall from about 240,000 BPD to 217,000 BPD. The consumption of electricity rose by about 11% annually during the same period. With 1987 production of crude oil at roughly the 1985 level of about 890,000 BPD and natural gas output 25% higher, Egyptian crude oil exports have fallen to slightly less than 190,000 BPD in recent months. With prospects of a continued levelling for the production of crude oil and slower increases likely in the production of natural gas, exports of crude oil are likely to continue to fall. Only low growth in the overall economy caused the rate of growth in consumption of petroleum products to be limited to about 5% during 1985 and to less than 2% during 1986. Sharp increases in local product prices would restrain consumption and prevent exports of crude oil from falling more rapidly, but at the cost of a politically sensitive decline in private purchasing power.

Despite declines in international oil prices and the May 1987 increases in domestic energy prices, the average domestic prices for petroleum products and natural gas as of December 1987 represented only about 25% of international prices. Current electricity tariffs are only about 23% of the economic price. These disparities have arisen because of the very low prices of domestic energy products in the early 1980's and the slow pace in their adjustment since. Average electricity tariffs rose by 9%, 17% and 13% respectively during the three fiscal years 1982/83 -1984/85 and then by 35% in July 1985. A further average 29% rise did not take place until May 1987. Overall, these increases did not keep pace with the rate of intervening inflation. No increases in the prices of gas oil, kerosene, diesel fuel or natural gas were undertaken from 1980 until the end of April 1987 when they were increased by about 67%.[1]

The annual value of the implicit subsidy for energy consumption by not charging international or economic prices totals LE 6.0 billion or $2.7 billion based on oil market conditions of December 1987. This figure represents the equivalent of 30% of the GOE's total budget. The calculations, detailed in Appendix I, can be summarized as follows:

- petroleum products, LE 2.6 billion(ex Egyptian Electricity Authority)
- natural gas, LE 0.4 billion(ex Egyptian Electricity Authority)
- electricity sales, LE 3.0 billion
- Total LE 6.0 billion

The actual profit transfer and tax from the international and domestic operations of Egypt Petroleum Corporation amounted to LE 1.50 billion during 1985/86. Assuming taxes on gasoline, and an immediate rise in prices to international levels on electricity and other locally consumed petroleum products, gross energy revenues for the central government on reduced domestic consumption would rise by at least LE 4 billion annually. These actions would cut the present budget deficit by half, but again at the politically sensitive cost of an equivalent decline in private sector disposable income. There would, furthermore, be substantial savings on investment spending in new electricity generation facilities which would no longer be needed, assuming a vigorous conservation response to higher prices.

B. Agriculture

Historically, agriculture has been the dominant sector in the Egyptian economy, accounting not only for over 33% and 15% of employment and output respectively , but also for significant

[1] See appendix 2, p. 27

foreign exchange earnings. Over the past two decades, the most serious structural problems in Egyptian agriculture have been pricing and cropping controls which have adversely affected the pattern of production and investment throughout the sector. These have discouraged production of Egypt's most valuable agricultural crop (long-staple cotton) in favor of commodities for which Egypt has no comparative advantage. For example, cotton procurement is monopolized by the government and farmers are paid only about two fifths of the world price, in order to maintain low input prices for Egypt's domestic textile industry. Meanwhile, due to restricted imports and correspondingly high local prices for red meat, animal fodders offer farmers higher financial returns. Production decisions based on these price relationships have held down productivity growth and foreign exchange earnings. Conversely, the relaxation of price rigidities for some fruits and vegetables during the early 1980's has encouraged a good growth rate in their output.

Reflecting these pricing and cropping controls, the average annual growth rate of agricultural production fell from 3.5% during the 1970's to 2.1% from 1980-84. Rapidly increasing consumption combined with sluggish production led to decreasing exports for cotton and rice and increasing imports for wheat, sugar and corn. Many Egyptian officials express concern over Egypt's declining food sufficiency, measured as the ratio of domestic supply to total consumption. The following chart illustrates the declining self-sufficiency trends in Egyptian agriculture over the last 25 years.

TABLE I
Self-Sufficiency Ratios (%)

	1960	1974	1981	1986
Wheat	70	37	25	22
Corn	94	87	71	66
Lentils	93	81	6	20
Sugar	114	96	53	52
Vegetable Oil	95	50	32	34

Some modest progress in raising producer prices has been made in recent years. For 1987, the cotton procurement price was raised by 14% to LE 116 per kantar, while the procurement prices for sugar and rice were raised by 10 and 18% respectively.[2] The 1988 cotton procurement price was recently raised by 25%.

[2] See appendix 2, p.27

Since early 1986, the GOE has achieved substantial progress in reducing restrictions in the agricultural sector with U.S. assistance. Marketing regulations have been liberalized, and the private sector has been given an enlarged role in importing many agricultural commodities, especially sugar, feed and red meat. The government has eliminated its intervention in crop planting decisions in all but three crops - cotton, rice and sugarcane. The GOE has also reduced substantially the feed subsidies (imported corn and local cottonseed cake) given to largely uneconomic local meat producers. The USG has encouraged such liberalization measures through the USAID-financed Agricultural Credit and Production Project and the Self-Help measures of the annual PL-480 Title I agreements. To maintain incentives for wheat production (despite the depressing effects of the government's bread and flour subsidies), the government has introduced a higher support price for voluntary deliveries of wheat by the farmer; as a result, the 1987 wheat harvest was the largest ever at 2.44 million tons, up from 1.93 million tons in 1986. Continued increases in procurement prices beyond the inflation rate, especially for cotton, and the promised removal of remaining governmental controls, would stimulate even greater agricultural production. A major reform objective would allow greater red meat imports so that local meat prices will decline and production shift to products in which Egypt enjoys a comparative advantage.

C. Industry

Egypt's industrial sector remains dominated by public sector enterprises, a legacy of widespread nationalization in the early 1960's. Since 1974, the public sector's share of industrial output has declined by 10 percentage points. Nevertheless, public sector firms continue to account for fully two-thirds of Egypt's industrial output. Poor management practices in many public sector firms have dampened overall industrial growth. Over-valued exchange rates which discouraged exports and frequent shortages of foreign exchange for necessary inputs and spare parts have also hampered industrial production.

Public sector firms have frequently enjoyed preferential foreign exchange and interest rates and, in some industries, continue to enjoy sharply advantageous electricity rates. Some highly favored public enterprises pay less than 10% of the electricity price charged to private sector firms. A major U.S. objective has been to urge GOE removal of these discriminatory provisions so that private firms can compete on an equal basis with public firms.

Real growth in the industrial sector has decelerated since 1980 from about 10% annually to the current rate of less than 5%. The pattern of growth has been skewed in favor of those heavy industries for which preferential prices for electricity, natural gas, or foreign exchange have been especially important.

Rapidly rising local consumption and the decreasing competitiveness of many Egyptian manufactured products caused steady declines in industrial exports for most years since 1978. An April 1983 regulation permitting industrial exporters the retention of earnings at the free market rate stimulated a significant expansion in industrial exports during 1983/84. A more competitive exchange rate and simplifications of export regulations in February 1987 are now leading to a revival of non-oil export growth.

Even where a healthy growth trend is experienced, the net contribution to the Egyptian economy of public sector industry may be small or even negative, in some cases, owing to distortions. Prevailing price distortions, especially with respect to electricity, result in a situation in which <u>many Egyptian industrial enterprises are producing with a negative value added.</u> According to a World Bank study, 20 of 25 public enterprises in metals, chemicals, paper and transport equipment experienced primary and intermediate input costs in excess of the value of their output, when all were measured at economic prices. One example is the Nag Hamadi aluminum plant, which now consumes 12% of all the electricity generated in Egypt as a result of rapid production expansion from 54,000 tons during 1976, to 116,000 tons in 1980 and 150,000 tons per year from 1981/82-1984/85. In 1987, the economic cost in Egypt of the electricity alone needed to produce a ton of aluminum was about the same as the world price per ton of aluminum. Reorganization or closure of industrial firms with negative value added would be justified on purely economic grounds, though such an approach would admittedly entail closure of the bulk of world aluminum capacity at current world market prices.

The inability of Egyptian public sector firms to raise product prices adequately to cover their rising costs has resulted in low profitability and correspondingly low budgetary transfers. An analysis of the budgets of the 372 public sector companies (PSCS) indicates that transfers of profits and taxes to the central government together with retained earnings measured about LE 1.22 billion during 1984/85, representing an estimated 4% of the capital employed in these enterprises.

In 1984, the Minister of Industry announced his intention to move towards prices which would provide industrial enterprises with a 10% rate of return by 1992. On this assumption, the government's net fiscal position would improve by over LE 1 billion per year and retained earnings by another LE 500 million, again at the expense of an equivalent decline in consumer purchasing power. Achieving this favorable result would have required the prices of the PSCs to rise by an average of some 22%. Pursuant to this policy, the prices of a number of industrial products were increased by 25-50% during the November 1984-January 1985 period.[3]

Greater autonomy apparently being given to individual industrial enterprises could result in higher productivity. If electricity and other input prices rise strongly pursuant to the reform programs in other sectors, achievement of higher rates of return in the industrial sector would require large improvements in efficiency and/or large increases in industrial product prices. These anticipated rises in input prices together with the recent slow pace of increases in industrial output prices make achievement of the 10% return objective by 1992 especially difficult.

D. Consumption and Trade

Pursuant to the social contract inherited from the Nasser era, the GOE has sought to preserve living standards for urban Egyptians, to the point of shielding them from the full impact of unfavorable external developments. GOE officials maintain that the need to preserve social and political stability argues for a gradual approach to economic reform. Maintaining the price of bread at one and then two piasters per loaf has been a main GOE policy for keeping the cost of living low for poor consumers. The economic cost for bread is about nine piasters per loaf. The budgeted GOE subsidy to cover these production losses currently runs about LE 800 million per year. The GOE's explicit subsidies to cover the losses on distributing maize, edible oils, sugar, frozen chickens and other foodstuffs are running about LE 900 million per year. These subsidies would rise by nearly LE 2 billion annually, if foodstuffs were imported at a realistic exchange rate without a corresponding increase in sale prices. Wheat, flour, sugar, edible oil and tea are imported at an exchange rate of $1 = LE 0.70, less than one third the current free market rate of about $1 = LE 2.20, while other foodstuffs have long been imported at a higher but still subsidized exchange rate. Recent proposals have been made to delete sugar and tea from the list of commodities receiving this preferential exchange rate. Total implicit and explicit food subsidies currently measure LE 3.7 billion, equivalent to 8% of GDP.

The prices of transport facilities, water and other utilities, fertilizer and many industrial commodities are fixed so low that substantial losses to the responsible enterprises result. Explicit GOE subsidies to these enterprises totalled about LE

[3] See appendix 2, p. 27

800 million during 1984/85, including LE 71 million for public transport in Cairo and Alexandria, LE 129 million for the Textile Corporation, LE 130 million for fertilizers and LE 126 million for industrial products. These operating losses would have been much larger if many utilities and industrial firms provided better maintenance or did not defer essential rehabilitation to reduce needed recourse to GOE Subsidies. (The GOE has attempted to freeze total subsidies at present levels or even to reduce them so has not been sympathetic to applications for increases). An important effect of low consumer prices is thus increasing deterioration of many industrial plants and basic utilities.

Since the 1977 disturbances, the GOE has moved cautiously with respect to food subsidies. Replacement of 1 piaster bread by 2 piaster bread began in September 1984 and was largely complete by the summer of 1986. The price of flour was also raised in September 1984, while similar increases in the prices of cooking oil and macaroni were reversed the next month and only re-instituted during the spring of 1987. The prices of rice and tea were increased substantially in early 1985, while the price of vegetable oil purchased beyond ration entitlements jumped in December 1985. The price of government imported feed corn was doubled in July 1986 and increased by a further 50% and 22% on July 1, 1987 and January 21, 1988 respectively. Intermittent shortages of subsidized rationed commodities have forced increased purchases through much more costly private channels. It has not been possible to quantify the effect of such shortages, however, on the overall budget for subsidies.

Subsidized utility rates have also been rising slowly. Telephone rates were raised substantially in January 1984 and again, to some extent, in April 1986. Water tariff rates were raised by 50% in Cairo and several other cities on July 1, 1985 pursuant to the 1985 National Tariff plan and the memorandum of understanding with USAID calling for water rates to cover all operating and maintenance costs. There have been no increases, however, in railway tariffs except for sharp increases in very low fares on the Cairo-Helwan commuter metro. There have been no further rises in water tariff rates since 1985.

The GOE's explicit subsidy bill increased steadily from LE 710 million in 1978 to a peak of LE 2.75 billion in 1984/85. Preliminary figures indicate some reductions in 1985/86 and a levelling off since. Total explicit subsidies are equivalent to 6% of GDP.

IV. Monetary and Fiscal Policies

Several weaknesses in macroeconomic policies have contributed to inefficiency throughout the Egyptian economy.

A. Exchange Rates

Egypt's system of multiple exchange rates developed gradually since 1979, as the government sought to hold down price increases through exchange rate policy. Overvalued official exchange rates have acted as a hindrance to exports and domestic production, and as stimulus to excessive imports and a rise in parallel market transactions. The government has made significant progress during 1987 under its commitment in the May 1987 IMF Stand-By Arrangement to move towards a unified exchange rate system.

The major reform in May 1987 was the establishment of an inter-bank free market rate at a level close to what prevailed on the open market. Forty per cent of transactions which had been taking place at the $1 = LE 1.35 commercial bank rate were moved immediately to the new rate and another 40% were transferred on November 17. The old commercial bank rate has been devalued in many small steps, reaching $1 = LE 1.85 in early January. The principal effect of this creeping devaluation has been to raise the cost of imports and augment government revenues. This is because the valuation basis for computation of customs duties since the August 1986 Customs Reform has been the old commercial bank rate. During December 1985 - January 1986, the basis for pricing airline tickets purchased in Egypt and for pricing air freight was raised 62% to the $1 = LE 1.35 rate. In May 1987, the pricing basis was increased further by about 15%. Another major effect of this creeping devaluation has been to gradually reduce the implicit subsidy on the two dozen commodities, handled by the General Agency for Supply Commodities (GASC), which enjoy the use of the commercial bank rate.

The major problem remaining in Egypt's exchange rate system is continued use of the $1 = LE 0.70 exchange rate for oil and cotton exports, Suez Canal revenues, imports of basic foods and debt servicing. While no progress has yet been made in moving this rate upward, the issue remains under review.

Since May 1987, the inter-bank free market rate has been set within a fairly narrow band ranging between $1 = LE 2.165 and $1= LE 2.245. This limited movement in the face of substantial internal inflation, combined with a failure of the system to meet all demands, has resulted in only a relatively small depreciation in the exchange rate on the parallel market. Greater flexibility in official rate setting would enable the market to equilibrate and would hold down pressure on the parallel market. In addition, opening the bank market to all legitimate users would discourage parallel market transactions.

B. Interest Rates and Inflation

Rapid dollarization of the Egyptian economy has taken place in recent years because of low pound deposit interest rates, high inflation, and the ability of Egyptians to hold dollar-denominated accounts within the domestic banking system. Egyptian pound deposits earn a maximum return of 13.25%, while the inflation rate has been running at about 20% annually and may be accelerating slightly. The result of this spread, compounded by the expectation of future devaluation, has been the growth in private sector domestic assets held in foreign currency to the present $10 billion, or over half of the total pool of domestic deposits. Additional worker remittances have been invested in banks and other assets abroad.

The lifting of many restrictions and bureaucratic controls could permit an expansion in domestic savings and investments. One significant reform would be movement toward positive real interest rates. However, the only change in interest rates which took place on May 1, 1987 in connection with the IMF Stand-By Arrangement was a one percentage point rise in loan interest rates with maturities exceeding one year and a two percentage point rise for maturities exceeding two years. Most LE loan rates remained in the neighborhood of 13% thus providing an implicit subsidy for borrowers with access to bank credit. Deposit rates were unchanged and are still limited to 9.5% or less for maturities of less than one year. The GOE has been reluctant to move further, out of concern for religious strictures against interest and fears that high interest rates would lead to bankruptcy for some heavily leveraged firms.

The inflation rate in Egypt is not accurately reflected in official statistics but appears to have been averaging 20-25% per year since 1984. On this assumption, increases of more than 10 percentage points would be needed to allow the structure of LE bank interest rates to become positive in real terms.

Prudent limits on credit expansion, which will require a sharp decline in the government's budgetary deficit, will be necessary to bring the inflation rate under control. Already, a policy of bank-by-bank quarterly credit ceilings since the spring of 1987 has limited the growth of private sector loans during 1986/87 to 9%. However, administered low LE rates have unfortunately required rationing and shortages of bank credit to the private sector. By contrast, the growth of net bank credit to the public sector in 1986/87 was 21%.

C. Fiscal Policies

For the last twenty-five years, the public sector has dominated economic activity in Egypt. Total government budgetary expenditures currently represent nearly one half of GDP; revenues one third; and the overall deficit exceeded one fifth of GDP from 1981/82 through 1985/86. A LE 1.7 billion spurt in government investment spending more than offset a fall in the explicit subsidies, on a commitment basis, during 1985/86, so that the deficit continued to rise to 22.5% of GDP during that year.[4]

Preliminary information indicates that the GOE's budget deficit may have declined to LE 7.5 billion during 1986/87. The large salary increase of May 1987, lower than planned increases in custom revenues, and insufficient measures for revenue increases or expenditure reductions may cause the 1987/88 budget deficit to rise again to over LE 8 billion, or 16% of GDP. This is three percentage points above the target agreed upon with the IMF.

Egypt's dependence on foreign assistance to cover budgetary deficits increased steadily through 1985/86, reaching a peak of $1.2 billion after amortization payments during that year. This was largely due to high volumes of externally financed development projects. With net foreign assistance falling during 1986/87, and with expenditures roughly level after sharp rises during each of the previous three years, GOE recourse to domestic financing has been rising. Domestic financing consists of two parts: 1) bank borrowing and 2) drawings from pension accounts, social security funds, mandatory investment certificates and bonds. This latter non-bank financing has risen from LE 1.5 billion in 1982/83 to an estimated LE 2.6 billion in 1985/86. GOE borrowing from banks, has risen from LE 2.0 billion in 1982/83 to an estimated LE 3.6 billion in 1985/86. The GOE has stated its intention to reduce the budgetary deficit sufficiently to eliminate the inflationary recourse to bank borrowing.[5]

The major categories of government revenues and expenditures are shown in the table below. On the revenue side, total average revenue growth has been a modest 10.5% annually from 1982/83 through 1985/86 as a result of inelastic taxes and profit transfers. This represents about one half of the inflation rate over this period. While lower international petroleum prices have limited the revenue growth from petroleum, a much more significant factor in the revenue stagnation from that source has been the slow pace of

[4]See appendix 2, p. 27
[5]See appendix 2, p.27

increase in domestic petroleum prices. The present disparity between domestic and international prices for petroleum products, natural gas and electricity represents an implicit LE 4 billion GOE subsidy to Egyptian industries and consumers.

The new revenue measures implemented during the last two years include a tax on airline tickets imposed in August 1985 and raised in April 1986 amounting to LE 100-150 or 10% of ticket value, whichever is less, and the April 1986 rise in registration fees on automobiles and in excise taxes on refrigerators, recorders, air conditioners, dryers and cars.

On the expenditure side, the most rapidly increasing items have been interest (average 20% annually); investment (18%); defense (16%); and civilian wages and salaries (also 16%). Direct budgetary outlays for subsidies constitute a substantial but decreasing share of total expenditures. Subsidy expenditures have been restrained through lower international food prices and the following measures: 1) a doubling in the price of bread begun in September 1984; 2) a series of increases in the price of government-imported feed corn in July 1986,July 1987, and early 1988 to a level near international prices; 3) the recent streamlining efforts within GASC to improve efficiency in distribution operations; and 4) the recent price increases on several other basic foods for quantities supplied in excess of the basic ration. Elimination of the Central Bank exchange rate, $1 = LE 0.70, used in the importation of essential foodstuffs would cause the reported subsidy expenditures through the GOE budget to more than triple in Egyptian pound terms. Conversely, GOE revenues from the Suez Canal Authority, the Egyptian Petroleum Company, and the Cotton Marketing Authority would show correspondingly large increases. The government could then decide separately whether and how fast the higher costs for foreign exchange would be passed on to the consumer.

As part of the program supported by its May 1987 IMF Stand-By Arrangement, the GOE agreed to reduce the budget deficit to 13% of GDP by 1987/88 and then by 2 percentage points annually to 4% of GDP by 1991/92. This would imply adoption of additional far-ranging measures to raise taxes and control expenditures, above and beyond those already undertaken for 1987.

Table II

Government of Egypt Budget (Actuals)
(In L.E. Million)[1]

	1982/83	1983/84	1984/85	1985/86	1986/87
REVENUES					
1. Suez Canal	484	448	412	481	
2. Petroleum	1,601	1,414	1,336	1,504	
3. Other Profit Taxes	933	994	1,216	1,535	
4. Personal Income Taxes	111	129	177	302	
5. Customs Duties	1,644	1,920	1,907	1,808	
6. Consumption Duties	1,195	1,302	1,444	1,489	
7. Investment Self Financing	1,507	1,628	2,011	2,347	
8. Other Revenues	2,273	2,535	2,810	3,326	
9. Total Revenues	9,749	10,371	11,311	12,792	
Expenditures					
1. Defense	1,683	2,120	2,385	2,646	
2. Civilian Wages and Salaries	2,202	2,620	3,158	3,446	
3. Subsidies (Commitment Basis)	2,342	2,609	2,749	2,155	
4. Interest	890	1,111	1,253	1,537	
5. Investment	5,020	5,518	6,556	8,261	
6. Other Expenditures	2,360	2,559	2,383	2,838	
7. Total Expenditures (Commitment Basis)	14,496	16,537	18,484	20,883	
Overall Deficit (Commitment Basis)	4,748	6,166	7,173	8,091	7,500
(As Percent of GDP)	21	22	22	22	
External Financing (Net)	858	1,052	1,530	1,351	

Source: American Mission, Cairo

1. Foreign currency computed by GOE at $1=LE 0.70

V. Balance of Payments Trends

The main trends of Egypt's recent balance of payments experience through 1985/86 or 1986/87, shown in Table III, have included declines in petroleum exports, worker remittances, imports and supplier credits, stagnation in non-petroleum exports, and a sharp rise in external arrears. Both unfavorable external circumstances and inappropriate government policies have contributed to Egypt's adverse balance of payments situation.

Unfavorable external developments -- the sharp fall in international petroleum prices, reduced earnings in the Gulf oil producing countries, and political uncertainties or incidents in the area have depressed Egypt's petroleum revenues, worker remittances, and tourism earnings. The government policies described in the preceding sections have also had major depressing effects on Egypt's external earnings. Low domestic petroleum and electricity prices have encouraged excessive domestic consumption of fuels, and thus lower quantities of crude petroleum have been available for export. Low and distorted agricultural producer prices have induced low acreage and late planting of the cotton crop and have diverted the use of high-quality, long-staple local cotton to production of coarse quality yarns and textiles-- all of which reduces the value of Egypt's cotton exports. Restrictions on industrial pricing, and the multiple exchange rate system, have dampened industrial exports. The flow of worker remittances to Egypt has been adversely affected by the frequent lack of access to the most favorable exchange rate and by low deposit interest rates. More broadly, the same pricing and monetary distortions have led to large budgetary deficits and sub-optimal growth which in turn have contributed to the balance of payments difficulties.

The exchange rate measures introduced during 1987 have had a strong favorable impact on tourism receipts, some industrial exports, and on worker remittances through official channels. While higher oil revenues and tourist income have contributed to improved balance of payments prospects for FY 87/88, Egypt continues to experience a severe depression in imports necessary for economic growth and arrearages on debt service obligations has reemerged, even after the beneficial effects of the Paris Club debt rescheduling.

Table III

Egypt: Balance of Payments
Merchandise Trade

	(In Millions of Current Dollars) 1983/84	1984/85	1985/86	1986/87	Projected 1987/88
Petroleum Exports[1]	2,957	2,891	2,215	1,380	1,700
Crude	(2,396)	(2,363)	(1,638)	(994)	
Non-Petroleum Exports	1,393	1,294	1,191	1,361	1,500
Imports[2]	-11,866	-11,593	-10,616	-8,453	-8,900
Trade Balance	-7,516	-7,408	-7,210	-5,700	-5,700
Services					
Shipping & Airline Companies	521	606	574	504	500
Suez Canal Dues	974	897	1,028	1,148	1,200
Tourism[3]	1,050	1,200	800	1,200	1,800
Worker Remittances[4]	4,400	4,200	3,800	3,700	3,700
Investment Income	1,079	1,044	914	790	700
Other	789	781	757	1,196	1,000
Total Service Receipts	8,800	8,700	7,900	8,500	8,900
Interest Payments[5]	-2,035	-1,133	-1,068	-1,100	-700
Outward Remittances[6]	-300	-560	-810	-720	-700
Other Payments [6]	-1,248	-1,262	-1,258	-1,287	-1,300
Current Account Balance	-2,300	-1,600	-2,500	-300	500
-% of GDP	8	6	7	1	
Capital Account					
Supplier Credit Receipts	1,547	850	1,192	645	700
International Assistance	1,397	1,607	1,968	1,644	1,750
Direct Investment[7]	1,273	1,287	1,265	920	1,050
Amortization Payments	-1,818	-1,321	-1,897	-1,440	-1,100
- Public Creditors	(-571)	(-580)	(-792)	(-883)	(-500)
- Suppliers	(-1,247)	(-741)	(-1,105)	(-557)	(-600)
Other and Errors	100	800	100	1,500	2,900
and Additions to Reserves [8]	-400	-500	-1,200	-200	600
MEMO: Rise in External Debt Arrears/ Rescheduling	520	1,353	1,274	1,650	2,300

Source: Government of Egypt and IMF reports with American Mission/Cairo adjustments. Footnotes are given in Appendix 3, p.28

A. Exports

Sharply rising domestic consumption of petroleum products, due to the price distortions discussed earlier, has limited the quantities of Egyptian crude available for export. The sharp fall in petroleum revenues during 1985/86 and 1986/87 was caused by steep declines in international prices. The decline in revenues would have been steeper in 1985/86, but Egyptian authorities correctly perceived the impending price collapse during the fall of 1985 and exported extra quantities during that period. Conversely, the fall was steeper than price trends warranted during 1986/87 because Egyptian authorities cut sales volume in the face of low prices. With current international prices holding fairly steady at double the lows of 1986, but half the price of the early 1980's, petroleum revenues may rebound by about $300 million during 1987/88.

The long-term trend in non-petroleum exports had been steadily downward, the result of rising domestic consumption and adverse trade, pricing, and exchange rate policies. Low producer prices for cotton, for example, have depressed cotton production and exports. A favorable change in the policy on retention of foreign exchange proceeds caused a temporary rise in industrial exports during 1983/84.

Industrial exports are currently rising sharply in response to the sharp drop in the real effective exchange rate of the Egyptian pound since mid 1985 and the February 1987 simplification of governmental procedures for licensing exports. Liberalization of price controls and the removal of remaining government restrictions would be important stimulants to further rapid growth in industrial as well as agricultural exports.

B. Worker Remittances and Other Service Receipts

Worker remittances have been depressed by both external circumstances and by inappropriate governmental policies. The reduction in income in the Gulf oil producing states has certainly played a role in restricting worker remittances to Egypt, but diversion of these earnings to Europe may have been induced by low Egyptian pound interest rates and by over-valued exchange rates. The 1986 census indicated that there were 2.2 million Egyptians working overseas. Their number had increased rapidly through the 1970's and early 1980's, but has probably held roughly level or declined slightly during the last two or three years. Wages for some Egyptians abroad have declined in light of the oil sector decline and increased competition from Asians coming to the Middle East. The official statistics thus show worker remittances going down during 1984/85 and 1985/86 to $3.50 billion and $2.97 billion respectively from $3.93 billion during 1983/84. There were partially offsetting increases in unrecorded flows going into foreign currency free accounts. The initial steps toward exchange rate unification are probably causing a strong one-time rise in recorded worker remittances during 1987/88.

Until recently, the vast majority of tourism revenues probably flowed through unofficial channels, owing to the previously wide divergence between official and free market foreign exchange rates. The general trend had been level with the exception of the disastrous year 1985/86, in the aftermath of terrorist incidents in Europe and the Middle East. A major upturn of tourism revenue is now occuring in the atmosphere of relative political tranquility, aided by the freeing of the tourist exchange rate in the spring of 1987.

The trend for Suez Canal dues, alone among major foreign exchange earners, has been steadily upward with the exception of 1984/85, principally reflecting increases in the fee structure and the devaluation of the dollar against the SDR, the currency in which the fees are billed.

Investment income receipts represent interest on the Egyptian banking system's foreign assets of some $10 billion held in deposits outside of Egypt. The trend has been downward in line with the interest rate declines in world financial markets.

C. <u>Service Payments</u>
Actual interest payments made on external debt have fallen from $1.9-2.0 billion annually during 1981/82-1983/84 to only $1.1 billion annually thereafter. A part of this decline is attributable to falling interest rates internationally. Most of the decline was caused by sharp increases in arrears on external debt: from an estimated $260 million in 1981/82 to $1.3 billion annually in 1984/85 and 1985/86. The increase in arrears rose to $1.65 billion in 1986/87, while the rescheduled interest and principal due during 1987/88 amount to an estimated $2.3 billion.

On the other hand, service payments aside from interest payments on external debt have risen steadily from $1.55 billion in 1983/84 to $1.80 billion in 1984/85 and $2.06 billion in 1985/86. A major new element in this rise has been a rapid growth in investment transactions. Remittances abroad of profits, royalties and repatriated capital rose sharply to $560 million in 1984/85 and $810 million in 1985/86 from perhaps $300 million in 1983/84.

D. <u>Imports</u>
This had been the swing factor in Egypt's balance of payments, rising or falling in response to the trends in earnings. During the late 1970's, with the spurt in foreign exchange earnings, imports grew at annual rates of 20 to 30%. Imports peaked at $11.9 billion in 1983/84 when earnings from petroleum and service receipts also peaked at $11.8 billion. Since then imports have declined in tandem with the declines in service receipts and petroleum earnings.

The decline in imports during 1986/87 has actually been sharper than the declines in service receipts and petroleum <u>earnings.</u>[6] Imports are rising very slowly during the current

[6]See Appendix 2, p.27

year. This sharp fall in imports last year and slow recovery during the current year have arisen in part from the promulgation of the August 1986 customs reform with its new basis for assessing customs duties on imports, and with its expansion in the range of import bans. The steady rise since May 1987 in the valuation basis for assessing customs duties has been one measure for discouraging imports. The other major depressant on imports has been the sharp drop in the real effective exchange rate of the Egyptian pound since mid 1985 and the requirement for 100 per cent cash cover before importers can open letters of credit. Lack of available financing may also play a role in lower import levels. While the net effect has been a helpful impact on the balance of payments, economic growth has been constrained by lack of capital inputs.

VI. Capital Inflows, Foreign Aid, Payment Arrears and Debt Rescheduling

A deterioration has taken place on the Egyptian capital account during 1986/87 and 1987/88. While gross capital inflows averaged $4.13 billion per year during 1983/84-1985/86, they fell to $3.2 billion during 1986/87. The 1987/88 figure may be $3.5 billion. Actual amortization payments, however, have declined from $1.9 billion in 1985/86 to $1.4 billion in 1986/87 and to perhaps $1.1 billion in 1987/88, reflecting the accumulation of arrears and subsequent rescheduling.

A. Direct Investment

Non-petroleum direct investments amounted to $145, $210 and $209 million during 1983/84,1984/85 and 1985/86 respectively. This modest level has been dwarfed by the extent of investment in equipment for exploring and developing oil fields brought in by foreign oil companies. While such petroleum expenditures have exceeded $1 billion annually in recent years, the recent sharp declines in international petroleum prices and a cutback in new oil concessions caused these investments to decline by 34% during 1986/87.

B. Foreign Assistance

Gross foreign assistance disbursements for non-military purposes have averaged about $1.7 billion per year over the last four years. Aid from the United States comprises about one half the total. The other major donors are Germany, Japan, France, the World Bank and the European Economic Community. With the restoration of diplomatic relations between Egypt and many other Arab countries in November 1987, assistance flows from several of those countries may resume.

The U.S. role in assisting Egypt was greatest during 1985/86 as the result of a $500 million supplemental cash transfer. With this supplementary assistance, the total foreign civilian assistance, net of amortization payments, increased from $0.8

billion during 1983/84 to $1.0 billion during 1984/85 to $1.2 billion during 1985/86, before declining to perhaps $0.8 billion again during 1986/87.

The present stock of military debt from Western sources is about $9 billion, half of which is due the United States. Since US FY 1985, military assistance from the United States has been provided entirely in grant form, at an annual level of $1.3 billion.

C. <u>Increasing Debt Servicing Difficulties & Payment Arrears</u>
Debt servicing had been kept within reasonable limits until about 1984/85. Egypt began experiencing difficulties during that year when total inflows of external resources on current account levelled off, while military interest obligations rose sharply. The debt crisis became acute when debt servicing obligations continued to increase while petroleum export revenue fell sharply during 1985/86 and 1986/87.

Much of the civilian Egyptian debt was built up in 1975-79, when public and publicly guaranteed debt grew at an annual rate of 26%. On the other hand, the American military debt was accumulated from 1979-84 and much of the other military debt was also acquired during this period.

Table IV

External Debt Egypt 1983-1986 1
(As of end of year in $ billion)

	1983	1984	1985	1986
Suppliers Credit 2	4.5	4.8	5.5	5.8
Banks	1.1	0.9	1.1	1.1
Multilateral	4.0	4.3	4.6	4.8
Bilateral	9.9	10.5	11.5	12.6
Short term 3	4.4	4.8	5.0	4.8
FMS Debt	4.0	4.4	4.6	4.8
Other Military 4	3.3	3.9	4.5	4.6
Total	31.2	33.6	36.8	38.5
% of GDP	104	111	120	125

	1983/84	1984/85	1985/86	1986/87
Actual Debt Service Payments	3.85	2.49	2.96	2.54
Rise in External Arrears	0.52	1.35	1.27	1.65
Total Debt Obligations	4.37	3.85	4.24	4.19
Inflows of External Resources	17.38	16.66	15.70	14.48
of which: Current Account	13.16	12.91	11.28	11.28
Debt Service Ratio 5	33	30	38	37

Source: Adapted from World Bank Computer Print-Out 12/8/87

1/ Disbursed and outstanding debt only, including principal and interest in arrears, military and civilian.
2/ Much higher than previously reported by World Bank due to more complete coverage.
3/ Excludes interest of approximately $.5 to $.6 billion per year on foreign currency deposits of residents.
4/ Excludes debt to East European/Soviet Bloc countries.
5/ Debt obligations as a percent of total current account receipts.

Egypt's public and publicly-guaranteed external debt was estimated at $38.5 billion as of December 31, 1986. The average annual increase since 1983 of about 8% has been relatively modest, but the debt size had already grown dangerously large for Egypt's credit rating. Egypt's debt service ratio measured 31% in 1982/83, and then jumped to 38% by 1985/86, before receding slightly during 1986/87.

The one favorable aspect of Egypt's debt servicing problem has been the restraint shown on the accumulation of high interest-bearing, short-term debt. The total has hovered in the $4.8-5.0 billion range since 1983. As a proportion of total outstanding debt, short-term debt has fallen from 15% in 1983 to 13% in 1986. Part of the reason for this apparent restraint may have been a decline in offers of short-term finance owing to creditor concerns about Egypt's credit rating. Lower import levels may also have contributed to this development.

A principal adverse factor bringing on the present debt crisis was the rapid rise in military debt servicing during the mid-1980's. American military aid began in 1979 with a Foreign Military Sales (FMS) credit of $1.5 billion. The total FMS debt contracted during the 1979-84 period was $4.55 billion, all at high fixed rates averaging 11.8%. Military debt contracted from other Western sources totalled about the same amount. FMS interest payments actually made amounted to $173 million during 1981/82 and rose to $451 and $525 million respectively during 1985/86 and 1986/87. No principal repayments on FMS debt are due until 1989. Because principal repayments were due earlier on European military debt, scheduled repayments on other Western military debt had already reached $550 million in 1984/85 and over $750 million during each of 1985/86 and 1986/87.

Of total disbursed debt, approximately 25% or $10 billion is owed to the United States. The U.S. is Egypt's largest bilateral creditor. Aside from the FMS program, the largest outstanding loans are under the A.I.D. and PL 480 programs, totalling $2.5 and $2.4 billion respectively at two or three percent annual interest rates.

Debt service arrears increased sharply between 1984 and mid-1987 in response to the growing severity of the balance of payments crisis. Following the Baghdad Conference of November 1978, the Egyptian government issued a decree banning the transfer of amortization payments and interest related to all loans and deposits controlled by the Arab countries participating in the Baghdad decisions. This ban affected about $4 billion of Egypt's debt. Pursuant to this decision, most of Egypt's debt to the Arab countries has not been serviced since the late seventies. Debt to Iran is also not fully serviced. The government began falling behind in its military repayments to the U.S. in 1984, and covered only $178 million (38% of total due) during 1984/85. Arrears on loans to other Western countries also increased. On the servicing of supplier credits too, Egypt began to accumulate arrears in 1984/85, with delays in settlement since then sometimes amounting to 5-6 months.

As a result of this adverse debt servicing experience, the stock of external arrears increased from an estimated $0.8 billion in the middle of 1982 to $4.3 billion in the middle of 1986, with the annual rise in arrears averaging $1.3 billion during 1984/85-1985/86.

D. Paris Club Debt Rescheduling

Representatives of 18 countries, including the United States, met in Paris in May 1987 to reschedule certain Egyptian debts owed to them. These debts include commercial credits guaranteed or insured by these governments and official loans with original maturities of more than one year and concluded before October 31, 1986. The agreement provides 10 years rescheduling, with 5 years grace, for all arrears as of December 31, 1986 and for all principal and interest payments falling due between January 1, 1987 and June 30, 1988.

Egypt has agreed to seek terms at least this generous from countries not participating in the Paris Club. In late March, for example, agreement was reached with the Soviet Union on repayment of $1.7 billion in Russian military debt over a 25 year period, including a six-year grace period. Cancellation of the annual two percent interest rate has been reported. There is another unconfirmed report that the old $1-LE 0.40 exchange rate will be used on the repayments so that, in effect, the current value of the repayments will be much less that $1 billion.

Among Paris Club creditors, bilateral agreements had been signed with France, Spain, Germany, the United States and Austria by January 1988. The average annual interest rate set on the rescheduled payments has been about 8%. For the rescheduled debt payments to the United States, interest rates range from 3% per year on PL 480 and AID debts, to 7.3-8.9% for the Department of Defense, and current market rates on CCC and Eximbank debts.

The May 87 agreement reschedules payments falling due through June 30, 1988. (All Paris Club reschedulings are by definition short-term exercises,since the period for which payments are consolidated roughly coincides with the period of the IMF stand-by). Should Egypt again be in danger of imminent default on its external obligations after that date, the Paris Club could again consider a request for rescheduling, provided Egypt were taking steps to correct the underlying causes of its difficulties through an adjustment program supported by another formal arrangement with the IMF.

VII. Conclusions:

A. Economic Reform

Egypt has begun to address its deep-seated economic problems. Nevertheless, much more needs to be done, particularly in moving toward market pricing in agriculture, energy and industry, reducing the budgetary deficit, and liberalizing governmental controls. The pace of economic reform accelerated during the first half of 1987, but may have slackened since then, reflecting concern over social reaction to the pace of price increases.

B. Debt Situation

Egypt's medium-term balance of payments prospects remain difficult, due to a heavy debt overhang combined with the long-term impact of an inward-oriented policy environment. If vigorous reforms are undertaken, the structural imbalances impeding the resumption of growth can eventually be overcome, and Egypt may again be in a position to fulfill its normal debt servicing obligations. However, the magnitude of the current distortions suggests that Egypt will continue to need extraordinary support from international creditors over a number of years, even if a vigorous adjustment effort is pursued. Should the reform program unwind and exchange rate and price distortions increase again, the balance of payments could worsen and economic growth languish with resulting severe damage to Egypt's debt servicing capacity.

C. U.S. Role in Encouraging GOE Pursuit of Vigorous Economic Reform

The United States role in encouraging GOE pursuit of a vigorous economic reform program takes place in two contexts: bilateral and multilateral.

USG policy is to support economic reform measures in the bilateral context through policy dialogue undertaken in connection with sectoral and cash transfer programs. For example, the Agricultural Production and Credit project provides a three year disbursement schedule totalling $100 million conditioned upon implementation of significant structural reforms that the GOE has set for the agricultural sector. These reforms comprise the elimination of most price and area controls and of crop procurement prices, enlarged private sector access, and the removal of subsidies on fertilizer, pesticide and feed. Similar reforms are incorporated in the Self-Help measures of the PL-480 agreements. An energy sector program has been under discussion that would be related to significant steady rises in the real prices of electricity and petroleum products. Individual power projects would also be affected by the implementation of such reforms. The cash transfer and any major expansion in the Commodity Import Program will be based upon significant progress being made in economic reforms in key areas, such as exchange and interest rates, budgetary deficit, energy prices, agriculture and industry.

In the multilateral context, the U.S. encourages macro-economic reform through coordination with the World Bank, the IMF and other donors. Reforms in the agriculture and energy sectors are pursued through similar negotiating strategies on AID's and the World Bank's parallel projects. The U.S. continues to encourage the Government of Egypt to work closely with multilateral institutions in designing growth-oriented adjustment programs that address the underlying policy problems in the Egyptian economy.

Appendix 1

Table V
Estimation of Petroleum Subsidy, December 1987

Product	Quantity sold 1986 (000 mt. tons)	Approximate Prices (LE per metric ton) retail	world*	% of world price	Subsidy (millions of LE)
Butagas	671	52	450	11	267
Kerosene	2328	63	364	17	701
Gas oil	3828	60	337	18	1,060
Fuel oil	7656	28-32	162	18	1,011
Bitumen	604	27	210	13	111
Total NG					3,150 764

* Converted at inter-bank free market rate of $1 = LE 2.20

Source: American Mission, Cairo

3.92 incl NG

As shown in Table V, the gross figure for the implicit subsidy on petroleum products is LE ~~3.1~~ billion annually. However, after deducting the subsidies of petroleum products to the Egyptian Electricity Authority (LE 560 million) the net implicit subsidy for petroleum is LE 2.6 billion or $1.2 billion.

Natural gas is sold at a price of LE 7.2 per ton to the fertilizer, textile and iron and steel firms and at varying subsidized prices averaging about LE 34 to other industries and most households. With an international price of approximately LE 212 per ton, and total comsumption of over 5 million tons of NG annually, this subsidy represents a cost of about LE 960 million. After deducting the NG subsidy to the EEA, the net NG subsidy becomes LE 400 million.

The long-run marginal cost of producing electricity in Egypt was estimated at about 13 piasters per kilowatt hour in 1987, representing the fully distributed cost of providing an average additional generation facility. Since the present average weighted price of electricity is only about 3.0 piasters per kilowatt hour and current electricity sales are running at about 30 billion KWH annually, the implicit subsidy for electricity is about LE 3.0 billion annually, or $1.36 billion.

Appendix 2

Footnotes to Text

1. The price of fuel oil for the cement, lime, brick and gypsum industries was more than quadrupled to LE 32 per ton during 1985. For electricity plants, the price of fuel oil and natural gas was doubled to LE 15 per ton during 1985. For gasoline, recent price increases have been substantial--33 and 25% in August 1985 and July 1986 respectively for ordinary gasoline and 15,25,25, and 20% in April 1982, April 1985, August 1985 and July 1986 respectively for premium gasoline.

2. During 1984, procurement prices for wheat, maize, onions, and groundnuts were reportedly raised by one third, for cotton and lentils about 28%, and for rice about 24%. In 1985, the price of wheat was raised by as much as an additional 37%, and there were also smaller price increases for sugar, rice, onions, sesame and lentils. In 1986, the procurement prices were reportedly increased as follows: sorghum-42%, rice and soybeans-32%, sugar and onions-25%; and lentils-20%.

3. These products include tomato concentrate, light bulbs, agricultural tractors, cotton yarn and cloth, and steel products. The price of coking coal was increased from LE 62 to 120 per ton. Four price increases in cigarettes, averaging about 10% each, took place in September 1984, July 1985, April 1986 and June 1987. The price of tomato paste was doubled in July 1987.

4. The Ministry of Finance liquidated LE 825 million in bank bonds from the General Agency for Supply Commodities (GASC) during 1985/86, accumulated on the basis of food imports outstripping budgetary allocations in past years, and LE 611 million in bonds from other corporations, so that, on a cash basis, the deficit ratio was 24.6% OF GDP during that year.

5. To prevent debt relief from contributing to inflationary expansion of the Egyptian budgetary deficit, the IMF Stand-by Arrangement provides for the establisment of "blocked accounts; the public sector will transfer into these accounts the pound counterpart due on its external debts, as originally contracted for, from January 1, 1987." Withdrawals from the blocked accounts may be made only for the domestic currency counterpart of the external debt service actually effected abroad.

6. 1986/87 imports were $3.2 billion below the 1984/85 level compared to a $1.7 billion fall in these receipts and earnings.

Appendix 3

Footnotes to Balance of Payments Table

1. Includes bunkers, but excludes foreign partners' profit share and cost recovery shipments. Allowance for value of partner companies' exports would add estimated $1.1 to $1.3 billion annually for 1982-1985, and $0.8 to $1.0 billion in 1986 to Petroleum Exports and to Remittances accounts, negating each other in the Current Account Balance.

2. The official figures for the 1983/4-1986/7 period of 10,738; 10,516; 9,560 and 7,760 million dollars respectively include an adjustment for unrecorded grant shipments. The IMF figures are further adjusted by EGPC figures on equipment for exploring and developing oil fields brought in by foreign oil companies of 1,128; 1,077; 1,056; 693 and perhaps 800 million dollars respectively. Military imports and foreign military assistance are excluded from this table.

3. Based on Ministry of Tourism figures on tourist nights.

4. The official figures are 3,930; 3,497; 2,973 and 2,845 million dollars respectively. The following adjustment is made to these figures: The IMF indicates that unrecorded flows into foreign currency free accounts may have totalled 457; 686; 860 850 and perhaps 850 million dollars respectively.

5. The actual interest payments were obtained by using IMF estimates of interest obligations and subtracting therefrom the figures for annual increases in external arrears. Amounts given here and in IMF presentations include military interest payments.

6. Central Bank breakdowns of the other service payments item for 1984/5 and afterwards contain a component called capital and investment account transactions. This component is listed in this table as remittances.

7. IMF 1985 figures adjusted by amounts of 1,128; 1,077; 1,056 and 693 million dollars annually in foreign oil company equipment imports for exploring and developing oil fields.

8. The second row of figures would have been applicable if there had been no increases in net external arrears or rescheduling and thus more clearly reflects Egypt's true balance of payments position.

DWCarr

DRAFTER:ANE/DP/P&A, DCarr:JLewis:#1609R

Table 1

Annual Real GDP Growth Rates (Excluding Petroleum)

	1982/83	1983/84	1984/85	1985/86	1986/87
Agriculture	3	2	3	2	2
Manufacturing	6	8	6	3	2
Electricity	11	15	9	7	9
Construction	5	6	4	4	-2
Transportation & Communications	17	10	10	5	3
Trade	15	7	7	3	2
Financial and Insurance	11	3	12	4	6
Housing	10	10	7	6	6
Tourism	5	7	8	-7	16
Total	7.3	5.3	5.9	3.3	2.3

Table 2

Agricultural Production
(in thousands of metric tons)

	1982/83	1984/85	1986/87
Wheat	1,996	1,872	2,722
Onions	224	189	127
Cotton	401	435	347
Rice	2,442	2,310	2,404
Maize	3,509	3,700	2,916
Millet	622	535	540
Citrus	1,297	1,399	1,567
Other Fruits	990	1,042	1,222
Potatoes	1,095	1,478	1,431
Vegetables	7,218	8,329	10,014

Source: CAPMAS

Table 3

Index of Industrial Production
(1975=100)

	1982/83	1984/85	1986/87
Cotton Textiles	126	128	137
Preserved Fruits and Vegetables	287	375	362
Soft Drinks	449	478	395
Sulfuric Acid	75	128	111
Superphosphates	113	183	203
Ammonium Nitrate	1033	1009	1070
Tires	143	164	196
Cars	216	180	139
Trucks and Tractors	247	315	193
Refrigerators	417	505	540
Televisions	986	1077	380
Reinforcing Bars	128	110	114
Steel Sections	197	246	183
Cast Iron	297	139	223
Phosphate	151	176	165

Source: Ministry of Industry

Table 4

Value of Industrial Output
(In Current LE Million)

	1982/83	1984/85	1986/87
Building Materials	83	198	294
Chemicals and Pharmaceuticals	923	1456	1883
Engineering and Electrical	1689	2286	2487
Food	2389	3491	4459
Mining	72	87	102
Spinning and Weaving	1773	2227	2765

Source: CAPMAS

Table 5

External Debt 1983-1987[1]
(As of end of year in $ billion)

	1983	1984	1985	1986	1987
Suppliers Credit[2]	4.5	4.8	5.5	5.8	5.5
Banks	1.1	0.9	1.1	1.1	1.2
Multilateral	4.0	4.3	4.6	4.8	4.9
Bilateral	9.9	10.5	11.5	12.6	13.7
Short Term[3]	4.4	4.8	5.0	4.8	5.1
FMS Debt	4.0	4.4	4.6	4.8	5.0
Other Military[4]	3.3	3.9	4.5	4.6	4.9
Total	31.2	33.6	36.8	38.5	40.3
% of GDP	95	97	106	110	112

Source: Adapted from World Bank Computer Print-Out 12/8/87

1/ Disbursed and outstanding debt only, including principal and interest in arrears, military and civilian.

2/ Much higher than previously reported by World Bank due to more complete coverage.

3/ Excludes interest of approximately $.5 to $.6 billion per year on foreign currency deposits of residents.

4/ Excludes debt to East European/Soviet Bloc countries.

Table 6

Principal Creditors (in $ billion)

	1981	1984	1987
United States	5.15	8.50	10.10
France	0.75	2.40	4.00
GODE[1]	2.00	2.30	2.60
Germany	0.85	1.50	2.20
Kuwait	1.00	1.00	1.49
Spain	0.25	0.90	1.50
IBRD	0.54	0.72	1.35
Japan	0.35	0.80	1.30

1/ Gulf Organization for the Development of Egypt

Table 7

MLT Debt Service Obligations

(in $ Billion)

	1984/85	1985/86	1986/87	1988/89	1989/90
Civilian	3.05	3.58	4.07	4.95	5.47
Civilian & Military	4.20	4.81	5.77	6.30	6.82
% of GDP	12	14	16		
% of Current Account Earnings	42	46	54		

Table 8

Public and Publicly Guaranteed Civilian Debt Servicing Obligations
(in $ Million)

	1981/82	1983/84	1985/86	1986/87
Suppliers Credits	1558	1523	892	1054
Banks	341	271	50	176
Multilateral	354	289	613	243
Bilateral	1317	994	518	562
Total	3571	3079	2074	2036

Source: IBRD Debtor Reporting System

Table 9

Government of Egypt Budget (Actuals)
(In L.E. Million)[1]

REVENUES	1982/83	1983/84	1984/85	1985/86	1986/87
1. Suez Canal	484	448	412	481	525
2. Petroleum	1,601	1,414	1,336	1,504	1,112
3. Other Profit Taxes	933	994	1,216	1,535	1,511
4. Personal Income Taxes	111	129	177	303	302
5. Customs Duties	1,644	1,920	1,907	1,808	1,906
6. Consumption Duties	1,195	1,302	1,444	1,489	1,723
7. Investment Self Financing	1,507	1,628	2,011	2,347	1,858
8. Other Revenues	2,273	2,535	2,810	3,326	3,568
9. Total Revenues	9,749	10,371	11,311	12,793	12,405
EXPENDITURES					
1. Defense	1,683	2,120	2,385	2,646	2,788
2. Civilian Wages and Salaries	2,202	2,620	3,158	3,446	3,675
3. Subsidies (Commitment Basis)	2,342	2,609	2,749	2,155	2,567
4. Interest	890	1,111	1,253	1,537	1,840
5. Investment	5,020	5,518	6,556	8,261	6,600
6. Other Expenditures	2,360	2,559	2,383	2,838	2,688
7. Total Expenditures (Commitment Basis)	14,496	16,537	18,484	20,883	20,158
Overall Deficit (Commitment Basis)	4,748	6,166	7,173	8,090	7,753
(As Percent of GDP)	21	22	22	22	18
External Financing (Net)	858	1,052	1,530	1,796	1,446

Source: American Mission, Cairo

1/ Foreign currency computed by GOE at $1=LE 0.70

Table 10

Explicit Subsidies
(in million LE)

	1982/83	1984/85	1986/87
General Authority for Supply Commodities (Food)	1,624	1,863	1,486
Cairo & Alexandria Transport	38	71	69
Fertilizer & Seed	159	135	134
Textiles	127	129	54
Bottled Gas & Kerosene	42	54	30
Housing	35	57	90
Credit	48	69	73
Industries	268	370	631
Total	2,342	2,749	2,567
% of GDP			4
Implicit: from using \$1 = LE 0.70 exchange rate on oil and cotton exports and on Suez Canal fees rather than free rate of \$1 = LE 2.35			4,500
% of GDP			8
Implicit: from charging prices on electricity and fuels 75% lower than their economic or international prices			4,000
% of GDP			6
Implicit: from charging prices on industrial output of public corporations yielding a rate of return below 4% of capital employed rather than 10%			1,500
% of GDP			2

Table 12

Major Categories of Exports and Imports

	1983/84	1984/85	1985/86	1986/87
Exports				
Petroleum	4532	4781	3995	2679
Egypt	2957	2891	2210	1470
Foreign Company	1575	1890	1785	1315
Cotton	452	414	356	343
Other Agriculture	211	140	119	123
Textiles	265	294	288	350
Other Manufactures	463	446	436	545
Imports				
Wheat and Flour	1056	1013	983	718
Other Agriculture	1877	1698	1583	1293
Intermediate Goods	3369	3532	3100	2222
Petroleum	514	469	303	189
Other Int. Goods	2855	3063	2797	2033
Capital Goods	3359	3475	3234	2412
Domestic Companies	2231	2398	2178	1719
Foreign Oil Comp.	1128	1077	1056	693
Manuf. Cons. Goods	1667	1875	1681	1808