ENCC

المجلس الوطني المصري للتنافسية

Egyptian National Competitiveness Council

BEYOND THE FINANCIAL CRISIS: COMPETITIVENESS & SUSTAINABLE DEVELOPMENT

The 6th EGYPTIAN COMPETITIVENESS REPORT

CAIRO, JUNE 2009

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Vision:

The ENCC will become an instrument of influence on government policies, business climate, and public attitudes to make the nation's institutions more globally competitive. It seeks to develop solutions for specific issues that will increase the productivity of business and workers.

Mission:

To improve the quality of life for all Egyptians, the ENCC will achieve its vision by being an efficient and effective platform that will bring together stakeholders — business, government, academia and civil society — in order to raise awareness and advocate policies that will enhance competitiveness.

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GREATER INTERNATIONAL COMPETITIVENESS

ACRONYMS

ACC	:	Agriculture Competitiveness Council
APE	:	Association for Protection of the Environment
BMI	:	Business Monitor International
BAC	:	Business Advisory Council
CPI	:	Corruption Perception Index
CAGR	:	Compound Annual Growth Rate
CAPMAS	:	Central Agency for Public Mobilization and Statistics
CBE	:	Central Bank of Egypt
CDM	:	Clean Development Mechanism
CIP	:	Citrus Improvement program
CO	:	Development Citizen Organization
CPA	:	Consumer Protection Agency
CSR	:	Corporate Social Responsibility
ECA	:	Egypt Competition Authority
ECES	:	Egyptian Centre for Economics Studies
ECL	:	Egyptian Cotton Logo
ECR	:	Egyptian Competitiveness Report
EEAA	:	Egyptian Environmental Affairs Agency
EEI	:	Egyptian Education Initiative
ERRADA	:	Egyptian Regulatory Reform and Development Activity
EITI	:	Extractive Industries Transparency Initiative
EIU	:	Economist Intelligence Unit
ENCC	:	Egyptian National Competitiveness Council
EOS	:	Egyptian Organization for Standardization and Quality
ESCAP	:	Economic and Social Commission for Asia and the Pacific
EU	:	European Union
FAO	:	Food and Agriculture Organization
FDI	:	Foreign direct investment
FEA	:	Friends of the Environment
G-20	:	Group of Twenty Countries
GCC	:	Gulf Cooperation Council
GCI	:	Global Competitiveness Index
GCR	:	Global Competitiveness Report
GDP	:	Gross Domestic Product
GFMIS	:	Government Financial Management Information System
GHG	:	Green House Gas
HEPCA	:	Hurghada Environmental Conservation and Protection Association
HIV/ AIDs	:	Human immunodeficiency virus /Acquired immune deficiency syndrome
HRCC	:	Human Resource Competitiveness Council
IALI	:	International Association of Labour Inspection
ICPEN	:	International Consumer Protection and Enforcement Network
ICT	:	Information and Communication Technology
IFAD	:	International Fund for Agricultural Development

ACRONYMS

IFC	:	International Finance Corporation
ILO	:	International Labour Organization
IMF	:	International Monetary Fund
IDSC	:	Information and Decision Support Centre
IPCC	:	Intergovernmental Panel on Climate change
IPU	:	Investment Promotion Unit
IPR	:	International Property Rights
ISO	:	International Organisation for Standardisation
ITIDA	:	Information Technology Industry Development Agency
L.E.	:	Livre Egyptien (Egyptian pound)
M FA	:	Multi-Fibre Arrangement
MDG	:	Millennium Development Goals
MDP	:	Media Development Program
MENA	:	Middle East and North Africa
MeTA	:	Medicine Transparency Alliance
MOF	:	Ministry of Finance
MTEF	:	Medium-Term Expenditure Framework
NIRs	:	Net International Reserves
NOA	:	National Outsourcing Association
NPLs	:	Non-Performing Loans
NREA	:	New and Renewable Energy Authority
NRI	:	Networked Readiness Index
NSDS	:	National Sustainable Development Strategy
OECD	:	Organization for Economic and Co-operation And Development
PEFA	:	Public Expenditures Financial Assessment
PETS	:	Public Expenditure Tracking Survey
PRI	:	Principles on Responsible Investment
R&D	:	Research and Development
RCI	:	Responsible Competitiveness Index
RIA	:	Regulatory Impact Assessment
SME	:	Small and Medium-sized Enterprise
KFAED	:	The Kuwait Fund for Arab Economic Development
TIMSS	:	Trends International Mathematics and Science Study
T&TCC	:	Travel and Tourism Competitiveness Council
TVET	:	Technical Vocational Education and Training
UNDP	:	United Nations Development Program
UNIDO	:	UN Industrial Development Organization
USAID	:	United states Agency for International Development
USD	:	US dollar
WBCSD	:	World Business Council for Sustainable Development
WDI	:	World Development Indicators
WEF	:	World Economic Forum
WEO	:	World Economic Outlook

MINISTERIAL TESTIMONIALS

DR. YOUSSEF BOUTROS-GHALI

Minister of Finance

Globalization has greatly influenced world economies over the past three decades. Boundaries between countries have dropped through mutual trade of goods and services and investment activities. These linkages made all economies closely tied together and more dependent on each other's economic fortunes. Contagion from the financial crisis spread rapidly through these channels, dampening growth rates over the globe. The collapse in confidence accompanying the financial crisis paralyzed the global financial sector. In the space of a few short months, countries went from robust growth to deep recession. In the most severe downturn since World War II, the world economy is expected to shrink by 1.3 percent in 2009.

While advanced countries are taking their share of the heat, the developing and poor countries are feeling a social pain manifested in increased poverty, even though they were innocent bystanders. Like many developing countries Egypt has not escaped the slowdown resulting from the financial crisis that has gripped the world. Its strong domestic economy has however served to soften the blow of the crisis relative to other countries.

Since October 2008, global actions have been focused nearly exclusively on resolving the financial crisis and stimulating growth rates. Many fiscal stimulus measures and stabilization mechanisms have been implemented across the world with the hope of pulling the world economy up by 2010. Egypt has also taken pre-emptive steps to stabilize the economy. A diversified frontloaded fiscal stimulus package of some L.E. 15 billion was recently implemented. Another package for 2009/2010 is under consideration. The aim of both packages is to shore up demand, generate employment and income for small businesses, and build the infrastructure projects of tomorrow that will increase the longer-term productivity of the Egyptian economy.

Are policies directed at resolving the financial crisis critically important? Yes. We policymakers are pre-occupied with applying the right mix of fiscal and monetary policy responses to reverse the decline. But is it a challenge we should focus on to the exclusion of all others? No. As compelling as the financial crisis is, it has served as a timely reminder of the difficult challenges accompanying Egypt's economic growth, and must not be allowed to distract us from other equally important risks that continue to undermine Egypt's growth and competitiveness. During the transition to global recovery we need to build the foundation for sustainable long term growth and competitiveness that will not only drive our economy beyond the present crisis, but will also enable it to emerge stronger and be able to respond to changes that cannot be predicted but that we know will come. The structure of the world economy will be changing in important ways, with effects that are difficult to predict. Crises tend to have lasting effects such as corporate failures and the attrition of skills that accompanies prolonged unemployment. Undoing these effects and their impact on the Egyptian economy will not be easy. The reforms we are implementing—business environment, trade, tax and budget changes—will prepare Egypt to face and join the new world order that will emerge from the crisis.

A final thought. The financial crisis does not mean that we should retreat from globalization. While greater openness and linkages with the global economy have allowed the financial contagion to impact Egypt, these same linkages will enable Egypt to recover rapidly when global growth is restored.

Youssef Boutros-Ghali
Minister of Finance

MINISTERIAL TESTIMONIALS

ENG. RACHID M. RACHID

Minister of Trade and Industry

The expanding role of civic society in bringing together different stakeholders and stimulating an open and serious dialogue on matters of national economic interest is very often a function of the increasing maturity of that society's constituents. The Egyptian National Competitiveness Council (ENCC), as one member of Egypt's civic society, has contributed to a policy dialogue on the economy in part through its Egyptian Competitiveness Report (ECR). This year's edition, the Sixth Egyptian Competitiveness Report, arrives at a truly critical juncture in time.

The economic policies put in place since mid-2004 have been discussed in prior editions (such as comprehensive fiscal, trade, investment and industrial policy reforms), and they remain the hallmark of Egypt's economic re-invigoration in recent years, with Gross Domestic Product (GDP) growth registering a comfortable 7.2 percent in fiscal year 2007-2008. Successes of that nature tend, however, to raise the standard and to elevate expectations. In essence, those of us in government are very keenly aware of the greater hurdles we now face as a result, not only because of the very challenging conditions of the global economy in 2008-2009, but precisely because of the impressive results posted in recent years. Although we have already seen GDP growth decline, growth remains at levels far better than many peers and more developed economies; it is a test of our ability to navigate through the challenges of the global storm. It is rare, however, when challenges ever present themselves without opportunities.

This year's edition of the ECR quickly takes on the effects on Egypt of the crisis in global financial systems. There are a number of worthwhile recommendations proposed which will certainly be examined further by government, particularly to give greater impetus to the LE 15 billion six-month stimulus package assembled at the end of 2008. The ECR's special focus on agriculture in this year's edition is very welcome, given that the food crisis in early 2008 remains a serious concern for policymakers. From the perspective of strengthening Egypt's competitive position, there are several suggestions which interact with agro-industrial policy, an area that the Ministry of Trade and Industry has invested heavily in so as to push Egypt further downstream in terms of value chains. The ECR's inclusion in the sixth edition of a section on responsible competitiveness, particularly from an environmental point-of-view, is exceptionally visionary. There is little doubt that the industries of the 21st century must be environmentally sound, not only because of the ecological threats facing the world, but because awareness of these threats has permanently altered consumer tastes and preferences. Good business sense demands it, if industries are to be competitive globally and locally.

In closing, it is an honor to have been invited to preview this year's edition of the ECR. Truly measurable progress in competitiveness requires a long-term holistic approach ranging from education to industry, from energy to infrastructure. The ENCC's role in maintaining the policy debate in these areas in the short-term helps all stakeholders to remain focused and open to new ideas.

Rachid M. Rachid
Minister of Trade and Industry

DR. MAHMOUD MOHEILDIN
Minister of Investment

As the global economy comes under extensive pressure to avoid falling victim to systemic recession, the launch of the Egyptian Competitiveness Report for the current year assumes special importance. The housing bubble in the United States and the associated proliferation of delinquencies on subprime mortgages has imposed a great toll on the global economy. The crisis has already triggered damage in the real economies of many countries in terms of losses in output, jobs and real wealth. While the Egyptian economy has been progressing with speed to integrate into the global economy by virtue of the series of liberalization measures which have accelerated starting mid-2004, the brunt of the global financial crisis has not been as harsh as what has been witnessed in the developed world as well as in many of the emerging markets. A key factor which has shielded the Egyptian economy from receiving a full-blow in the aftermath of global financial turmoil was that Egyptian banks had no exposure to toxic assets. Thanks to the financial sector reform program which was in 2005, liquidity remained sound as well as carefully regulated.

As the real economy in Egypt is adjusting to the fact that the timing as well as the strength of recovery from the global turmoil remains uncertain, real Gross Domestic Product (GDP) growth has been slowing down. With an average annual real GDP growth rate of 6.4 percent during the period 2004-2008, the Egyptian economy has been one of the fastest growing among emerging markets. The fact that we have been doing so well, having surpassed the world average, the average for the newly industrialized Asian economies and the average for the entire Middle East in terms of growth has, ironically, made analysts capture with increased interest the slowdown in real GDP growth to reach 5.8 percent and 4.1 percent during the first and second quarters of the 2008-09 fiscal year, respectively. Despite the slowdown, we remain positive regarding growth prospects beyond 2008-09. This view is shared by many analysts, with the International Monetary Fund (IMF) anticipating that Egypt will sustain its position as one of the world's fastest growing economies. Confidence in the future is anchored to hardcore facts. During the last four-year period, the Egyptian economy has seen a significant increase in the number of new establishments. Growth in the coming period will be supported by the momentum of investments that have been initiated. These projects are still in their initial development phases and are for the most part expected to continue with their plans unhindered.

While policy makers have intensified their efforts to promote Egypt as a relatively safe and stable haven for investments — both domestic and foreign — the issue of the 'quality' of investments will be taking center stage during the coming period. The relative efficiency with which resources —including labor and capital — are employed in production will invariably determine future prospects for the Egyptian economy in terms of capturing the needed levels of investor interest. This is becoming particularly true in the midst of a global investment environment which will only accommodate best-performers. Providing further support to productivity improvements in establishments operating in all economic and social domains is the key to sustainable long-term economic growth.

Mahmoud Moheildin
Minister of Investment

MINISTERIAL TESTIMONIALS

MR. AMIN ABAZA

Minister of Agriculture and Land Reclamation

The Egyptian agriculture sector has long been an important part of Egypt's culture and identity as well as a backbone of the economy. The country's fertile soil and yearly supply of Nile water offer a special comparative advantage and a historically important source of livelihood for rural Egyptians. Today, these assets are ready to be transformed into a major source of competitive advantage for Egypt.

But despite its sizable contribution to national GDP, employment and food security the agriculture sector has been facing mounting threats. The sharp fall in agriculture's share of investment, from 10 percent in 2004 to 5 percent in 2007, is an obvious symptom of the sector's perceived decline. As highlighted by chapter three of this report, before progress can be made looming problems such as overpopulation, desertification and climate change need to be adequately addressed. Most importantly, with increasing demand on scarce resources it is increasingly being recognized that growth within this sector must come from significant gains in productivity and efficiency.

It is also recognized that increased agricultural competitiveness is quite often a matter of policy changes including the creation of a stable macroeconomic environment that facilitates capital investments, efficient legislation and institutions and regulations that call for optimal resource allocation. To this end the adoption of a "Sector Transformation Strategy" by the government of Egypt represents a major step toward rebuilding sector competitiveness. The strategy seeks to build on the existing strengths of the agriculture sector — including its large export potential, production growth that has kept up with population growth and the availability of high-quality natural resource inputs — to enhance the long term economic contributions and value added of agricultural activities. Through its focus on agro-industry and the intersection of the agricultural and industrial sectors, the strategy hopes to foster more economic linkages and widespread growth. The second important focus of the strategy is resource optimization, which is not only vital for productivity but also the sustainability of the sector. Better resource management can be a way to tap into the higher value added markets of organic agriculture as well as a source of greenhouse gas emission reductions in Egypt.

Due to the emergence of opportunities brought about by the twin crises of global food security and climate change, the Egyptian agriculture sector has vast economic potential. It is anticipated that over the next 10 years Egypt's 1,740,000 new jobs will be created by the agriculture and agro-industry sectors, a trade balance surplus of LE 26.2 billion will replace the current LE 8.6 billion deficit and annual agriculture GDP growth will double to 5.25 percent from the historical average of 2.16 percent. However, the sector can also become a major drag on national competiveness if a collective government and private sector effort is not made.

This report is a step toward realizing the aforementioned gains. This is because fostering stakeholder dialog and disseminating information is essential in tipping the balance away from agriculture as a competitive disadvantage toward a competitive advantage and an engine of growth and prosperity.

Amin Abaza
Minister of Agriculture and Land Reclamation

ENG. MAGED GEORGE ILLIAS

Minister of State for Environmental Affairs

Egypt's competitiveness depends largely on the quality and availability of natural resources and on the country's capacity to steward its environmental and natural resources. Egypt has made notable effort and progress in the area of environmental management. We were among the first in the region to adopt environmental legislation and standards. We are among the earlier signatories of environmental conventions and active participants in the international arena. We established an environment protection fund and actively sought financial and technical support from our development partners. We implemented activities with tangible results throughout the various sectors. However, we now need to move to the next phase.

Egypt aspires for a larger share in the international market, and for higher economic growth, but financial and natural recourses are scarce. It is only by protecting its resource base can Egypt move forward on the path to greater and sustained competitiveness. Responsibility towards the environment is not a luxury for the rich. It is a prerequisite for further economic advancement. The casual relationships between responsibility and competitiveness remain complex, but are most certainly there. Experience around the world has shown that adopting a more responsible approach to development is an integral part of competitiveness.

This report is valuable in that it shows that Egypt's next stage needs, in addition to compliance with environmental requirements, to also be driven by its desire to become an actor in the global market. Egypt's environmental improvements need not be driven solely by the stick of national and international legislation. They need to be also driven by the realization of the pressures and the sustainable dealing with our valuable natural resources; by an internal desire to improve living conditions. Most importantly, they need to be based on local innovation.

Innovation pays off. Global markets are increasingly rewarding responsible behavior of firms, and the demand for innovation in environment is rising exponentially worldwide. The global markets for environmental technology are estimated at 100 billion Euros and are growing.

Improvement in environmental conditions requires a consolidation of all efforts from governmental, non-governmental and civil society organizations and is not the responsibility of one specific party. It is in this context that a National Sustainable Development Strategy (NSDS) sets the stage for effective action towards responsible and sustainable competitiveness. A NSDS is not a government plan, but rather a forum where the combined innovations from the government, business sector and civil society will yield goals and strategies that enhance sustainable development. A national sustainable development strategy is essential for Egypt as it harnesses the combined forces of the government; business sector and civil society to capitalize on opportunities that will help Egypt become more competitive and offer a better quality of life now and for generations to come.

Maged George Illias
Minister of State for Environmental Affairs

PREFACE BY

Honorary Chair of the Egyptian National Competitiveness Council

Prof. Hossam Badrawi M.D., M.P.

One of the most valuable national resources a country can have is its people. With a population of 75 million, over a third of which are below the age of 15, Egypt has the largest workforce in the region. This endowment can work to the detriment or advantage of Egypt's national competitiveness depending on how the country chooses to invest in its human capital.

Human resource underdevelopment is presently a major competitive disadvantage for the country. The 2008-2009 Global Competitiveness Report showed higher education and training as well as labor market efficiency to be two major areas of weakness pushing down Egypt's overall competitiveness ranking. On the other hand, countries which have performed remarkably well over the past decade have done so with the help of a well-educated and highly skilled workforce. Examples include Taiwan, South Korea and Israel whose impressive competitiveness rankings are underpinned by high levels of educational attainment and quality instruction.

In today's globalized labor markets, economic gains hinge upon the availability of knowledge, know-how and expertise, making a strong case for greater investments in human capital. The returns to such investments can help us meet short-term goals including Gross Domestic Product (GDP) growth, Foreign Direct Investment (FDI) and employment creation — all of which are vital priorities for Egypt — as well as advance long-term innovative and productive capacity. This includes the ability to employ more advanced management systems and bolster more high-tech and IT-driven sectors.

Efforts are underway to improve Egypt's human capital base. A new National Strategy for Education is being considered by the Ministry of Education and already, the government allocates a substantial amount of resources, nearly 5 percent of GDP each year, toward education. The high levels of public spending have coincided with a decrease in illiteracy, which fell from 39.4 percent in 1996 to 29.3 percent in 2006, and an increase in enrollment rates. Between 1995 and 2005, net enrollment rates increased by 13.2 percent for primary, 5.75 percent for secondary and 4.36 percent for tertiary education. Nevertheless, certain aspects of Egypt's education system require further attention. Priorities need to include the refinance of higher education to increase quality and equality; expansion of primary and secondary enrollment and improvement of the quality of vocational education. Addressing the missing link between the education system and labor market needs is another chief area of concern. It demands much greater public-private coordination to invest in the nation's human resources.

In 2008, the Egyptian National Competitiveness Council took a bold step toward addressing these needs by establishing the Human Resources Competitiveness Council (HRCC). The HRCC brings together key stakeholders to raise awareness, obstacles to human resources competitiveness and suggest ways to overcome these obstacles. Its action plan for the upcoming year includes several innovative and promising initiatives and a special focus on higher education.

In closing I would like to note that investing in individuals is as much about spreading the gains of global economic integration and enhancing the social mobility of ordinary citizens as it is about wealth accumulation. It is a win-win investment which is rightly emphasized in this and past Egyptian Competitiveness Reports. It is my hope that this information becomes the necessary catalyst for change now and in upcoming years.

Hossam Badrawi
Honorary Chair of the Egyptian National Competitiveness Council

PREFACE BY

Chair of the Egyptian National Competitiveness Council

Helmy Abouleish

The 6th Egyptian Competitiveness Report comes at a critical time for Egypt. Like other developing countries, Egypt must learn to survive and even flourish within a turbulent global economy in the midst of an unfolding environmental crisis. The present volume tackles the vital issues of climate change and sustainable development in the Egyptian context. Studies have shown that even a slight change in weather patterns will jeopardize important industries and economic sectors. Also at stake are Egypt's dwindling water supplies and national food security, both already threatened by a rapidly growing population. These risks make it increasingly obvious that climate change is as much a local problem as it is a global one.

Egypt has been making gradual progress toward sustainability, particularly in the area of renewable energy. Investments in solar, wind and biomass technologies as well as energy efficiency have grown significantly. Other areas are in need of renewed attention. Sustainable agriculture is a key example. Given the importance of the agricultural sector as a source of GDP, employment and food security, it is alarming that more is not being done to protect it. A focus on more sustainable agriculture techniques would not only increase the efficient use of Egypt's water and energy resources, but could also transform the sector into a major carbon sink due to the potential for soil carbon sequestration – capturing up to 942.7 kg/feddan/year according to the Rodale Institute.

How we define the relationship between sustainability and national competitiveness will be critical to any future progress. Sustainable development is widely known as the ability to meet the needs of present generations without compromising the ability of future generations to meet their needs. National competitiveness, on the other hand, is about long-term prosperity and improving standards of living. The two goals are not only consistent but can be mutually reinforcing through a combination of innovative public policies, forward looking corporate strategies and wider public participation. Specifically we as a nation must first, consider the wider social, environmental as well as economic consequences of each decision and second, replace short term planning horizons with long-term ones.

In order to achieve more "responsible" competitiveness – i.e. markets that balance economic outcomes and broader social and environmental goals - a number of countries are espousing National Sustainable Development Strategies or NSDS. It cannot be considered a silver bullet for environmental problems. Nevertheless, an Egyptian NSDS is an essential element to a balanced long term development that is mindful of both future generations and existing underprivileged communities that suffer disproportionately from unmitigated environmental damage.

A chief message in this report is that, in a world where risk and uncertainty is the norm not the exception, more can and must be done to protect the natural resources upon which 75 million Egyptians depend. A more responsible and environmentally sustainable competitiveness requires nothing short of a concerted effort among civil society groups, the private sector as well as individual citizens.

Finally, I would like to thank all of the individuals who have contributed to this report and those who have lent their valuable time, insight and support to promote a shared vision of a more competitive and prosperous Egypt.

Helmy Abouleish
Chair of the Egyptian National Competitiveness Council

EXECUTIVE SUMMARY

Mona El Baradei

In its sixth year of publication the Egyptian Competiveness Report (ECR) continues to strive to bring thorough analysis, multi-stakeholder insight and solutions to Egypt's development discourse. The annual report is dedicated to presenting key challenges and hurdles to Egyptian competitiveness. Chapter one sheds light on persistent areas of decline including macroeconomic stability, higher education and training, and health and primary education, signaling the need for stronger human resource development and broad economic reform. Since 2006, it has also included special sections examining sectors which are critical to enhancing competitiveness, each year bringing a different sector into the spotlight.

The 2008 ECR identified a number of prevalent problems in the Egyptian economy namely inflation, high budget deficit, unbalanced growth and a mismatch between skills and labor market demands. It also examined Egypt's ability to cope with global threats like energy security, resource depletion and climate change. This year's report builds upon previous findings, but it also focuses on new challenges facing the nation like the current financial crisis, promoting sustainable agriculture and adopting a National Sustainable Development Strategy (NSDS). The global financial meltdown, which reached full scale by September 2008, is tackled in chapter two along with its ramifications for Egypt. Although Egypt's economy has faired relatively well, its ability to remain on track with macroeconomic reforms and sustained growth rates hangs in the balance.

Chapter three focuses on agriculture which was selected to be the sectoral focus of the 2009 ECR. This is not only because of the sector's vast future potential in terms of untapped sources of value added but more importantly, because agriculture development can be used to simultaneously address a number of challenges. From inflation and unemployment to food security, energy security and climate change, agriculture can create more balanced and sustainable growth. In addition to being a carbon sink and source of biomass, improved resource optimization and organic production techniques in this sector represent relatively easy and cost effective ways to reduce Egypt's carbon footprint. Finally, in line with chapter three, chapter four expands and elaborates on the idea of responsible competitiveness for a sustainable and prosperous Egypt. One of the main goals of the chapter, and indeed of this report, is to help promote a NSDS for Egypt.

EGYPTIAN COMPETITIVE PERFORMANCE IN 2008-2009

Egypt's score on the Global Competitiveness Index (GCI) has been relatively stable over the last couple of years. Yet, its ranking has deteriorated from 77 out of 131 in 2007-2008 to 81 out of 134 in 2008-2009. Chapter one reviews Egypt's competitiveness ranking and explores the main reasons for the decline. The main areas of weakness include macroeconomic stability, goods market efficiency, higher education and training and health and primary education where Egypt ranked 125, 106, 91 and 88 out of 134 countries respectively. By far the most alarming ranking was the labor market efficiency where Egypt ranked last out of 134 countries, dropping four positions from its 2007-2008 rank of 130 out of 131 countries.

The low and declining rankings in labor market efficiency, higher education and training and health and primary education reflect a major deficiency in human resource development in Egypt. The reasons for this include the very poor quality of instruction across education levels and unequal access to education. The result is a highly uneven pattern of growth and a labor market that lacks the quantity or quality of skills it needs. The pillars on which Egypt showed improvement both in terms of score and rank were those of infrastructure, market size and financial market sophistication. Egypt also made progress in fostering technological readiness in terms of increased penetration of Internet, PCs and mobile telephones. However, progress in these areas did not offset the poor performance in other pillars, where Egypt's position is

rapidly deteriorating. A central message of chapter one is that there is a clear need for Egypt to focus on macroeconomic stability and human resources — in particular education and labor market reform — which will be vital for any improvements in competitiveness.

MACROECONOMIC STABILITY THROUGH THE FINANCIAL STORM

Chapter two examines Egypt's macroeconomic competitiveness and the impact of the financial crisis. Since 2004, macroeconomic reforms have stabilized the exchange rate, reduced fiscal deficit and public debt, enhanced public financial management and improved the business and investment climate in Egypt. Reductions in customs duties and the cost of doing business have boosted the country's external competitiveness and growth rates have gone from 4 percent in June 2004 to 7.2 percent in June 2008. But despite these improvements in Egypt's economic fundamentals, macroeconomic stability remains a major weakness. Dropping one position from last year to 125th out of 134 countries, the macroeconomic stability pillar was the second lowest ranked for Egypt in 2008-2009. Chapter two explains this apparent paradox and offers important insights into the sources of weakness within the macroeconomy.

The international economic slowdown has only exacerbated Egypt's macroeconomic problems. Although weakening demand has caused a decline in commodity prices, (especially oil) as a commodity exporter Egypt's losses have outweighed its gains. Revenues from the Suez Canal and tourism have seen sharp drops – especially the latter – while construction activity and foreign investment have been scaled back due to limited international liquidity. Thus far Egypt's sound fundamentals have helped it brave the first effects of the financial crisis but how it will fare over upcoming months remains to be seen.

The Ministry of Finance has agreed to spend an additional LE 13.5 billion or 1.34 percent of Gross Domestic Product (GDP) by June 2009 to stimulate growth, increase public investment and ensure social security and poverty reduction is not compromised. The stimulus package is expected to provide stability, but will also increase public debt levels. Striking a balance between short-term fiscal spending to spur economic growth and long-term fiscal deficit and competitiveness is now the daunting task facing the Egyptian government. One important lesson to be learned is that while globalization can have large economic benefits for Egypt, there are also major risks that require appropriate precautions.

NEW OPPORTUNITIES FOR A MORE COMPETITIVE AGRICULTURE SECTOR

The chapter highlights the strengths and weaknesses of the Egyptian agriculture sector as well as the opportunities and threats it faces. Historically a major source of comparative advantage, the sector employees 27 percent of the work force and generates approximately 15 percent of GDP. Agriculture production has grown at a Compound Annual Growth Rate (CAGR) of 1.8 percent over the past 15 years and even kept up with population growth thanks to the availability of Nile water, basic infrastructure, cheap labor and fertile soil. However, the sector is plagued by low labor productivity and inefficient resource use, among other endemic problems discussed in the chapter.

The Egyptian government has recently formulated an agricultural transformation strategy geared towards enhancing agri-industrial production and generating national economic growth. It seeks to strengthen the links between the agriculture and industrial sectors to increase competitiveness and generate larger combined spillovers. A main aim of this year's report is to promote that strategy and underscore the importance of a better organized agriculture value chain. Sustainable agriculture is a topical issue discussed in chapter three of the report. Beyond being a source of economic growth and national competitiveness, Egypt's agriculture sector has the potential to pave the way for a sustainable path of development. The benefits include better soil quality, higher energy efficiency, minimized fertilizer/pesticide consumption and contamination, and improved productivity. Six strategic objectives encompassing a number of measures at farm, industry and national levels are suggested for adoption in the transformation strategy.

SOCIAL RESPONSIBILITY: COMPETITIVENESS FOR PRESENT AND FUTURE GENERATIONS

Responsible competitiveness, the main theme of chapter 4, builds on this notion of long-term economic gains without compromising social and environmental goals. Amidst daunting domestic challenges, Egypt must also make every effort to deal with a mounting climate change threat. Because of the disproportionate impact of environmental risks, it is a necessity more than a luxury that developing countries like Egypt achieve competitiveness in a way that is socially and environmentally responsible.

The chapter also examines Egypt's performance on the Responsible Competitiveness Index (RCI). Created to help countries benchmark their progress toward sustainability, the RCI identifies Egypt as a complier or mid-performing country meaning that it is striving to meet international standards of quality, labor and environmental protection in order to further integrate economic activities in international market. One of the index's main messages is that responsibility is not only compatible with competiveness, but that the two goals can be mutually reinforcing. A shift toward the sustainability paradigm can also create opportunities for new industries such as renewable energy, eco-tourism, carbon trading and recycling industries. It can also be a way to foster productivity through the greater use of IT technologies and advanced production techniques that are cost-effective and less resource and pollution intensive.

To effectively balance economic, social and environmental goals Egypt needs a comprehensive national strategy along with significant willpower and wide-reaching stakeholder involvement. Currently under discussion is a National Sustainable Development Strategy that will allow Egyptians to avoid impending threats and seize the new opportunities created by environmental challenges. The chapter seeks to promote such a coordinated and high-level effort among policymakers and private sector businesses as the potential for responsible competitiveness is being tapped in more and more countries.

EGYPT MOVING FORWARD

The world economy has reached a watershed in 2009. Recent international experience has shown that piece-meal and fragmented approaches to economic development have run their course. With a world as interconnected as it is today, it will be the nations that are 'connected' within themselves, that will be most competitive, going forward.

Releasing potential capital and wealth depends on visualizing and then materializing high-value new applications for existing assets. It means mobilizing alternative uses for land, natural, human and other national resources so as to convert comparative advantage into competitive advantage. This can be done most effectively in the context of a whole of government and a connected-nation approach. So, future progress depends on a comprehensive approach — improving all key elements in parallel. The Egyptian National Competitiveness Council (ENCC) believes that great strides in competitiveness can be made through an integrated approach based on three inter-related mechanisms; connectivity, productivity and responsibility — where the nation's resources are effectively applied in support of a unified vision and strategy.

Connectivity advocates the need to create a collective national vision of a more competitive Egypt, bringing Egyptians together to build a consensus around the need for major change. This entails more dialog, communication and a 'connected' government, where ministries cooperate with each other as well as the private sector and the Egyptian community at large. The end goal is to form a national team moving together in one direction: forward. Raising productivity, at all levels, is a fundamental step to creating a competitive Egypt. Productivity extends beyond maximizing output to a focused and dedicated leadership which can visualize and create new sources of value: a leadership which will orchestrate efforts at the corporate, industry and national levels to ensure the greatest possible national gain. Finally, responsibility reflects a firm commitment to sustainability and equity. It lays the foundation for national competitiveness that benefits everyone and embraces social and environmental goals. For Egypt, connectivity, productivity and responsibility represent the essential building blocks of international competitiveness and long-term development.

Egypt's Competitiveness Indicators

Malak Reda

Egypt's score on the Global Competitiveness Index (GCI) has not changed over the last few years. Yet, its ranking has deteriorated from 77 out of 131 countries in 2008 to 81 out of 134 this year. The decline in ranking is largely driven by three key weaknesses in the Egyptian economy: macroeconomic instability, poor labor market efficiency and the weak quality of educational institutions. Macroeconomic instability remains a major challenge for the government, as reflected in the very low ranking obtained in this pillar (Egypt ranked 125 out of 134 countries). In labor market efficiency, Egypt ranked last among all 134 countries. The quality of Egypt's educational institutions ranked just 124th. To improve Egypt's competitiveness, adequate plans have to be put in place to achieve macroeconomic stability, improve the quality of education and increase labor market efficiency.

This chapter first examines Egypt's results and compares them to other countries with the aim of drawing recommendations for improved economic policies and institutional reforms. The chapter then reviews trends in key competitiveness indicators and cross-references the scores obtained in the GCI with other independent data and results of other studies. Unless otherwise stated, comparisons are for the results of the Global Competitiveness Report (GCR) of 2008-09 as compared to 2007-08.

1.1 EGYPT'S COMPETITIVENESS

Egypt's competitiveness score has been stable over the last few years at 4.0 (scores range between 1 and 7; 1 being the worst and 7 being the best). The lack of improvement has led to the decline of Egypt's rank vis-à-vis other countries. Table 1.1 shows Egypt's score and ranking in the last three consecutive indices (2006-2009). If Egypt's rank is divided by the total number of countries per year, a deterioration in Egypt's absolute rank from 0.58 in 2006-07 to 0.59 in 2007-08 to 0.60 in 2008-09 is apparent.

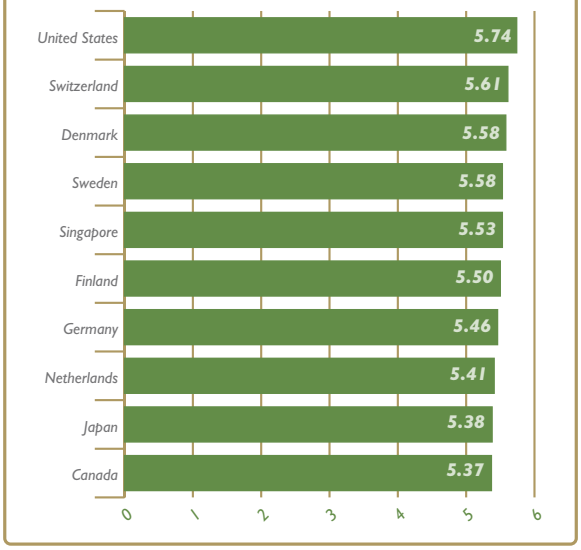
Table 1.1: *Egypt's Performance on the Global Competitiveness Index*

	Rank	Score (1-7)
GCI 2008-2009 (out of 134 countries)	81	4.0
GCI 2007-2008 (out of 131 countries)	77	4.0
GCI 2006-2007 (out of 122 countries)	71	4.0

Source: World Economic Forum (WEF). The Global Competitiveness Report 2008-2009. Geneva. 2008. (hereafter referred to as "WEF 2008").

As shown in Figure 1.1, the U.S., Switzerland, Denmark, Sweden, Singapore, Finland, Germany, the Netherlands, Japan and Canada were the top 10 performing countries in the 2008-2009 GCI. The number one performer in both 2007-2008 and 2008-2009 was the United States of America with a score of 5.7 despite the financial crisis and macroeconomic weaknesses. The reasons for the exceptional performance of the USA are its highly sophisticated and innovative companies operating in very efficient factor markets and its excellent university system that collaborates strongly with the business sector in research and development (R&D). As compared to the United States, Egypt ranked 77th in business sophistication, 67th in innovation and 91st in higher education and training.

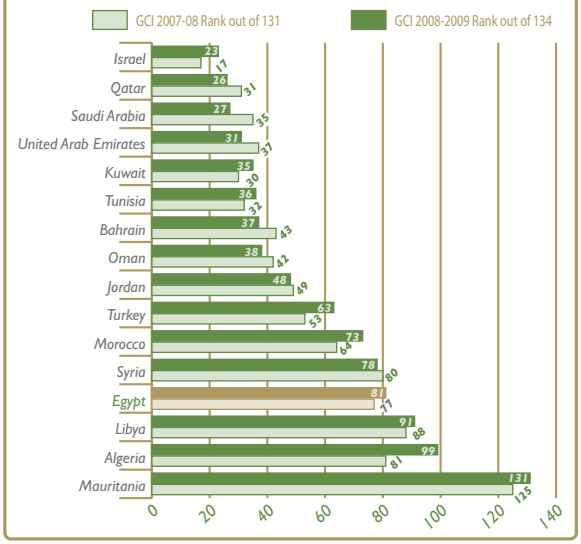
FIGURE 1.1: *TOP 10 COUNTRIES IN GCI 2008-2009 BY SCORE*



Source: WEF 2008.

Compared to other Middle East and North Africa (MENA) region countries, Egypt's rank was worse than most of the countries with the exception of Syria, Algeria, Libya and Mauritania in the GCI 2007-2008 and Libya, Algeria and Mauritania in the GCI 2008-2009. Of the top 10 countries in the MENA region, seven improved their ranking, further expanding the gap between Egypt and the most competitive countries in the MENA region. Egypt's ranking is compared to other MENA countries in Figure 1.2.

FIGURE 1.2: *EGYPT'S RANK COMPARED TO OTHER MENA COUNTRIES IN 2007 & 2008*



Source: WEF 2008.

If we compare Egypt to other MENA countries in the same stage of development, namely Syria and Mauritania, we note that Egypt's rank was higher than both of them in 2007. Yet, in 2008 Syria's ranking surpassed that of Egypt. Table 1.2 categorizes MENA countries according to stage of development and Gross Domestic Product (GDP) per capita.

Table 1.2: *MENA Countries Classified by Stage of Development and GDP Per Capita*

Stage of development	Stage 1	Transition from 1 to 2	Stage 2	Transition from 2 to 3	Stage 3
	Factor driven		Efficiency driven		Innovation driven
GDP per capita in (US$)	<2,000	2,000-3,000	3,001-9,000	9,001-17,000	>17,000
MENA countries	Egypt Mauritania Syria	Jordan Kuwait Libya Morocco Oman Saudi Arabia	Algeria Tunisia	Bahrain Qatar Turkey	Israel UAE

Source: WEF 2008.

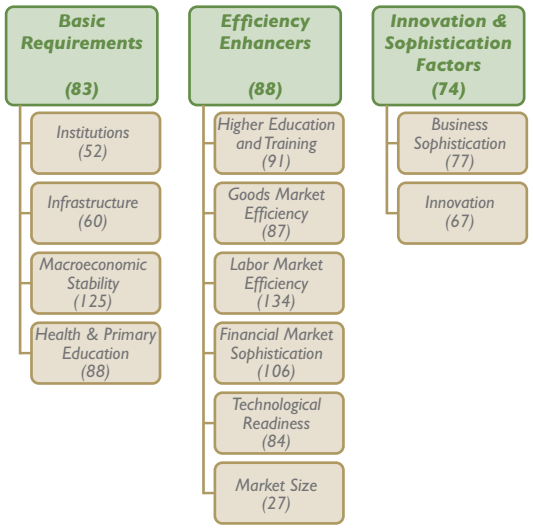
1.2 EGYPT'S PERFORMANCE IN THE 12 PILLARS

Egypt's position in all three competitiveness sub-indices has deteriorated in 2008-2009 as compared to the previous year. Egypt lost four places in the basic requirements index, three places in the efficiency enhancers' index and eleven places in its ranking in the innovation and sophistication factors index. The deterioration of Egypt's position is due to neither the increase in the number of countries covered[1] nor to methodological changes, as weights assigned for the various components have been steady over the last couple of years.

Indeed, understanding the underlying causes of the decline in Egypt's ranking requires an examination of the various pillars and their related indicators, allowing for an assessment of the areas of weakness and strength, and the development of policy recommendations for fostering greater competitiveness. Unless otherwise mentioned, Egypt's results will be compared for the years 2008-09 and 2007-08 as prior to this date the weights for the various pillars were different.

Figure 1.3 presents a summary of Egypt's results in the GCI 2008-2009. Egypt's ranking was particularly poor vis-à-vis the other 133 countries in the following pillars: macroeconomic stability and health and primary education under the basic requirements index; and higher education and training, financial market sophistication and labor market efficiency under the efficiency enhancers index.

FIGURE 1.3: *EGYPT'S RANK ON THE 12 PILLARS OF THE GCI 2008-2009 (HIGHEST=1, LOWEST= 134)*



Source: WEF 2008.

[1] The total number of countries increased by three in 2008-09 as compared to 2007-08, whereas Egypt's overall ranking deteriorated by four positions.

Where did Egypt improve?

The pillars in which Egypt improved both in terms of score and ranking vis-à-vis other countries in 2008-09 as compared to 2007-08 were: infrastructure, technological readiness, market size and financial market sophistication.

Mixed results are witnessed in the pillar for private and public institutions where the score improved but the rank of Egypt declined by one position, signaling that other countries are developing faster.

Where is Egypt uncompetitive?

Poor ratings in macroeconomic stability, goods market efficiency, business sophistication and human resources development led to the decline in Egypt's competitiveness ranking.

As shown in table 1.3, a comparison of 2007-08 and 2008-09 rankings reveals that the macroeconomic stability score declined by 18 percent. As a result, Egypt lost one position in this pillar. In terms of goods market efficiency, Egypt's score deteriorated by 3 percent leading to a decline in relative ranking in this pillar by 11 ranks compared to other countries.

Looking at human resources development, Egypt lost a total of 20 ranks in aggregate relative to other countries: 5 positions for health and primary education, 11 positions for higher education and training, and 4 positions for labor market efficiency. Egypt's score in the business sophistication pillar declined by 15 percent leading to a loss of 10 ranks in relation to other countries. The innovation ranking remained at 67, yet Egypt's score has declined slightly. While the labor market score improved slightly in 2008-09, Egypt still lost four positions in ranking to become the worst performer in all 134 countries.

Analysis of the results reveals that there is a definite need for Egypt to focus on macroeconomic stability and human development (education, health and labor issues) as they are essential to improving competitiveness.

Table 1.3: ***Two-year Comparisons of Egypt's Scores and Ranks on the 12 Pillars of the GCI (2007-2008 and 2008-2009)***

	Score GCI 2007-2008	Score GCI 2008-2009	% Change	Improve (↑) Decline (↓)	GCI 2007-2008 Rank out of 131	GCI 2008-2009 Rank out of 134	Δ In Rank	Improve (↑) Decline (↓)
1st pillar: Institutions	4.19	4.25	5%	↑	51	52	-1	↓
2nd pillar: Infrastructure	3.54	3.74	20%	↑	62	60	2	↑
3rd pillar: Macroeconomic stability	3.74	3.56	-18%	↓	124	125	-1	↓
4th pillar: Health & primary education	5.23	5.19	-4%	↓	83	88	-5	↓
5th pillar: Higher education & training	3.68	3.56	-12%	↓	80	91	-11	↓
6th pillar: Goods market efficiency	4.03	4.00	-3%	↓	76	87	-11	↓
7th pillar: Labor market efficiency	3.21	3.26	5%	↑	130	134	-4	↓
8th pillar: Financial market sophistication	3.50	3.68	18%	↑	113	106	7	↑
9th pillar: Technological readiness	2.84	3.04	20%	↑	87	84	3	↑
10th pillar: Market size	4.52	4.67	16%	↑	31	27	4	↑
11th pillar: Business sophistication	4.08	3.93	-15%	↓	67	77	-10	↓
12th pillar: Innovation	3.17	3.15	-2%	↓	67	67	0	-

Source: WEF 2008

A. Basic Requirements

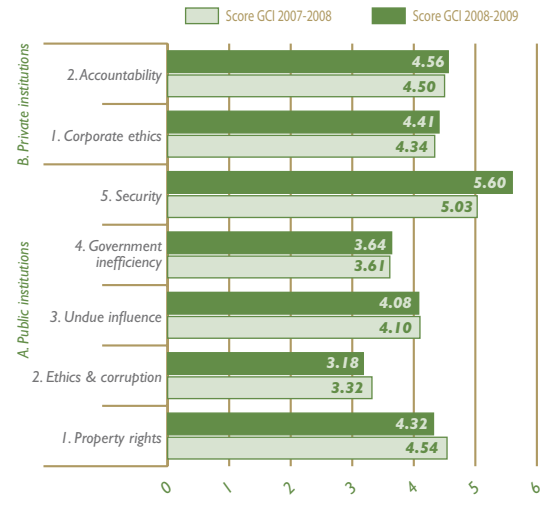
The basic requirements index includes four pillars: institutions, infrastructure, macroeconomic stability, and health and primary education. These four pillars represent 60 percent of Egypt's overall competitiveness score.

Pillar 1: Institutions

This pillar examines private sector perception of public and private institutions. It evaluates perceptions of public institutions in key dimensions including property rights, ethics and corruption, undue influence, government inefficiency and security. As for private institutions, the evaluation includes perceptions along the following dimensions: accountability and corporate ethics. The overall public institutions rank declined by two positions, whereas the private institutions improved by three ranks. Notable improvements were achieved in the security dimension (business cost of terrorism, business cost of crime and violence, organized crime and reliability of police services) as observed by the increase in score from 5.03 to 5.6 and increase in ranking by 16 positions in those areas as shown in Figures 1.4 and 1.5.

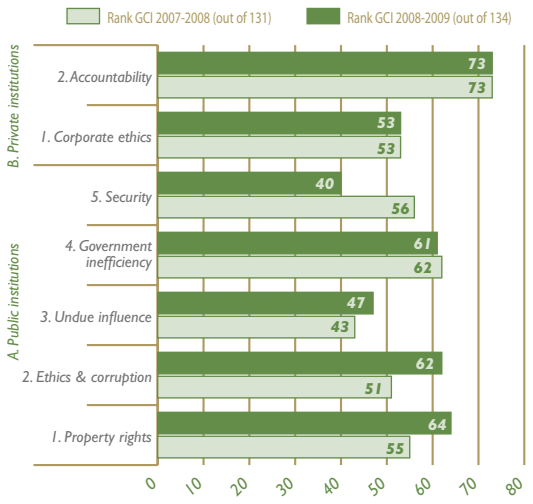
Areas where Egyptian public institutions declined include the protection of property rights, which deteriorated from 55 to 64. The ethics and corruption ranking deteriorated by 11 positions from 51 to 62. Favoritism in decisions of government officials[2] deteriorated to 61 from 50 (a loss of 11 positions). Wastefulness of government spending[3] also deteriorated by 19 ranks from 67 to 86.

FIGURE 1.4: *EGYPT'S SCORES ON THE KEY COMPONENTS OF THE INSTITUTIONS PILLAR IN 2007-08 & 2008-09*



Source: WEF 2008.

FIGURE 1.5: *EGYPT'S RANKING ON THE KEY COMPONENTS OF THE INSTITUTIONS PILLAR IN 2007-08 & 2008-09*



Source: WEF 2008.

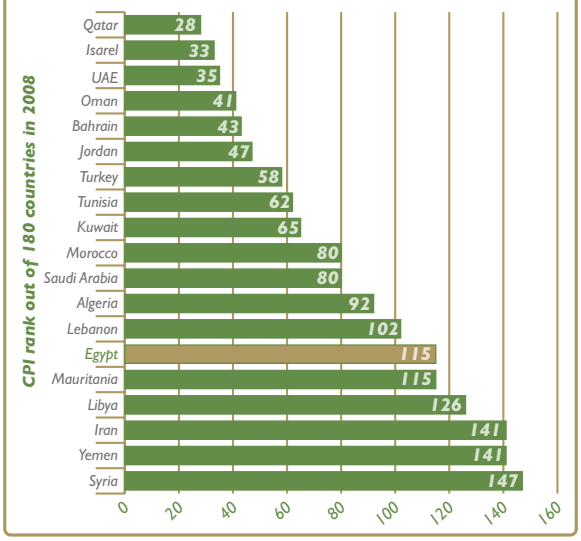
Under the institutions pillar, Egypt had a key comparative advantage vis-à-vis other countries in judicial independence (42 out of 134), business costs of crime and violence (23 out of 134) and organized crime (21 out of 134).

The perceived corruption results of the Executive Opinion Survey (EOS) are also confirmed by Egypt's poor ranking in the global corruption index that is compiled by Transparency International on an annual basis. The Corruption Perception Index (CPI) ranks the countries of the world according to "the degree to which corruption is perceived to exist among public officials and politicians." Corruption is defined as "the abuse of entrusted power for private gain." In the 2008 CPI, Egypt tied with four other countries for the 115th place out of the 180 countries included in the survey. Egypt's score is 2.8 out of 10 compared to 2.9 a year earlier. Scores under 5 indicate "a serious corruption problem." Compared to other MENA countries, Egypt lagged behind (Figure 1.6 demonstrates CPI ranks of MENA countries in 2008).

[2] Favoritism in decisions of government officials is one of two indicators within the sub-component undue influence. The second indicator that falls under undue influence is judicial independence.

[3] Wastefulness of government spending is one of the indicators under the government inefficiency sub-component.

FIGURE 1.6: *EGYPT'S RANK COMPARED TO OTHER MENA COUNTRIES IN 2008*

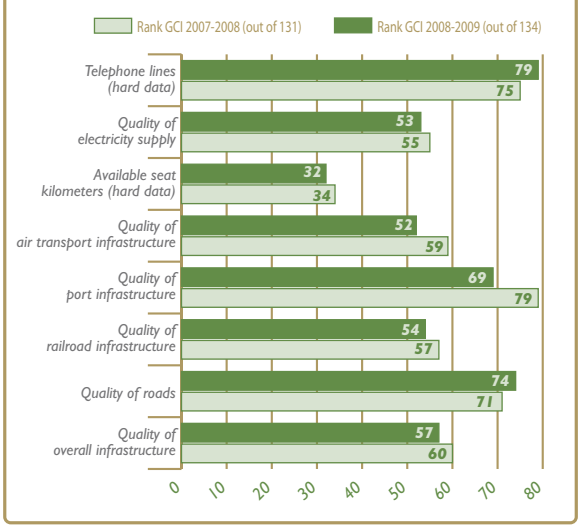


Source: Transparency International. Corruption perception index (2008).

Pillar 2: Infrastructure

Egypt's infrastructure score in 2008-09 improved by 20 percent (two ranks) compared to the previous year's rank. This is attributable to the improved perception regarding the quality of infrastructure, particularly ports, air transport infrastructure and electricity supply (Figure 1.7). Nevertheless, the perceived quality of roads has deteriorated. It is worth noting that the low quality of roads undermines Egypt's potential as one of the leading global tourism destinations. It is one of the attributes that led to the decline of Egypt's travel and tourism competitiveness ranking to 66 out of 130 countries in 2007-08 instead of 58 out of 124 countries a year earlier.

FIGURE 1.7: *EGYPT'S RANKING ON THE KEY COMPONENTS OF THE INFRASTRUCTURE PILLAR IN 2007-08 & 2008-09*



Source: WEF 2008.

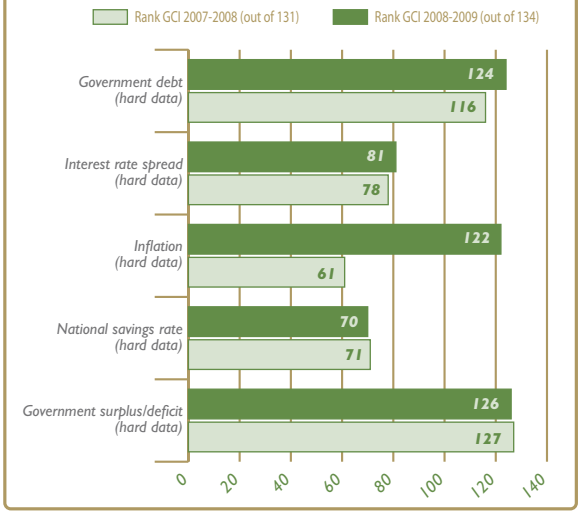
Egypt's telecom infrastructure is a liability. It is worth noting that the indicator used in this respect is the penetration rate of fixed telephones. Egypt's fixed telephone lines stood at 14.3 percent of the population in 2006, lower than many other countries. However, the fixed line penetration does not reflect the status of connectivity in the country as mobile phones are increasingly replacing fixed telephones.

Under the infrastructure pillar, Egypt had only one competitive advantage relative to other countries, namely available seat / kilometers, where Egypt ranked 32nd out of 134 countries. This indicator measures the number of seats available on each flight multiplied by flight distance in kilometers for the weekly average.

Pillar 3: Macroeconomic Stability

Egypt's ranking in this pillar is very poor. Egypt was ranked 125th out of 134 countries in the 2008-09 GCR. Macroeconomic stability is one of the biggest reasons for Egypt's overall low rank. A fiscal deficit, relatively high inflation, alarming government debt and a wide interest rate spread explain the low rank in this pillar (Figure 1.8).

FIGURE 1.8: *EGYPT'S RANKING ON THE KEY COMPONENTS OF THE MACROECONOMIC STABILITY PILLAR IN 2007-08 & 2008-09*



Source: WEF 2008.

The hard data used for the macroeconomic stability pillar in the GCI 2008-09 date back to 2007. At the time, government gross debt to GDP was huge at 105.8 percent in 2006-07. The inflation rate was high relative to other countries at 11 percent in 2006-07. Government deficit as a percentage of GDP was 5.7 percent in 2006-07. The interest rate spread between lending and deposits rate stood at 6.4 percent

in 2007. All of the above factors dragged Egypt's ranking down. According to Central Bank of Egypt data (CBE), annual inflation reached 11.7 percent in 2007-08, peaking at 22.4 percent in September 2008. It started falling gradually due to the slow-down of global demand and the drop in fuel and food prices. By February 2009, inflation had dropped to 14.2 percent, it further declined to 11.7 by April 2009. According to the Ministry of Finance, net domestic budget sector debt as a percentage of GDP decreased to 53.4 percent in June 2008 as compared to 67.4 percent in June 2004. The budget deficit was 6.8 percent as a percentage of GDP in 2007-08 and is expected to get even bigger in 2008-09 as the government implements its countercyclical fiscal stimulus.

Egypt's fiscal profile weaknesses not only include the high budget deficit and large public debt ratios but also budget rigidities. The three main elements of fiscal budget rigidity are expenditures related to subsidies, interest payments and public sector wages. Egypt's budget rigidities constrain efforts to improve infrastructure, health and education — the key sectors that lead to improved human capital. The current global financial crisis along with limited budget space pose a serious challenge to Egypt's macroeconomic stability and overall competitiveness. Egypt's macroeconomic instability and its implications will be discussed in depth in Chapter 2 of this report.

Similarly, a comparison of Egypt's national saving rates as a percentage of GDP to the MENA region average for both 2006 and 2007, reveals that Egypt's rates are more than 13 percent lower than the region's average. The top ranked country in the last two GCI's was Kuwait with an average rate of savings of 66 percent of GDP as shown in Table 1.4 below.

Table 1.4: ***National Savings Rate as a Percentage of GDP and Rankings for MENA Countries (GCI 2007-08 and GCI 2008-09)****

Country	Rank out of 131 (GCI 2007-2008)	Rank out of 134 (GCI 2008-2009)	National savings rate as a percentage of GDP (2006)	National savings rate as a percentage of GDP (2007)
Kuwait	1	1	65.2	67.5
Qatar	2	3	59.2	57.9
Algeria	4	4	56.5	53.7
Saudi Arabia	10	10	46.7	44.3
Libya	9	12	47.9	43.9
United Arab Emirates	19	14	37	40.4
Oman	51	26	24.8	30.8
Bahrain	22	30	35.2	29.9
Morocco	56	50	24.3	25.6
Syria	49	63	25.5	23.3
Israel	69	65	21.7	23
Tunisia	70	67	21.5	22.2
Egypt	71	70	21.3	21.5
Turkey	53	71	24.5	21.4
Jordan	85	115	18	12.5
Average national savings rate as a percentage of GDP for MENA			35.3	34.5

Source: WEF 2007 and WEF 2008.

** Rankings are based on data from the previous year*

It is worth noting that the rate of Egypt's gross savings as a percentage of GDP is lower than other emerging economies such as Malaysia, Korea, India and Indonesia (as reflected in Table 1.5).

Table 1.5: *Gross Savings as a Percentage of GDP for Select Emerging Economies*

	2000	2001	2002	2003	2004	2005	2006	2007
Egypt	19	18	20	19	20	21	22	24
Brazil	14	14	15	16	19	16	17	22
Indonesia	28	28	26	30	25	26	28	26
India	25	26	27	28	32	34	35	37
Korea	34	31	30	32	34	32	30	30
Malaysia	37	32	32	34	31	30	32	36

Source: World Development Indicators online database 2008.

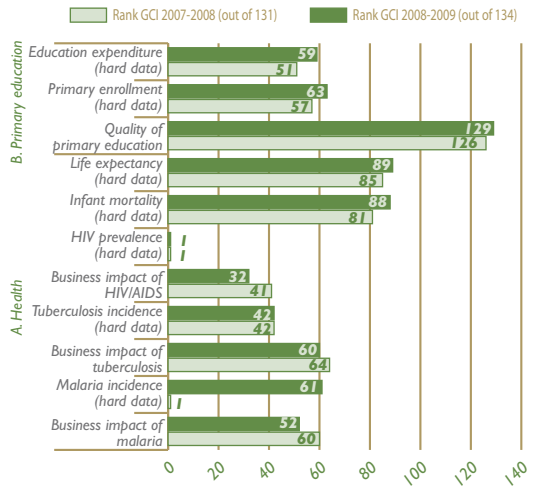
Pillar 4: Health and Primary Education

Egypt's overall score in health and primary education fell by 4 percent between 2007-08 and 2008-09. This led to a decline in Egypt's rank relative to other countries by five places from 83 out of 131 to 88 out of 134. The deterioration in health exceeded that of primary education.

The key factors that led to the nine-place decline of Egypt's health ranking were increases in malaria incidence (0.1 per 100,000 persons, 2003), infant mortality (28 per 1,000 live births in 2005), and life expectancy (68 years, 2006). Figure 1.9 illustrates how Egypt's ranking for malaria incidence fell from 1 out of 131 countries to 61 out of 134 countries. This is due to the fact that according to data used in the Global Competitiveness Report 2007-08, Egypt had no incidences of malaria, whereas (0.1 per 100,000 persons) incidence was reported in the Global Competitiveness Report of 2008-09. A drawback of the WEF reports is the occasional inconsistency of data reported or the change in sources. The 2007-08 report used hard data for malaria incidence dating back to 2004, while controversially the Global Competitiveness Report of 2008-09 used hard data for malaria incidence dating back to 2003. Similarly, Egypt's rank in business impact of malaria improved from 60 out of 131 countries to 52 out of 134 countries. This indicator comes from the responses of the EOS where executives are asked how serious they consider the impact of malaria on their company in the next five years (score range from one indicating extremely serious and seven implying it is not a problem). Egypt's score was 6.5 in 2008-09, higher than the mean of 5.8.

The GCR 2008-09 identifies the key health competitive advantages for Egypt as the low incidence of HIV/AIDS (< 0.1 percent of adults aged 15-49 years in 2007) and the low incidence of tuberculosis (24 per 100,000 persons, 2006). Figure 1.9 shows that Egypt ranked first in HIV prevalence due to extremely low incidence estimated to be less than 1 percent in the general population in 2007.

FIGURE 1.9: *EGYPT'S RANKING ON THE COMPONENTS OF THE HEALTH AND PRIMARY EDUCATION PILLAR IN 2007-08 & 2008-09*



Source: WEF 2008.

According to the Ministry of Economic Development report, "Egypt Achieving the Millennium Development Goals: a Midpoint Assessment," June 2008, infant and under 5 mortality declined by almost 50 percent between 1990 and 2006. Moreover, there is noticeable progress in measles immunization. However, disparities in infant and child mortality by region, social class and gender remain a key challenge. The maternal mortality ratio declined by 66 percent from 174 maternal deaths per 100,000 live births in 1992 to 84 maternal deaths per 100,000 live births in 2000. Egypt has already succeeded in achieving the Millennium Development Goal (MDG) related to improved maternal health.

Moreover, Egypt has succeeded in controlling malaria, and tuberculosis and schistosomiasis are regressing. However, hepatitis B and C constitute major health threats. They are the leading causes of severe liver damage, hepatocellular carcinoma and death in Egypt. The Ministry of Health and Population carries a heavy burden in providing free health services. It plans to reform the health insurance system as part of a nationwide health care reform strategy with the objective of achieving universal coverage for all Egyptians by 2012. Investments in health services totaled LE 4.7 billion during 2007-08 of which 60 percent was public[4].

For primary education, Egypt's ranking worsened largely due to perceived low quality of education (from 126 out of 131 countries to 129 out of 134

[4] Data from Ministry of State for Economic Development.

countries). The quality of primary education is assessed from the EOS where executives are asked to give a score from one to seven describing the quality of primary schools in the country with one implying poor quality and seven indicating the quality of education in the country is among the best in the world. Egypt's score for quality of education was very low at 2.1 in 2008-09. The highest score for perceived quality of education was for Finland at 6.7.

In 2004, Egypt participated for the first time in the Trends in International Mathematics and Science Study (TIMSS) for 8th grade[5], providing an opportunity to compare Egypt's educational achievement with other countries. Egypt scored an average of 406 in math and 421 in science, which placed Egypt's 8th graders below international averages (467 and 474 respectively). Similarly, the low quality of primary education was pinpointed as one of the key challenges to Egypt's improved educational outcomes as per the World Bank, MENA Development Report "The Road Not Traveled."[6]

Egypt's ranking in terms of education expenditure declined from 51 out of 131 countries to 59 out of 134. It is worth noting, however, that Egypt's expenditure on education as a percentage of Gross National Income (GNI) in 2006 (4.4 percent) was higher than Kuwait (4.2 percent), Oman (3.7 percent), Turkey (3.5 percent), Syria (2.6 percent) and Mauritania (2.4 percent). Similarly, net primary enrollment in Egypt was 93.9 percent in 2006, higher than many MENA countries with the exception of Bahrain (98.2 percent), Israel (96.9 percent), Tunisia (96.1 percent), Algeria (95.2 percent) and Syria (94.5 percent).

Although Egypt spends a comparatively high proportion of its resources on education, this high expenditure is inefficient and to some extent inequitably allotted. The key inefficiencies include overstaffing, inefficiency of teacher hiring and deployment, which impairs school quality; wasteful and inefficient textbook spending; and the inability to analyze budget data at the school level (public schools).[7] Improvements in equity and quality have to be secured via improved efficiencies; that is, it is not the level of investment that needs to be changed but the nature of investment that requires adjustments. Major inefficiencies include high levels of non-teaching staff, low pay for teachers, low performance-related incentives, difficulty implementing innovative pedagogy, a highly centralized system and low levels of school-based management.[8] Also, targeting inequality is a priority for improvement of Egypt's educational outcomes as the two lowest income quintiles suffer from limited access to and poor quality of education.

In 2007-08, Egypt ranked 116 out of 179 countries in the Human Development Index, lagging behind all MENA countries with the exception of Morocco, Yemen, Mauritania and Sudan. Egypt's low rank was mainly attributed to its low score in the education index of 0.731.[9]

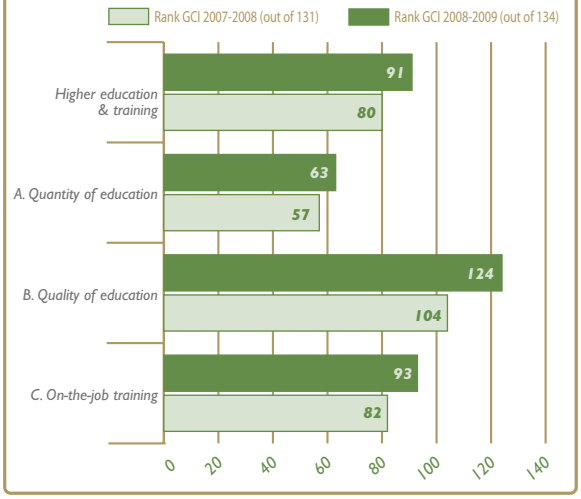
B. Efficiency Enhancers

The six pillars falling under the efficiency enhancers index are higher education and training, goods market efficiency, labor market efficiency, financial market sophistication, technological readiness and market size. These six pillars represent 35 percent of Egypt's GCI.

Pillar 5: Higher Education and Training

Egypt's rank in higher education and training fell considerably from 80 out of 131 to 91 out of 134. The higher education and training pillar can be subgrouped into three components: the quantity of education, the quality of education and on-the-job training. Figure 1.10 shows how Egypt's rank fell in the three components. However, the most challenging factors are the quality of education and on-the-job training. One of the key factors contributing to the number one ranking of the United States in the GCI 2008-09 was its excellent university system with its strong collaboration with the business sector in R&D.

FIGURE 1.10: *EGYPT'S RANKING ON THE COMPONENTS OF THE HIGHER EDUCATION & TRAINING PILLAR IN 2007-08 & 2008-09*



Source: WEF 2008.

[5] The World Bank Education Sector Policy Note (2007): "Improving Quality, Equality and Efficiency in the Education Sector: Fostering a Competent Generation of Youth."

[6] The World Bank MENA Development Report (2008): "The Road Not Traveled: Education Reform in the Middle East and North Africa".

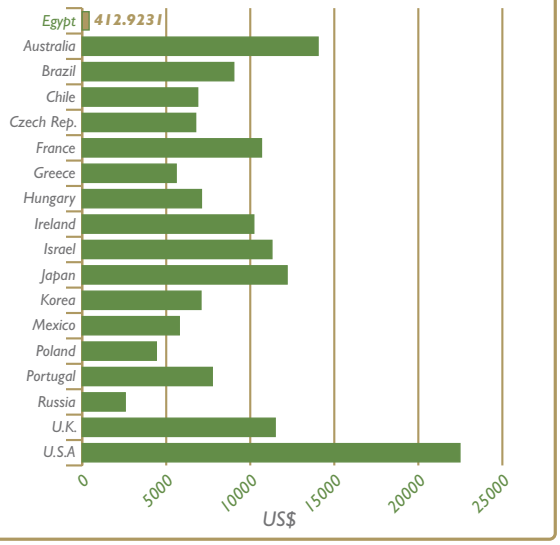
[7] The World Bank Policy Note 2 (July, 2005): "Making Egyptian Education Spending More Effective."

[8] World Bank 2007.

[9] Iceland obtained the highest score in the education index of 0.98 in 2007/08. Source: Human Development Report 2007-08.

Between 1998 and 2006, the budget expenditure on education increased by 89 percent in nominal terms.[10] The rate of budgeted expenditure increase for education surpassed that of change in enrollment and gross spending per student and appeared to improve by 40 percent over this period. Adjusted for inflation, the budgeted expenditure for education increased by 24 percent during the period 1998-2006, but expenditure per student fell by almost 8 percent. Looking at the per student expenditure, as a proxy indicator of the quality of higher education, Egypt averages US $ 413 per student after adjusting for inflation. This is very low as compared to the university expenditure per student in countries where education quality is high such as the United States, United Kingdom, Australia or France as shown in Figure 1.11 below.

FIGURE 1.11: *UNIVERSITY EDUCATION: EXPENDITURE PER STUDENT (2004 CONSTANT PRICES, $USD)*



Source: Lewis, Andrew (2008). Higher Education Competitiveness: Achieving Better Quality and Better Equity. Toward Competitiveness. November.

In 2006, the secondary enrollment rate stood at 87.8 percent, whereas the gross tertiary education enrollment rate was 34.7 percent. The government's five year plan 2007-2012 aims to increase enrollment rates, increase the number of schools and reduce class density.

Yet the quality of education is a key impediment to increasing Egypt's competitiveness. The factors where Egypt performed poorly compared to other countries include the quality of the educational system, the quality of math and science education, the quality of management schools and Internet access in schools. The educational system score for Egypt was 2.4, below the mean of 3.7. By far, it is the lowest of all MENA countries. The same goes for the quality of math and science education, where Egypt's score is again below the mean at 2.6. The perception of the quality of management schools score was 3.2 in 2008-2009, below the mean of 4.1 and lower than many MENA countries with the exception of Algeria (3.1), Libya (2.6) and Mauritania (2.5). Access to the Internet in schools is perceived to be low, reflecting the need for Egypt to speed up the process for creating smart schools. The Egyptian Education Initiative (EEI) launched by the government comprises four tracks: pre-university, higher education, life learning and Information, Communication and Technology (ICT) industry development. One of the key objectives of the initiative is to ensure that all preparatory schools get connected to broadband by 2012 and that teachers are trained on integrating ICT into their curricula.

The low quality of the educational system and the low quality of math and science education as reflected by EOS scores match with the findings of the 2007 World Bank "Education Sector Policy Note."[11] The key finding of the report is that while progress has been made in providing more educational opportunities to Egyptians, the quality of education remains low and unequally distributed, leading to a discrepancy in educational outcomes. Inequality of educational outcomes is particularly acute for the two lowest income quintiles, which adversely affects their labor market opportunities. The key factors that need to be addressed are the outdated curriculum and high-stakes tests that do not teach or measure skills needed by the labor market; the two track system which is based on those tests, namely general education and Technical and Vocational Education and Training (TVET); and the low incentive environment (low teachers pay, poor accountability and the pervasive prevalence of private tutoring).

Also, the Egypt Education Sector Policy Note stated that private rates of return on education in general are low (Table 1.6), and the returns for vocational secondary graduates are not only low, but falling (Table 1.7). Also, vocational graduates are far more likely to be in the informal sector for their first job. This is alarming, considering that 60 percent of students enrolled in secondary education are tracked into TVET secondary schools.

[10] Lewis, Andrew (2008). "Higher Education Competitiveness: Achieving Better Quality and Better Equity." ENCC Policy Note. November.

[11] The World Bank Education Sector Policy Note (2007). "Improving quality, Equality and Efficiency in the Education Sector: Fostering a Competent Generation of Youth."

Table 1.6: *Private Rate of Return* on Education in Egypt 1995-2000.*

	1995-1996	1999-2000
Basic education	-3.39	-0.11
Secondary	-0.67	2
University and above	7.1	8

**The private rate of return on education:* is the rate of discount that equates the present value of costs and benefits from investing in education.
Source: El Baradei, Mona (2003). "The Private Rate of Return to Education, Educational Inequalities and Poverty in Egypt". Research Papers Series, Economics Department, Faculty of Economics and Political Sciences. Cairo University.

Table 1.7: *The Return for Vocational Secondary Education.*

	1988	1998	2006
Vocational secondary education	0.085	0.048	0.047

Source: Said, Mona (2006). "The Fall and Rise of Earnings and Inequality in Egypt: New Evidence from the ELMPS, 2006." Economic Research Forum. Cairo.

The best performer in terms of the quality of the educational system was Finland with a score of 6.2 and the lowest was Paraguay with a score of 2. As for the quality of math and science education, the mean score for Egypt was 4.1, the best performer (Finland) obtained a score of 6.5 and worst performer (Timor-Leste) obtained a score of 2. Table 1.8 shows Egypt's score vis-à-vis the best and worst performers in selected indicators for 2008-09. The quality of management schools mean score was 4.1, and the best perceived management schools were those of France at 6.1, while the worst was Timor-Leste at 2. Again Finland was the best country in terms of perceived Internet access in schools with a score of 6.4 and the worst was Paraguay with a score of 1.5.

Table 1.8: *Selected Education Indicators in Comparison 2008-09.*

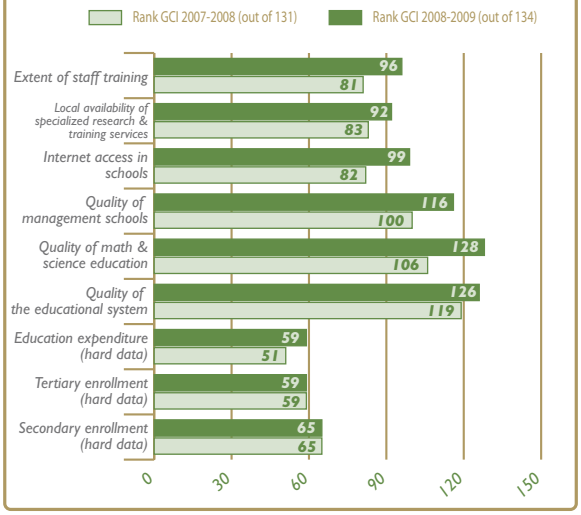
	Quality of education	Quality of math and science education	Quality of management schools	Internet access in schools
Top performer (name, score and rank out of 134)	Finland, 6.2, (1)	Finland, 6.5, (1)	France, 6.1, (1)	Finland, 6.4, (1)
Worst Performer (name, score and rank out of 134)	Paraguay, 2, (134)	Timor-Leste, 2, (134)	Timor-Leste, 2, (134)	Paraguay, 1.5, (134)
Egypt (score and rank out of 134)	2.4, (126)	2.6, (128)	3.2, (116)	2.5, (99)
Mean score for all 134 countries	3.7	4.1	4.1	3.6

Source: WEF 2008.

The on-the-job training rank deteriorated substantially from 83 out of 131 countries to 92 out of 134 countries. The extent of staff training is a matter that requires special attention and focus from policy makers especially since Egypt ranked last out of 134 in labor market efficiency.

The best country in terms of staff training was Denmark with a score of 5.9 and the worst was Chad with a score of 2.5. Egypt's score for staff training was 3.5, below the mean score for all 134 countries of 4. Figure 1.12 shows that Egypt's ranking on the various indicators of the higher education and training pillar fell or stayed constant.

FIGURE 1.12: *EGYPT'S RANKING ON THE VARIOUS INDICATORS OF THE HIGHER EDUCATION & TRAINING PILLAR IN 2007-08 & 2008-09*

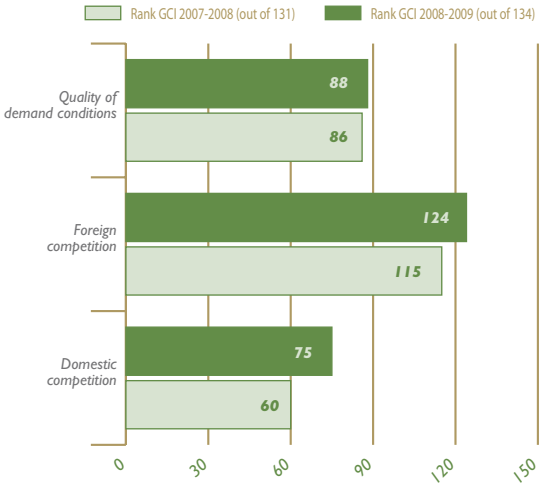


Source: WEF 2008.

Pillar 6: Goods Market Efficiency

Egypt's overall score for goods market efficiency did not change much, but its ranking in this pillar fell considerably due to faster improvements in other countries. Egypt's rank fell from 76 out of 131 countries to 87 out of 134 countries. As shown in Figure 1.13, Egypt's rankings in the three key components of the goods market efficiency (quality of demand conditions, foreign competition and domestic competition) deteriorated in 2008-09 as compared to 2007-08. Egypt's key relative advantages in goods market efficiency are in the extent and effect of taxation, the number of procedures required to start a business (seven procedures) and time required to start a business (nine days in 2007). [12]

FIGURE 1.13: *EGYPT'S RANKING ON THE COMPONENTS OF THE GOODS MARKET EFFICIENCY PILLAR IN 2007-08 & 2008-09*



Source: WEF 2008.

According to the World Bank "Doing Business 2009" Egypt's rank improved from 125 out of 178 countries in 2008 to 114 out of 181 countries in 2009. Egypt's rank improved in terms of starting a business[13] from 55 in 2008 to 41 in 2009. The number of procedures required to start a business improved to six in 2009 below the MENA region's average of 8.4. Similarly, the time required to start a business decreased to seven days in 2009 as compared to nine days in 2008, again much lower than the MENA region's average of 23.5 days.

Areas where Egypt lags far behind other countries include buyer sophistication, agricultural policy costs and foreign competition. In terms of buyer sophistication, Egypt ranked 130 out of 134 with a score of 2.4, lower than the mean of 3.7 in 2008-09, signaling that buyers in the country make purchasing decisions solely taking into account the lowest price, with little regard to quality or other factors. Agricultural policy costs are perceived to be burdensome for the economy. Egypt's score in the EOS was 3.6 lower than the mean for all countries of 4. The best performer, New Zealand, scored 5.8 reflecting that agricultural policy costs tend to balance the interests of taxpayers, consumers and producers.

[12] Source: WEF 2008 (obtained from The World Bank, "Doing Business 2008").

[13] Starting a business rank takes into account the procedures and costs associated with setting up a business in Egypt

Egypt's score on effectiveness of anti-monopoly policy stood at 3.3, below the mean of 4. The highest score of 6 was obtained by the Netherlands and Germany. Egypt's score reflects the need to exert more effort to improve the effectiveness of anti-monopoly policies and to promote competition. Efforts by the Consumer Protection Agency (CPA) and Egypt Competition Authority (ECA) to support consumers' rights have yet to bear fruit.

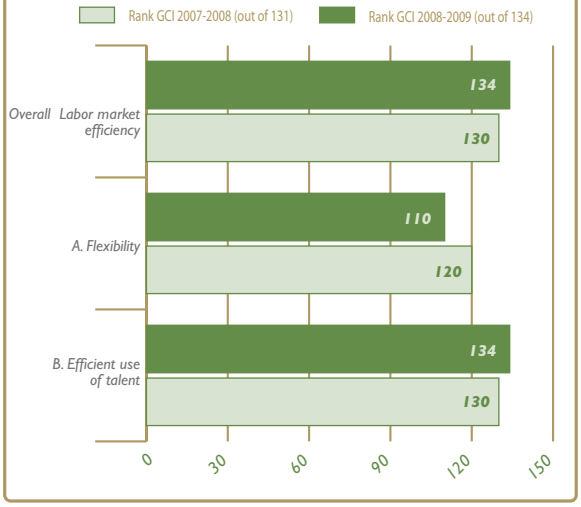
The CPA is working on its major milestone objective, namely the dissemination of awareness regarding consumer protection law and its enforcement to help consumers learn about their rights and obligations, while strengthening the role of consumer protection NGOs. The CPA's activities to date have included acceding to the International Consumer Protection and Enforcement Network (ICPEN) in 2007; approving the consumer rights code of honor; conducting training workshops for consumer protection NGOs; launching the first national CPA program about deceptive advertising in June 2008; establishing a hotline service to receive consumers' complaints;[14] and filing consumer complaints through the Egyptian National Postal Service and website. To date, the CPA has received more than 40,000 calls of which 3,500 where complaints. The resolution rate was around 81 percent of the total number of complaints.

The ECA was established a few months after the Anti-Monopoly and Fair Competition Act was approved by the parliament (Law 3 of 2005). The act bans monopolistic practices, and promotes competition and a healthy business environment. In January 2005, the Egyptian parliament approved an antitrust bill that does not focus on preventing monopolies per se, but on curtailing international monopolistic practices such as lowering prices or supply to the detriment of smaller competitors. According to the law, a company holding 25 percent or more market share may be subject to investigation if suspected of illegal or unfair market prices. Penalties on companies found to have engaged in monopolistic practices range from LE 100,000 to LE 300 million. Penalties are doubled for reoccurring violations. The ECA, which implements the law, is an independent body reporting to the prime minister and funded by direct government appropriations or donations from professional or academic bodies.

Pillar 7: Labor Market Efficiency

This pillar is composed of 10 indicators that are subgrouped under two key components: labor flexibility and efficient use of talent. Figure 1.14 illustrates Egypt's overall ranking in labor market efficiency along with its ranking in its two components in 2007-08 and 2008-09.

FIGURE 1.14: *EGYPT'S OVERALL RANKING IN THE LABOR MARKET EFFICIENCY PILLAR AND ITS RANKING IN ITS TWO COMPONENTS IN 2007-08 & 2008-09*



Source: WEF 2008.

Egypt ranks below all other countries on this pillar. Its rank fell to 134 of 134 in GCI 2008-09 from 130 of 131 in GCI 2007-08. The labor market suffers from several structural imbalances that explain this poor rank. Nevertheless, one has to be careful in interpreting the various indicators of this pillar since Egypt's labor market – like other highly populated developing countries – is characterized by a duality of formal and informal labor markets. The formal labor market has clear contractual obligations and rights between the employees and employer. Employees have all the benefits as per the labor law such as the number of working hours, vacations, medical care and insurance coverage. Informal employment, on the other hand, is not regulated and is not documented, making it impossible to quantify precisely the number of employees. Informal employees have no legal rights. Estimates for 2007 show that formal employment represents 51.3 percent as compared to informal employment of 47.7 percent.[15]

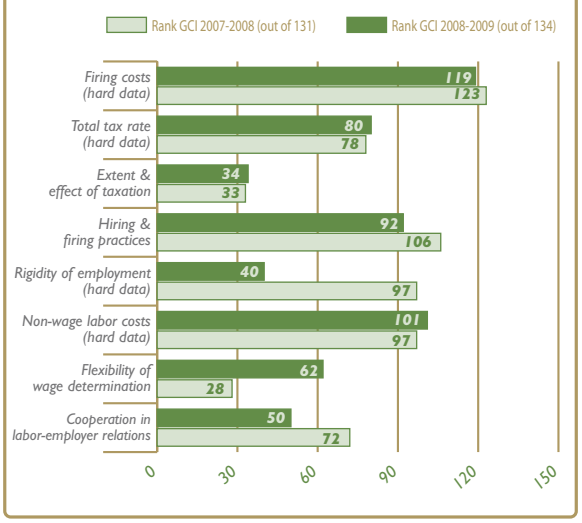
Under the flexibility component, Egypt has three areas of relative competitive advantages vis-à-vis other countries. Those are cooperation in labor-employer relations, where Egypt ranked 50th out of 134 countries, implying that labor-employer relations tend to be cooperative; rigidity of employment, where Egypt ranked 40th and obtained a score of 27 of a scale of 0-100, with 100 being the worst[16]; and the extent and effect of taxation, where Egypt ranked 34th (Figure 1.15).

[14] Currently available in the governorates of Cairo, Giza and Qalyubeya.

[15] CAPMAS, Labor Sample Survey for 2007 – June 2008.

[16] WEF data for the rigidity of employment from the World Bank's "Doing Business 2008."

FIGURE 1.15: *EGYPT'S RANKING IN THE INDICATORS REFLECTING LABOR MARKET FLEXIBILITY IN 2007-08 & 2008-09*



Source: WEF 2008.

Egypt's performance in the rigidity of employment improved significantly from last year. The improvement could be a result of the Labor Law No.12 in 2003, which allowed for greater flexibility in working hours, permitted fixed duration contracts and facilitated the firing process.

Areas where Egypt is far behind other countries in the labor market include: non-wage labor costs, 101[17]; hiring and firing practices, 92[18]; and firing costs, 119. The firing costs in weeks of wages mounted to 132 weeks in 2007[19] and remained at this high level in 2008,[20] much higher than the MENA average of 53.6. The extremely high firing costs are a strong disincentive for businesses to employ full-time workers.

Taking into account the duality in the labor market, Egypt's indicators for rigidity of employment, the hiring and firing practices, and wage flexibility do not reflect the existence of the informal labor market, which is characterized by total flexibility in hiring and firing labor, and great flexibility in setting salaries given the high unemployment rate. As for the formal labor market, the labor market law (Law 12 of 2003) that governs the relation between the employer and the employee in the formal private sector is also characterized by a great extent of flexibility in comparison to the previous law. The employer can use short-term contracts and partially or totally terminate employment contracts in cases of force majeure or negative economic circumstances (such as the current financial crisis). In such cases, the emergency fund is responsible for providing a subsidy for laid off workers.

In terms of efficient use of talent, Egypt is unquestionably the least competitive, ranked last out of 134 countries. Egypt's ranking dropped across all four key factors that are taken into consideration when looking at this sub-pillar:

1. **Pay and productivity:** Egypt's score in the EOS 2008 was 3.5, much lower than the mean of all 134 countries of 4.2 (score from 1 to 7, where 1 implies that pay is not related to worker productivity, and 7 implying that pay is strongly related to worker productivity). Studies like that of El-Essawy, Ibrahim 2002 and El-Ehwany, Naglaa 2008 found that pay and productivity were not strongly related. During the period 1995-2000, despite the fact that real wages were low in general, the real wage growth rate was 5.6 percent, surpassing that of real productivity of 1.7 percent.[21] Similarly, during the period 2000-2006, the real wage growth rate was 5.8 percent, higher than the real productivity growth rate of 2.3 percent.[22]

   Prerequisites to raising productivity include improving the quality of education, adopting a clear and well targeted training strategy, ameliorating the working environment and ethics.

2. ***Reliance on professional management:*** Executives were asked about whether senior management positions in Egypt are usually held by relatives or friends without regard to merit (score=1), or mostly held by professional managers chosen for their qualifications (score=7), Egypt EOS score was 3.5 much lower than the mean of 4.6 and the lowest of all MENA countries.

3. ***Brain drain:*** The EOS score for Egypt is 2.1, again much lower than the mean score for all countries, where 1= talented people tend to normally leave the country to pursue opportunities and 7= talented people tend to stay in country. Egypt ranked 129th out of 134 in the brain drain indicator, by far the worst country in the MENA region.

4. ***Female participation in labor force:*** The ratio of female to male participation in the labor force is very low at 0.3 as of 2006.[23] In terms of this indicator, Egypt ranked 133rd out of 134 countries, above only Saudi Arabia. The best performers in this indicator are Mozambique, Burundi, Serbia, Tanzania, Malawi and Cambodia with a female participation ratio of 1 as of 2006. It is note worthy, however, that the official figures reported for female participation in the labor force as a percentage of male participa-

[17] Egypt's non-wage labor costs are 25 percent of salary. The variable estimates social security payments and payroll taxes associated with hiring an employee in 2006 expressed as a percentage of workers' salary.

[18] Egypt obtained a score of 3.5 in the EOS indicator of hiring and firing practices below the mean of 3.8 (scores range from 1 to 7) where 1 implies that hiring and firing of workers is impeded by regulations, and 7 means that hiring and firing of workers is flexible as determined by employers.

[19] WEF 2008 data source the World Bank's "Doing Business 2008."

[20] World Bank "Doing Business 2009."

[21] El-Essawy, Ibrahim. 2002. "Egyptian Economy in 30 years." Academic Library.

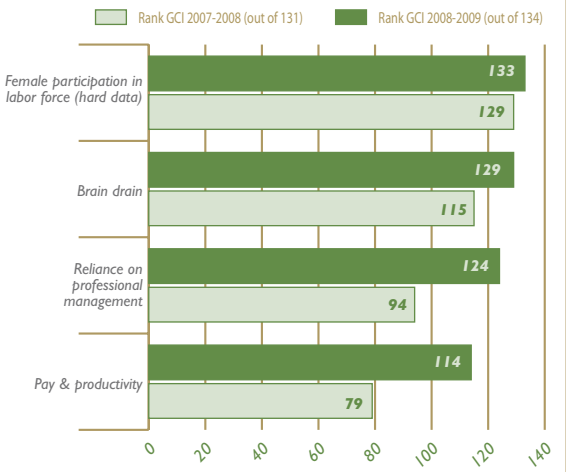
[22] El-Ehwany, Nagla. 2008. "Current Imbalances in Egyptian Labor Market and the Potential Impact of Global Economic Crisis." Presentation at the ENCC Media Awareness Campaign. Ein-El Sokhna, Egypt. March 12, 2009.

[23] WEF 2008

tion do not take into account the female participation in agricultural activities and the informal sector, where recent studies estimate female participation to be around 50 percent of total labor in both segments.

Figure 1.16 shows Egypt's ranking in the four indicators leading to Egypt's poor ranking in efficient use of talent.

FIGURE 1.16: *EGYPT'S RANKING IN THE INDICATORS REFLECTING EFFICIENT USE OF TALENT IN 2007-08 & 2008-09*

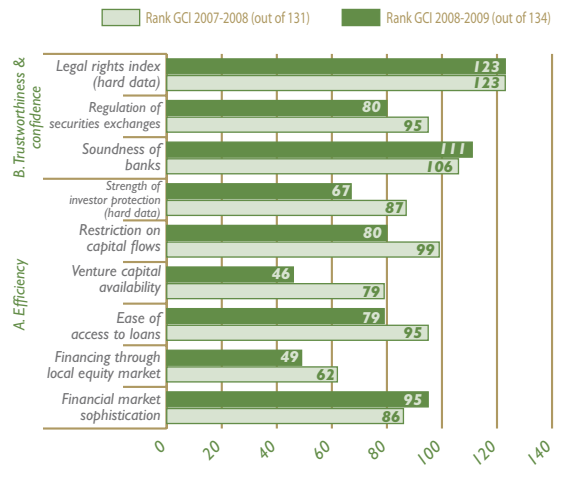


Source: WEF 2008.

Pillar 8: Financial Market Sophistication

Egypt ranked 106 out of 134 countries in 2008-09 in terms of financial market sophistication. The key sub-components of this pillar are financial market efficiency, and trustworthiness and confidence. In terms of financial market efficiency, Egypt ranked 72nd out of 134 countries, but its rank in terms of trustworthiness and confidence in the financial market declined to 126 out of 134 countries. As shown in figure 1.17, areas where improvement occurred under the financial market sophistication pillar include regulation of securities exchanges, venture capital availability and strength of investor protection. Financing through local equity market was a relative advantage for Egypt where it ranked 49th out of 134 countries.

FIGURE 1.17: *EGYPT'S RANKING ON THE FINANCIAL MARKET SOPHISTICATION PILLAR INDICATORS IN 2007-08 & 2008-09*



Source: WEF 2008.

In September 2008, the New York Stock Exchange in collaboration with the Africa Investor Organization awarded the Egyptian Stock Exchange "the most innovative African stock exchange."

The low ranking in trustworthiness and confidence in the financial market was a result of Egypt's poor ranking in the legal rights index (123 out of 134) and in the soundness of banks (111 out of 134 countries). According to the World Bank "Doing Business 2008" Egypt obtained a score of 1 in the strength of legal rights index (0-10). Egypt's score improved in "Doing Business 2009" to 3, yet remained slightly lower than MENA region's average of 3.3.

It is worth mentioning that in the last four years Egypt pursued banking reforms focusing on encouraging mergers and acquisitions, restructuring state-owned banks, addressing the problem of non-performing loans, and developing the regulatory and supervisory role of the CBE. Significant progress has been achieved in divestiture of public ownership in banks and in consolidation of the banking system, such that the number of banks decreased from 57 in 2004 to 33 in 2008. In 2006, the government sold its majority stake in Bank of Alexandria, one of the four main state-owned banks. In 2007, the government announced that Banque du Caire, another state-owned bank, was for sale. In June 2008, the auction of up to 67 percent of its shares was cancelled, however, as bids were determined to be too low to justify the sale.

The impact of the global financial turbulence on the Egyptian banking system has been limited so far. The equity market, however, has suffered great volatility and, like other emerging markets, dropped sharply in 2008 by 31.7 percent. The decline in the equity market started in May 2008, well before the financial crisis, when the government tried to reduce the impact of high inflation rates on those with low wages by declaring salary raises of 30 percent to employees in the public sector.[24] To finance such increases from real resources, among other measures,[25] taxes on treasury bills were imposed and low electricity and gas prices for energy intensive companies in free zones were abolished. The decline in the stock market was further exacerbated by the global financial crisis.

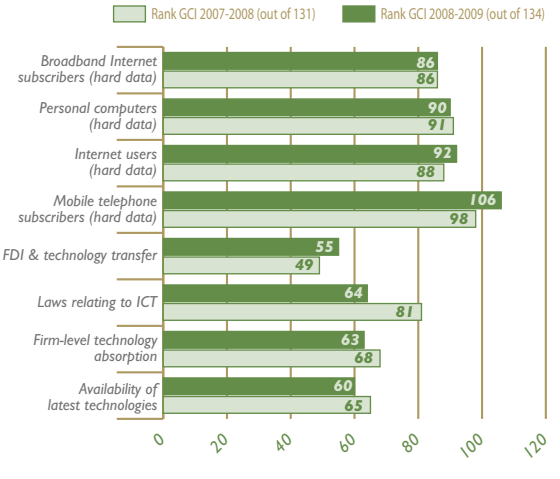
The recently introduced law no.10/2009 regulating control over non-banking financial markets and instruments aims to establish an authority for non-banking financial control instead of having several separate institutions namely; the Capital Market Authority, the Egyptian Insurance Supervisory Authority, and the Mortgage Finance Authority. The new authority will, among other things, supervise and control capital markets, insurance, real estate business, financial leasing and factoring.

Pillar 9: Technological Readiness

The technological readiness score measures the agility with which an economy adopts existing technologies to enhance the productivity of its industries. ICT access and usage are included in this pillar as essential components of an economy's overall level of technological readiness. Whether the technology used has been developed within the country is irrelevant in this respect. What matters is access to advanced products and blueprints, and the ability to use them.

Egypt's technological readiness rank improved from 87 out of 131 countries to 84 out of 134 countries in 2008-09. As shown in figure 1.18, areas where improvements occurred include laws relating to ICT, firm-level technology absorption, availability of latest technologies and personal computers.

FIGURE 1.18: *EGYPT'S RANKING ON THE TECHNOLOGICAL READINESS PILLAR INDICATORS IN 2007-08 & 2008-09*



Source: WEF 2008.

Areas where Egypt lost some positions relative to other countries despite improvements in hard numbers include mobile telephone subscribers (23.9 mobile subscribers per 100 population in 2006)[26] and Internet users (8 per 100 population in 2006) signaling that other countries are improving in those indicators at a greater speed. Also, the data used in the WEF report is not the latest available, hence not reflecting the recent boom in mobile, Internet, telephone and PC usage.

According to the Ministry of Communications and Information Technology, the number of mobile subscribers grew considerably to 35.1 million in June 2008. Similarly, Internet penetration grew to 15 percent by June 2008. Egypt's ICT policy aims to increase the number of households with a broadband Internet connection to 1.5 million and to raise the mobile penetration rate to 70 percent by the end of 2011.

The WEF Networked Readiness Index (NRI) 2007-08, which measures the propensity for countries to exploit the opportunities offered by information and communications technology, reflects a better position for Egypt. The NRI is a composite of three components: the environment for ICT, the readiness of the community's key stakeholders to use ICT and the usage of ICT among stakeholders. Egypt ranked 63rd out of 127 countries in the NRI 2007-08 rankings. Egypt's ranking came after several MENA countries, namely, Israel (18), UAE (29), Tunisia (35), Bahrain (45), Jordan (47), Saudi Arabia (48), Kuwait (52) and Oman (53).

[24] In May 2008, President Mubarak announced an increase of 30 percent in the basic pay for all government employees. In addition, an adjustment to the minimum incentives payments of local government employees (3.4 million employees) was enacted to raise the minimum salary of the lowest paid government employees. Monthly pensions were also increased by 20 percent (to a maximum of EGP 100) and distributions of rice, sugar and edible oil through the ration card system were expanded. The government relaxed eligibility rules for ration cards, which resulted in an additional 15 million new potential beneficiaries. This was the first time that new cardholders were added to the ration card registry since 1988.

[25] Cost-cutting measures introduced in May 2008 included partially scaling back energy subsidies by LE 7.5 billion, increasing sales taxes on cigarettes, raising fees on vehicle licenses, raising fees on cement quarries, and eliminating some income tax exemptions. The elimination of tax exemptions covers: interest on T–bills, profits of educational institutions, and profits of energy intensive Free Zone companies including those producing fertilizers, petrochemicals, steel, and liquid natural gas (LNG) manufacturing, liquefaction and transportation.

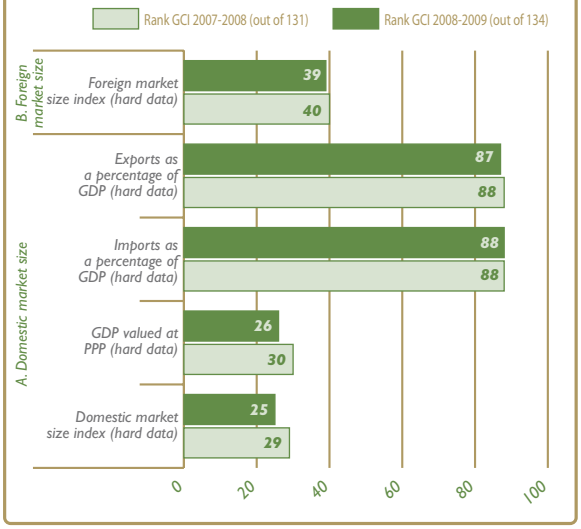
[26] WEF 2008.

Noteworthy are Egypt's ICT related awards in 2008. Egypt won the annual award of the British National Outsourcing Association (NOA) as off-shoring destination of the year. Similarly, according to Global Services Tholons 2008 study, out of the top 50 emerging global outsourcing cities, Cairo ranked 7th.

Pillar 10: Market Size

Egypt has a relative competitive advantage in terms of both domestic and foreign market sizes (Figure 1.19). The largest increase was in Egypt's ranking in terms of domestic market size which improved from 29 out of 131 to 25 out of 134. Out of a scale from 1 (worst) to 7 (best), Egypt obtained a score of 4.5 in terms of domestic market size index and a score of 5 in the foreign market size index.

FIGURE 1.19: *EGYPT'S RANKING ON THE MARKET SIZE PILLAR IN 2007-08 & 2008-09*



Source: WEF 2008.

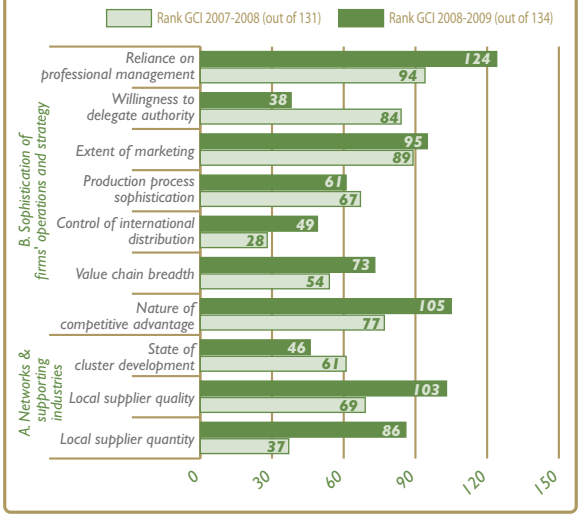
C. Innovation and Sophistication Index

As a factor-driven economy, the two pillars of business sophistication and innovation represent just 5 percent of Egypt's GCI score. The innovation and sophistication index measures investment in R&D, availability of high-quality scientific research institutions, extensive collaboration in research between universities and industry and the protection of intellectual property.

Pillar 11: Business Sophistication

Egypt's ranking in the business sophistication pillar dropped from 67 out of 131 countries to 77 out of 134 countries. Its score declined both in networks and supporting industries and sophistication of firms' operations and strategy. In terms of sophistication of firms' operations and strategy, Egypt's ranking decreased in terms of reliance on professional management from 94 out of 131 to 124 out of 134 indicating pervasive inadequate use of human resources. It also deteriorated in other factors such as the nature of competitive advantage and extent of marketing as shown in Figure 1.20. In terms of networks and supporting industries, Egypt's poor ranking stems mainly from its deterioration in ranking in both local supplier quality and quantity. Egypt's ranking in local supplier quality fell from 69 out of 131 in 2007-08 to 103 out of 134 countries in 2008-09. Similarly, its ranking in terms of local supplier quantity has dropped from 37 out of 131 countries in 2007-08 to 86 out of 134 countries in 2008-09.

FIGURE 1.20: *EGYPT'S RANKING ON THE BUSINESS SOPHISTICATION PILLAR INDICATORS IN 2007-08 & 2008-09*



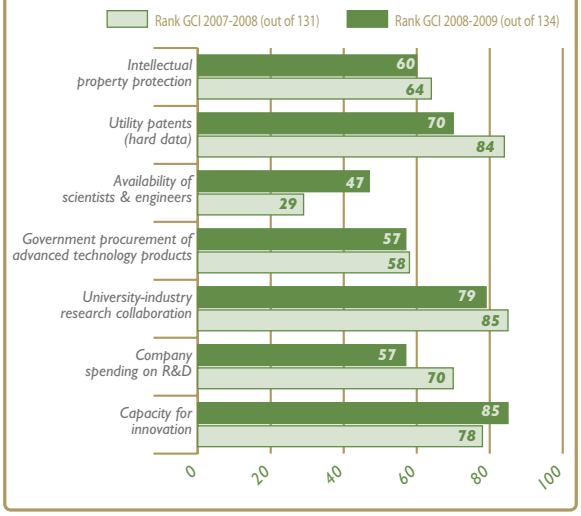
Source: WEF 2008.

Pillar 12: Innovation

Egypt's score and ranking in innovation remained stable at 67, though three additional countries were added. The seven factors that determine the innovation score are intellectual property protection, utility patents, availability of scientists and engineers, government procurement of advanced technology products, university-industry research collaboration, company spending on R&D and capacity for innovation.

The only relative advantage for the economy in this pillar is the availability of scientists and engineers, where Egypt ranked 47 out of 134 countries (Figure 1.21). Egypt scored 4.5, above the mean of 4.2, where 1= scientists and engineers are rare and 7 = scientists and engineers are widely available.

FIGURE 1.21: *EGYPT'S RANKING ON THE INNOVATION PILLAR INDICATORS IN 2007-08 & 2008-09*



Source: WEF 2008.

Egypt lags far behind other countries in terms of capacity for innovation and university-industry research. Egypt's score for capacity for innovation was 2.9,[27] below the mean of 3.4 in 2008-09. The top performer in capacity for innovation was Germany with a score of 6. Egypt's comes behind several countries in the region, namely Israel, Saudi Arabia, Tunisia, Oman, Turkey, Qatar, Jordan and UAE.

Egypt's university-industry research collaboration score is 3, again lower than the mean of all countries (3.4). The best performer in this indicator is the United States with a score of 5.8, reflecting strong collaboration between the business community and local universities.

One of the areas where Egypt made some improvement was company spending on research and development. Egypt's rank improved from 70 out of 131 countries in 2007-08 to 57 out of 134 countries in 2008-09. Yet, Egypt's score of 3.3 is still below the mean of all countries 3.4 in 2008-09, signaling Egypt's need to increase spending on R&D still further. Egypt's R&D expenditure as a percentage of GDP averaged 0.19 percent during the years 2000-2005, much lower than Israel, where the average expenditure on R&D was 4.46 percent and Tunisia where average R&D expenditure as a percentage of GDP was 0.6 percent during the same period.[28]

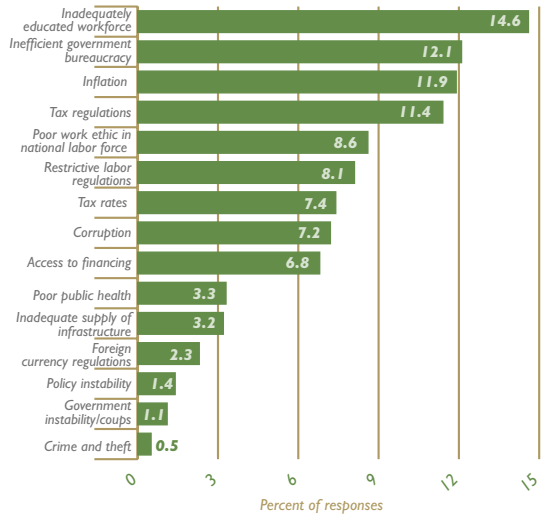
[27] Scores range from 1 to 7 with 1= companies obtain technology exclusively from licensing or imitating foreign companies and 7= companies obtain technology by conducting formal research and pioneering their own new products and processes.

[28] Human Development Report 2007-08.

1.3 THE MOST PROBLEMATIC FACTORS FOR DOING BUSINESS

According to EOS 2008, the most problematic factor for doing business in Egypt is the inadequately educated workforce. Figure 1.22 shows the most problematic factors for doing business. Several factors were related to the state of human capital development namely inadequately educated workforce, poor work ethic and poor health. Other factors that were problematic for doing business included restrictive labor regulations, tax regulations, inflation and inefficient government bureaucracy.

FIGURE 1.22: *THE MOST PROBLEMATIC FACTORS FOR DOING BUSINESS IN EOS 2008**

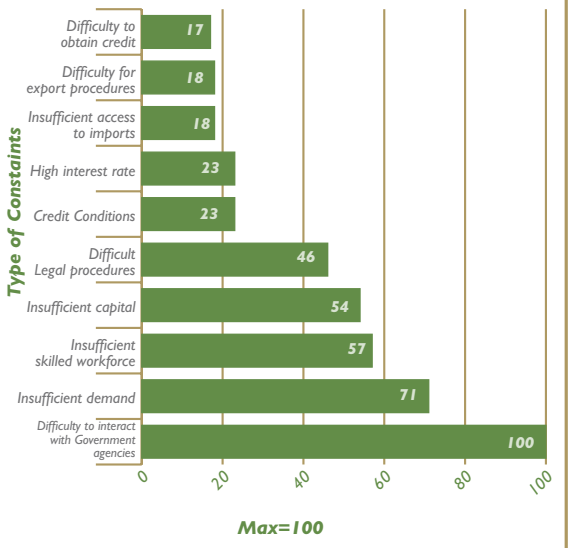


*From a list of 15 factors, respondents were asked to select the five most problematic for doing business in the country and to rank them

Source: WEF 2008.

Results of the Business Barometer conducted by the Egyptian Center for Economic Studies (ECES) (January, 2009) are somewhat similar to the WEF results concerning the major constraints facing businesses. According to the Business Barometer the major constraints are dealing with government bureaucracy, insufficient demand and insufficiently skilled workers. Businesses also expressed concern about insufficient access to capital and difficulty of legal procedures. Figure 1.23 illustrates constraints reported by firms as major factors affecting their performance.

FIGURE 1.23: *MAJOR CONSTRAINTS FIRMS FACE AS PER THE BUSINESS BAROMETER, JANUARY 2009*



Source: ECES Business Barometer survey results, January 2009, no.22.

1.4 CONCLUSION

What is holding Egypt back on competiveness? What is the best way forward?

Macroeconomic instability and low human development are major constraints hindering Egypt's development and achievement of greater competitiveness. In addition, many disparities and imbalances exist across Egypt's economy that are burdening the system. Urgent attention is needed to ensure that Egypt does not significantly compromise its competitiveness and fall back in its development.

This report has examined the state of Egypt's competitiveness on each of the 12 pillars comprising the GCI. Yet, all pillars are interrelated and mutually reinforcing. Egyptian competitiveness in the various macroeconomic indicators intersect; decreasing budget deficit is likely to improve government debt; lower government debt and budget deficit will allow the Central Bank of Egypt to move toward inflation targeting; containing inflation is likely to have a positive impact on interest rates both in real and nominal terms; clarity in monetary policy is likely to entice financiers to improve lending terms, which would then bring the possibility of narrowing the interest rates spread.

Egypt's low degree of human development as reflected by the GCR, especially the low quality of education and training, poor health and inefficient and poorly skilled labor, implies that Egypt should ensure that resources spent on human development are indeed investments in human capital. Inadequate human capital constrains productivity and growth and compromises the well-being of all Egyptians. Building a strong human capital base through quality education, training and better health should be a top government priority. Ensuring that the outcomes of the educational and training system are in line with those required by today's global economy as well as developing a serious monitoring and evaluation framework should be prioritized and highlighted in the government plan.

The poor skills of labor represent a significant concern to employers. Persistent skill mismatch and low education quality partly explain the modest economic returns to education in Egypt. On average, a university graduate would earn 37 percent more than a person with no formal education. The overall educational returns in Egypt are lower than other countries in the region such as Tunisia and Morocco. Policy makers should use incentives, public accountability, curriculum, and labor market reforms to improve competitiveness. Successful education reforms require better engineering of education, better motivation/incentives and improved public accountability.

Synergy between the private and public sectors and greater coordinated efforts between universities and businesses are also of great importance. Efforts should equally address labor market rigidities, non-wage labor costs, ways to prevent brain drain and increasing female integration in the labor force.

ENCC FRAMEWORK FOR GREATER INTERNATIONAL COMPETITIVENESS

Connectivity, Productivity and Responsibility Interlinked

The key facilitating elements in a connected nation are; 1) connectivity, in particular connected government 2) productivity and 3) responsibility and social inclusion. Connected government means joined up administrative processes, enhanced dialog with the private sector and the community and a framework for cooperation. National productivity requires creative thinking, clear vision, cooperation, seamless infrastructure and above all leadership. Linking-in to the educational, training and labor sectors will lead to productivity gains at the national, sector and enterprise level. Connecting the drivers of economic development in this way with one another and with the necessary checks and balances to safeguard society, is the challenge for Egypt going forward. The approach can give a quantum boost to competitiveness and provide the basis for balanced growth, where everybody wins. ***See the boxes on pages 81, 99 and 121***

The Egyptian Economy in the Face of Global Financial Turbulence: Steady through the Storm?

Amina Ghanem

In the wake of a favorable 2007/2008, Egypt's GDP growth reached 7.2 percent in June 2008. The strong performance underscored Egypt's bold reforms initiated in 2004 by Prime Minister Ahmed Nazif's cabinet.

The economy, however, has not escaped the slowdown resulting from the global financial crisis. Since October 2008 the rapid deterioration in the global environment has affected the world — Egypt is no exception. Nevertheless, Egypt is in a better place than many countries to weather the global financial turbulence and worldwide recession. Despite a number of pre-existing vulnerabilities that may slow recovery, strong fundamentals will help the Egyptian economy.

Two fundamental strengths have helped the economy weather the direct and harsh first round effects of the financial crisis: Egypt's relatively strong domestic economy and its limited integration with global financial markets. These two assets have provided a cushion against spillovers from the financial crisis to Egypt. However, the global financial crisis has served as a timely reminder of the difficult challenges accompanying Egypt's economic growth. Pre-existing weaknesses will be a stress test for the economy during the crisis, making the recovery more difficult. Although inflation in Egypt is now on a downward trend, an already high and rising budget deficit, tight fiscal space and the prospective economic slowdown will be added pressures on Egypt's deteriorating competitiveness.

While robust domestic demand will serve to buffer the economy to a large extent from the direct and harsh impact of the recent turmoil in the global economy, the contagion will be channeled to Egypt through its strong trade and investment links with the Middle East region and the rest of the world. The economy will be further affected if the global economic downturn turns out to be deeper and longer than originally foreseen.

As a result, economic growth will experience a significant slowdown in 2008-2009. The financial crisis has heightened Egypt's vulnerabilities and exposed weaknesses in its competitiveness. Managing these challenges will enable the Egyptian economy to emerge stronger and more resilient from this exceptionally difficult period.

2.1 ECONOMIC DEVELOPMENTS IN EGYPT BETWEEN 2003-2004 & 2007-2008: A REMARKABLE TURNAROUND STORY

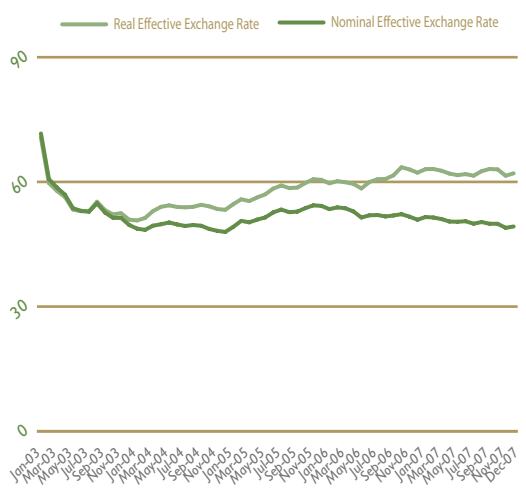
2.1.1 Bold Macroeconomic and Structural Reforms Paved the Way for Strong Growth

Egypt has seen positive results from the wide-ranging macroeconomic reform program it launched in 2004, following a stall in economic reforms and growth rates since 1998-1999. The reforms targeted the exchange rate, reductions in the fiscal deficit and public debt, the enhancement of public financial management, improving the investment climate and trade reforms that restored economic competitiveness. Combined with other trade reforms, reductions in customs duties and in the cost of doing business, these policies have spurred foreign investment and growth. In addition, financial sector reforms introduced and implemented in the past have brought about a resilient banking sector. On the external side, foreign debt ratios were low and there has been a substantial build up of reserves. Despite reform efforts, macroeconomic vulnerabilities remained in the form of a high budget deficit and rising inflation rates.

2.1.1.1 Monetary Policy

Regarding monetary policy, the Egyptian pound stabilized in 2004 after a significant depreciation since 2003. The first key ingredient to this stabilization was the establishment of an interbank market and open market operations that served to create a liquid foreign exchange market and converge the official and parallel markets. The second ingredient was the elimination of surrender requirements that enhanced the liquidity of the foreign exchange market because it gave confidence to the international community that Egypt will pursue sound economic policies that preclude the need to use such a restriction. The third component of the stabilization of the pound was the newly established Monetary Policy Committee, which started putting in place a credible and transparent momentary policy whose objective was price stability (MOF, 2009a).

FIGURE 2.1: *ANNUAL EFFECTIVE EXCHANGE RATE INDICES (JANUARY 2003 - DECEMBER 2007)*



Source: IMF

2.1.1.2 External Sector

These developments spilled over to the external sector in the form of inflows of private foreign capital that supported the accumulation of reserves and the repayment of external debt. Net international reserves (NIRs) jumped from US$ 14.8 billion in June 2004 to US$ 35 billion in June 2008 (MOF, 2009a). External debt as a percentage of GDP dropped from 34 percent in June 2004 to 20 percent in June 2008. Debt service as a percent of current account receipts was more than halved during the same period, falling from 9.7 percent to 4.3 percent.

The current account remained in surplus between 2003-2004 and 2007-2008, although the surplus narrowed from US$ 3.4 billion to US$ 0.9 billion. Receipts from the Suez Canal, workers remittances and tourism all increased significantly from some US$ 13 billion to US$ 27.2 billion during the past four years. Exports tripled from US$ 10.5 billion in June 2004 to US$ 29.4 billion in June 2008. Most of the increase came from oil exports, with the share of merchandise exports falling from 62 percent of total exports in June 2004 to 50 percent in June 2008. During the same period, imports almost tripled from US$ 18.3 billion to US$ 53 billion, partly reflecting greater openness in the economy and the counterpart imports to unprecedented Foreign Direct Investment (FDI) flows, but mostly the spike in commodity prices of 2007-2008, which saw alone a 38 percent increase in imports over the previous year.

2.1.1.3 Fiscal Policy

Fiscal reforms supported the ongoing changes on the monetary policy and external sector sides. A bold tax reform incorporating a 50 percent reduction in tax rates and better tax administration has significantly improved tax revenues. Tax revenues have more than doubled during the past few years, increasing from

some LE 102 billion in June 2004 to LE 221 billion in June 2008 through greater compliance and a broadening of the tax base.

The overall deficit was lowered to 6.9 percent of Gross Domestic Product (GDP) in June 2008, from 9.5 percent of GDP in June 2004. Gross domestic public sector debt was reduced to less than 60 percent of GDP in June 2008, from 80 percent in June 2004. This was facilitated by fiscal restraint, which contained the increase of the primary deficit to between 2.5-3 percent.

A new three-year public debt management project was recently introduced with the aim of improving Egypt's public debt management and developing the government securities market. The project focuses on:

- Implementing sound issuance practices
- Developing a comprehensive medium-term debt management strategy covering both domestic and external debt
- Enhancing repurchase agreement (REPO) transactions and regulating the REPO market
- Introducing new financial tools such as short selling, bond lending, as well as buyback and exchange operations
- Developing the primary and secondary market and promoting secondary market liquidity and pricing transparency
- Improving clearing and settlement processes

The improved management has resulted in the extension of its debt maturity from 164 days in June 2004 to approximately two years now. Currently rates on three-month, six-month and one-year treasury bills are 10.46 percent, 10.62 percent and 10.57 percent, respectively.

In the public financial management (PFM) area, reforms included enacting a treasury single account; improving budget classification and control; and rolling out the Government Financial Management Information System (GFMIS).

The Ministry of Finance is also developing, with assistance from the World Bank, a set of Public Expenditure and Financial Accountability assessment (PEFA) indicators. The objective is to ensure that (i) there is effective controls of the budget totals and management of fiscal risks and that (ii) the planning and execution of the budget and the management of budgeted resources contribute to the implementation of the government's objectives and supports aggregate fiscal discipline, strategic allocation of resources and efficient service delivery.

In addition, the ministry is in the process of shifting from the one-year framework the three-year budget by establishing a medium-term expenditure framework (MTEF) for budget formulation and preparation. To pave the way for the adoption of the MTEF, the Ministry of Finance introduced program-based budgeting in 2005. And, as a step to make government spending more effective, the Ministry of Finance is implementing a pilot public expenditure tracking survey (PETS) in the education sector. The objective is to track the spending of monies allocated to education by higher levels of government down through all the relevant levels of the system until the end-users and find out whether the money is reaching the beneficiaries and whether it is achieving the intended results. The PETS survey will at a later stage be scaled up to other sectors.

Recent trade reforms include a reduction in tariff adjustments in January 2009. Presidential Decree No. 51 of 2009 was issued reducing tariffs on a number of raw materials, machinery, equipment and production inputs and intermediate goods. The objective of the reductions is to enhance the competitiveness of national industries. Tariffs were reduced on environmentally friendly products and social goods.

2.1.1.4 Business Environment

There were also significant improvements in the business environment. The World Bank's "Doing Business 2009" placed Egypt as one of the world's top 10 reformers[1], moving its ranking from 165th (among 175 countries) to 125th (among 181 countries), in just three years. Egypt is the "systematic reformer" of North Africa, reforming more than five areas: (i) starting a business; (ii) dealing with construction permits; (iii) registering property (iv) getting credit; (v) protecting investors and (vi) trading across borders. Egypt also implemented some 22 reforms over the past five years (World Bank, 2009).

Strong progress was made in starting businesses over the past years. Easier regulations enabled easier entry of firms and thus an increasingly larger number of firms registered in General Authority for Investment (GAFI). The establishment of one-stop-shops has cut processing time to 9 days, compared to 11 days in Tunisia, 12 days in Morocco, 15 days in Saudi Arabia and 35 days in Kuwait. The number of procedures has also fallen from 10 to 7, approaching the OECD average of 6 procedures. The minimum capital required to start a business was slashed from LE 50,000 to LE 1,000. There is now a steady decline in bankruptcy rulings after a change in the Bankruptcy Law that allowed financial reorganization and liquidation (World Bank, 2009).

[1] These 10 countries are: Azerbaijan, Albania, Kyrgyz Republic, Belarus, Senegal, Burkina Faso, Botswana, Columbia, Dominican Republic and Egypt.

Table 2.1: *Doing Business in Egypt (2007 - 2009)*

Category	Doing Business 2007 Rank	Doing Business 2008 Rank	Change in Rank	Doing Business 2009 Rank	Change in Rank
Ease of Doing Business	152	126	26	114	12
Starting a Business	126	55	71	41	14
Dealing with Construction Permits	165	163	2	165	-2
Employing Workers	106	108	-2	107	1
Registering Property	147	101	46	85	16
Getting Credit	156	115	41	84	31
Protecting Investors	105	83	22	70	13
Paying Taxes	152	150	2	144	6
Trading Across Borders	86	26	60	24	2
Enforcing Contracts	146	145	1	151	-6
Closing a Business	124	125	-1	128	-3

Source: World Bank, Doing Business in Egypt 2008 & 2009.

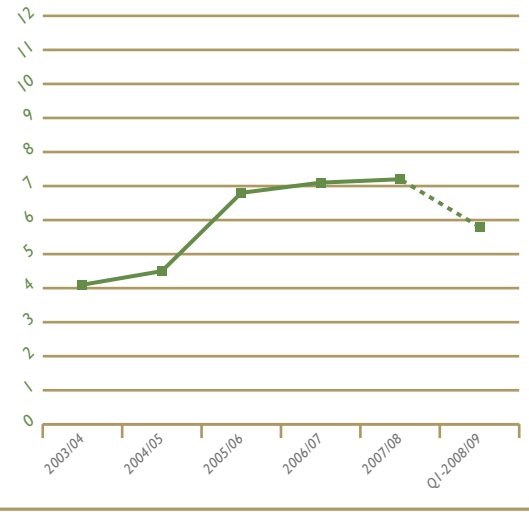
Recent reforms in property registration raised revenues by 39 percent. Egypt is also among the friendlier countries in dealing with construction permits, registering property, getting credit, protecting investors and trading across borders. Egypt, however, is not that friendly when it comes to employing workers, enforcing contracts, or closing a business (World Bank, 2009).

Improvements in the macroeconomy and business environment have magnetized FDI. In response to the improving business climate and other reforms implemented, foreign direct investment inflows have exponentially grown over the past years, jumping from a mere 3 percent of GDP (US$ 407 million) in June 2004 to 4.4 percent (US$ 3.9 billion) to 8.1 percent of GDP (US$ 13.2 billion) in June 2008. FDI inflows are being dispersed throughout the sectors of the economy, with nearly 48.5 percent going to Greenfields and non-hydrocarbon investments, 31.1 percent going to oil, 17.4 percent going to privatization, and the remaining 3 percent going to real estate and construction (MOF, 2009a).

2.1.1.5 Economic Growth

Following these reforms, GDP economic growth rates have progressively recovered during the past four years from 4 percent in June 2004 to 7.2 percent in June 2008. Figure 2.2 demonstrates the growth rate of GDP. The robust performance owes to the bold "homemade" changes implemented by a government with a "big appetite for reform" (Merrill Lynch, 2008).

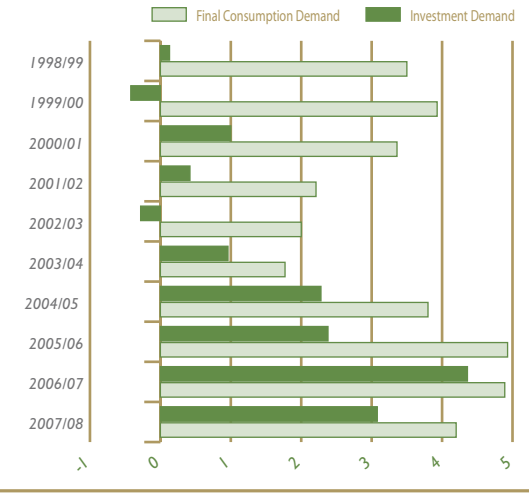
FIGURE 2.2: *ANNUAL REAL GDP GROWTH RATE (2003/2004 - SEPTEMBER 2008)*



Source: Ministry of Economic Development (MOED)

The main drivers of high GDP growth rates were buoyant domestic demand, reflected in robust consumption and surging investment demand levels, including foreign direct investment as discussed earlier (Figure 2.3).

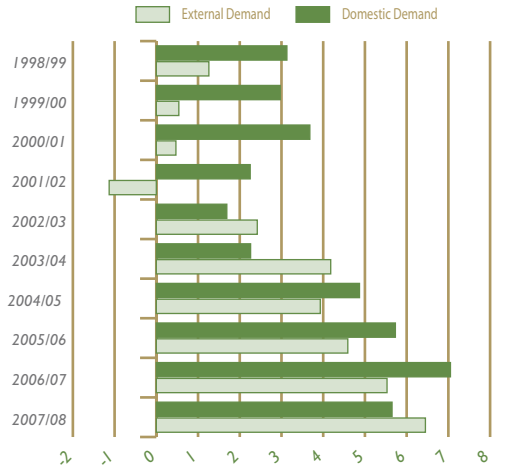
FIGURE 2.3: *ANNUAL PERCENT CONTRIBUTION OF INVESTMENT DEMAND & FINAL CONSUMPTION TO THE GROWTH IN DOMESTIC DEMAND (1998/1999 - 2007/2008)*



Source: MOED

External demand however, gained strength in 2007-2008 at the expense of domestic demand (Figure 2.4, GDP contributions, bars). The main advantage of strong domestic demand-led growth is that it helps reduce susceptibility to cyclical swings in the external sector.

FIGURE 2.4: *ANNUAL PERCENT CONTRIBUTION OF DOMESTIC & EXTERNAL DEMAND TO THE GROWTH IN GDP TOTAL USES (1998/1999 - 2007/2008)*



Source: MOED

The strong growth rates are driven by the private sector. Since 2004-2005, the private sector's contribution to real GDP has steadily increased over public sector contribution; private sector contribution in real terms reached some 4.9 percentage points of the 2007-2008 growth rate of 7.2 percent; or 68 percent of real growth. This compares to 63.3 percent of growth in 2004-2005 and 60.3 percent in 2005-2006. The main drivers of the strong growth have been the transportation and communication sector, wholesale and retail, and the large inflows of FDI into manufacturing, construction activities and tourism sectors. The increased role of the private sector in the economy has increased productivity substantially: the rise in total factor productivity is greater in the sectors that have higher private sector participation (World Bank, 2008).

2.1.1.6 Banking Sector

While the World Economic Forum's Global Competitiveness Index scores show that Egypt's banking system is not necessarily efficient or sophisticated, financial indicators show that the banking system is sound. Its lack of sophistication proved an asset in that it helped insulate it from the global market crisis. Financial sector reforms introduced and implemented in the past have brought about a resilient banking sector. Reforms include a strengthening of bank supervision, restructuring and consolidation, and a clean-up of Non-Performing Loans (NPLs) that left it well capitalized. NPLs as a percent of total loans have fallen from 18.2 percent to 16.6 percent between 2005-2006 and 2007-2008. The capital adequacy ratio has consistently improved over the past years, rising from 14.7 percent in 2005-2006 to 14.9 percent in 2007-2008 (IMF, 2009c).

The banking system has large holdings of liquid assets that have allowed it to contain the risks of liquidity pressures arising from tight international credit markets. Some 44 percent of total banks assets are in the form of liquid government securities. Return on assets rose from 0.8 percent to 0.9 percent between June 2006 and June 2007 (IMF, 2009c).

Furthermore, provisioning against default is substantial, with provisions as percent of NPL rising sharply from 76.2 percent to almost 90 percent over the past two years. Egypt's banking system is underpinned by sound regulations that strictly limit banks' levels of integration with the global system. Foreign currency deposits are a relatively stable share of total deposits; about 24 percent of total deposits are denominated in Egyptian pounds and the rest are denominated in foreign currency (MOF, 2009a). Banks, including foreign-owned banks, mostly rely on domestic funding to expand their balance sheets, thus have been unaffected by tight global capital markets. Foreign banks did not have to cut back on lending on account of tightening liquidity conditions in their home countries. Furthermore, corporate sector dependence on overseas financing is limited, with most enterprises relying on retained earnings and credit from financial institutions to fund new investments. In addition, credit growth has been low by emerging market standards, rising from 8.6 percent to 12.6 percent over the past two years. And given their already limited exposure to structured credit products, the banks have had limited exposure to subprime products (IMF, 2009c).

2.1.2 Nevertheless the Economy has a Number of Pre-Existing Macroeconomic Vulnerabilities that Undermine its Competitiveness

Despite the strong fundamentals of the economy that underpinned the healthy economic performance of the past four years, Egypt's competitiveness has consistently deteriorated during the past three years. Egypt ranks 81st in the 2008-2009 Global Competitiveness Report (GCR) on the Global Competitiveness Index, down from 77th place in 2007-2008, and from 71st place in 2006-2007. Key factors to the deterioration include macroeconomic instability reflected in double-digit inflation, a high budget deficit, and *labor market inefficiencies in which* ***Egypt ranks last among all 134 countries.*** Egypt's educational institutions continue to receive weak assessments (124th place).

Chapter 2 of the *Egyptian Competitiveness Report* (ECR), 2008 discussed some of these weaknesses in the context of Egypt's deteriorating competitiveness: double digit inflation, high domestic debt and fiscal deficit ratios, and unbalanced growth.

Despite its recent decline, inflation is still in double digits. In September 2008, inflation peaked to 22.4 percent compared to 8.4 percent in September 2007. Inflation has since come down (the recent plunge in food and fuel prices and slackened global demand have helped reduce inflationary pressures) but remains high at 14.3 percent in January 2009 compared to 10.5 percent in January 2008. Inflation in Egypt has on average been high (Shepherd, 2008), with implications for unsustainable growth, weak competitiveness and ineffective pro-poor policies.

Monetary policy through 2008 and mid-2009 grappled with the need to contain the impact of strong capital inflows and rising import prices without pressuring growth. In response to the strong and unprecedented FDI flows between 2004 and 2008 (see 1.1.2), the Central Bank raised the overnight interest rate sharply from 8.8 percent in January 2008 and to 11.75 percent in October 2008 by three whole percentage points in 10 months. More recently, in January 2009, the Central Bank has allowed rates to slide by 0.2 percentage points.

In the face of strong capital flows, and despite modest interest rate increases, the pound continued to appreciate during that period. Inflation thus remained high during 2008.

Analyzing Egypt's fiscal profile, three key weaknesses are noted. First, although domestic debt ratios have improved — with net domestic budget sector debt tumbling from 67.4 percent in June 2004 to 53.4 percent in June 2008, and net domestic public debt falling from 46.8 percent to 43.1 percent during the same period[2] — these ratios are high relative to other developing countries. These figures are twice the debt ratios for countries such as India, Morocco, Brazil, Mexico and Tunisia (Fitch, 2007, cited in ECR, 2008).

Second, the budget deficit remains high at 6.8 percent and is projected to go up to 6.9 percent as the government implements its countercyclical fiscal stimulus. Only Sri Lanka has worse fiscal ratios (Fitch, 2007, cited in ECR, 2008).

Third, and more serious, the budget suffers from a number of rigidities that minimize the fiscal space available to implement a large fiscal stimulus package to stimulate economic growth, or to make the needed improvements in the health and education sectors — two sectors crucial for the empowerment of Egypt's labor force and improving the competitiveness of the economy.

Examining the major components of the budget in Table 2.2, we find that as a percent of total expenditures, wages stand at 23 percent of total expenditures, compared to interest payments at 15.4 percent. If we add subsidies of 39 percent and defense expenditures of 7.5 percent[3], we find that 85 percent of total fiscal expenditures are rigid, and under the current social constraints would be difficult to re-prioritize. To create fiscal space, the government has to continue with structural reforms of the budget, creating more revenue sources and rationalizing expenditures.

Table 2.2: ***Breakdown of Fiscal Expenditures.***

	2007-2008		2008-2009	
	LE billion	% of total expenditures	LE billion	% of total expenditures
Wages	62.8	22.2	79	23
Interest payments	50.5	17.9	53	15.4
Subsidies	92.4	32.7	134	39
Other expenses	23.9	8.5	25.8	7.5
Sub-total		81.3		84.9
Purchases	18.5	6.6	23.8	6.9
Purchase of non-financial assets	34.2	12.1	28.3	8.2
Total Expenditures	282.3	100	343.9	100

Source: MOF (2009a)

The fourth challenge that the economy faces is that the macroeconomic pattern of growth is failing to generate job opportunities. In other words growth is being created from non-labor intensive sectors, as shown in the growth of gross domestic product in Table 2.3. As a result, unemployment marginally declined from 8.9 percent to 8.8 percent in 2007-2008 (IMF 2009c). Also poverty indicators have improved very slowly since 1999-2000. Between 1995-96 and 1999-2000 the average poverty rate declined from 51.4 percent to 42.6 percent. Between 1999-2000 and 2004-2005, it fell just 2.1 percentage points to 40.5 percent (World Bank, 2008).

Upon analyzing the components of GDP in Table 2.3, we find that most of the economic growth is explained by the private sector. However, it is led by sectors that require high skills, be they high technology such as manufacturing, communication or financial services; or in capital intensive sectors that do not generate sufficient employment opportunities and still require

[2] The Ministry of Finance uses a number of government debt indicators. Please refer to MOF (2009b), p. 4.

[3] Already below many other countries in the region

skilled labor (e.g. manufacturing and construction). The private sector contributed around 68.3 percent of the growth rate in 2007-2008.

On the other hand, areas of the economy such as the agriculture sector — which can absorb large sections of the unskilled labor force — continue to under-perform; growing much slower than the other sectors. In 2007-2008 agriculture contributed a mere 0.47 percentage points (11 percent) of the growth of the private sector, compared to 0.53 percentage points in 2004-2005.

Table 2.3: ***Private and Public Sector Contributions to Real GDP Growth in 2004/2005 to 2007/2008***

	2004/2005		2005/2006		2006/2007		2007/2008	
	Private	Public	Private	Public	Private	Public	Private	Public
Agriculture, Woodlands & Hunting	0.53	0.00	0.53	(0.01)	0.57	0.00	0.47	0.00
Extractions	0.07	0.48	0.28	1.35	0.08	0.26	0.12	0.47
Manufacturing Industries	0.74	0.11	0.99	0.12	1.23	0.14	1.15	0.14
Electricity	0.01	0.11	0.01	0.14	0.01	0.10	0.00	0.11
Water	0.00	0.02	0.00	0.03	0.00	0.03	0.00	0.02
Construction & Buildings	0.19	0.03	0.54	0.07	0.67	0.07	0.58	0.05
Transportation & Communication	0.42	0.07	0.52	0.08	0.62	0.09	0.59	0.21
Suez Canal	0.00	0.47	0.00	0.31	0.00	0.50	0.00	0.61
Whole Sale & Retail	0.35	0.02	0.73	0.02	0.92	0.04	0.75	0.03
Financial Intermediaries & Supporting Services	0.09	0.15	0.11	0.20	0.15	0.26	0.11	0.19
Insurance & Social Insurance	0.00	0.10	0.00	0.13	0.00	0.16	0.00	0.24
Restaurants & Hotels	0.61	0.01	0.15	0.00	0.44	0.01	0.83	0.01
Real Estate Activities	0.11	0.01	0.14	0.01	0.15	0.01	0.10	0.00
Public Government	0.00	0.30	0.00	0.33	0.00	0.32	0.00	0.18
Education, health, social, cultural, entertainment & personal services	0.12	0.00	0.15	0.01	0.21	0.01	0.20	0.01
Other Services	--	--	0.07	0.00	0.12	0.00	--	--
Sub-Total of Sectors	3.24	1.88	4.22	2.78	5.18	1.99	4.91	2.27
Total Real GDP Growth Rate	5.12		7.00		7.17		7.18	

Source: Ministry of Economic Development

2.2 IMPACT OF THE FINANCIAL CRISIS ON THE GLOBAL ECONOMY

Global growth has slowed substantially and is expected to continue falling until the end of 2010. Falling inflation, the creation of liquidity through monetary easing, the implementation of fiscal stimuli and liquidity injections should all stabilize global financial markets by the end of next year. Two risks to this recovery would be delays in implementing the measures aimed at stabilizing the global financial markets and the adoption of trade and financial protectionist measures by countries.

2.2.1 Global Economic Recovery Expected by the End of 2010

Global economic activity is falling — with advanced economies registering their sharpest declines in the post-war era — despite forceful policy efforts. According to the latest IMF forecast (G-20, 2009; WEO, 2009), world growth is projected to fall from some 5.2 percent in 2007 to 0.5 percent in 2009 (Table 2.4), its lowest rate since World War II, with the downturn led by advanced economies. The projected growth rate is down 0.75 percentage points from the October 2008 World Economic Outlook (WEO) projections. This would be the first annual contraction during the postwar period, although the downturn is comparable in magnitude to those that occurred in 1975 and 1982. Helped by efforts to ease credit strains as well as expansionary fiscal and monetary policies, the global economy should experience a gradual recovery in 2010, with growth picking up to 3.4 percent.

The downward revisions to 2009 real GDP growth projections are somewhat larger in emerging and developing economies, averaging 1 percent. This would

leave their growth rate at 5 percent, higher than in earlier business cycle troughs (for example, 1990, 1998 and 2001). However, the cyclical downturn in emerging economies is of a similar magnitude to that in the advanced economies when measured relative to their trend growth rates. Among the most affected are commodity exporters, given that commodity price projections have been marked down sharply, and countries with acute external financing and liquidity problems. Countries in East Asia —including China — generally have suffered smaller markdowns, because their financial situations are typically more robust. They have benefited from improved terms of trade from falling commodity prices, and they have already initiated a shift toward macroeconomic policy easing (WEO, 2009).

Table 2.4: ***Overview of the World Economic Outlook Projections (Percent change, unless otherwise noted).***

	Year over Year						Q4 over Q4		
					Difference from November				
			Projections		2008 WEO Projections		Est.	Projections	
	2007	2008	2009	2010	2009	2010	2008	2009	2010
World output	5.2	3.4	0.5	3	-1.7	-0.8	1.1	1.2	3.4
Advanced economies	2.7	1	-2	1.1	-1.7	-0.5	-1.1	-0.5	1.6
United States	2	1.1	-1.6	1.6	-0.9	0.1	-0.7	--	2
Euro area	2.6	1	-2	0.2	-1.5	-0.7	-0.7	-1.4	0.9
Germany	2.5	1.3	-2.5	0.1	-1.7	-0.4	-1.2		0.4
France	2.2	0.8	-1.9	0.7	-1.4	-0.8	-0.5	-1.8	2.2
Italy	1.5	-0.6	-2.1	-0.1	-1.5	-0.1	-1.5	-1.3	0.8
Spain	3.7	1.2	-1.7	-0.1		-0.9	-0.4	-1.5	0.5
Japan	2.4	-0.3	-2.6	0.6	-2.4	-0.5	-3	-0.2	0.8
United Kingdom	3	0.7	-2.8	0.2	-1.5	-0.9	-1.8	-1.5	0.8
Canada	2.7	0.6	-1.2	1.6	-1.5	-1.4	-0.4	-0.4	2
Other advanced economies	4.6	1.9	-2.4	2.2	-3.9		-1.6	0.1	2.7
Newly industrialized Asian economies	5.6	2.1	-3.9	3.1	-6	-1.1	-3.4	0.6	3.3
Emerging and developing economies	8.3	6.3	3.3	5	-1.8	-1.2	4.5	3.5	5.8
Africa	6.2	5.2	3.4	4.9	-1.4	-0.5	...	...	...
Sub-Sahara	6.9	5.4	3.5	5	-1.6	-0.7	...	...	...
Central and Eastern Europe	5.4	3.2	-0.4	2.5	-2.6	-1.3	...	...	...
Commonwealth of Independent States	8.6	6	-0.4	2.2	-3.6	-2.3	...	...	...
Russia	8.1	6.2	-0.7	1.3	-4.2	-3.2	2.7	-1.3	1.9
Excluding Russia	9.7	5.4	0.3	4.4	-1.3	-0.3	...	...	...
Developing Asia	10.6	7.8	5.5	6.9	-1.6	-1.1	...	...	...
China	13	9	6.7	8	-1.8	-1.5	6.8	7.5	8.1
India	9.3	7.3	5.1	6.5	-1.2	-0.3	5.1	5.3	7.1
ASEAN-5	6.3	5.4	2.7	4.1	-1.5	-1.3	4.1	3.1	4.5
Middle East	6.4	6.1	3.9	4.7	-1.5	-0.6	...	...	...
Western Hemisphere	5.7	4.6	1.1	3	-1.4		...	...	...
Brazil	5.7	5.8	1.8	3.5	-1.2		4.3	2.2	4.2
Mexico	3.2	1.8	-0.3	2.1	-1.2	-1.4	--	0.2	3.3
Memorandum									
European Union	3.1	1.3	-1.8	0.5	-1.6	-0.8	...	...	...
World growth based on market exchange rates	3.8	2.2	-0.6	2.1	-1.7	-0.7	...	...	...
World trade volume (goods and services)	7.2	4.1	-2.8	3.2	-4.8	-2.5	...	...	...
Imports									
Advanced economies	4.5	1.5	-3.1	1.9	-3	-1.8	...	...	...
Emerging and developing economies	14.5	10.4	-2.2	5.8	-7	-3.6	...	...	...
Exports									

Table 2.4: ***Overview of the World Economic Outlook Projections (Percent change, unless otherwise noted). (Cont'd)***

	Year over Year						Q4 over Q4		
					Difference from November				
			Projections		2008 WEO Projections		Est.	Projections	
	2007	2008	2009	2010	2009	2010	2008	2009	2010
Advanced economies	5.9	3.1	-3.7	2.1	-5	-1.8	...	...	...
Emerging and developing economies	9.6	5.6	-0.8	5.4	-5.8	-3.5	...	...	...
Commodity prices (U.S. dollars)									
Oil	10.7	36.4	-48.5	20	-16.7	9.7	...	...	...
Nonfuel (average based on world commodity export weights)	14.1	7.4	-29.1	7.3	-10.4	6.3	...	...	...
Consumer prices									
Advanced economies	2.1	3.5	0.3	0.8	-1.1	-0.8	2.6	0.3	0.9
Emerging and developing economies2	6.4	9.2	5.8	5	-1.3	-0.5	7.6	4.7	4.2
London interbank offered rate (percent)									
On U.S. dollar deposits	5.3	3	1.3	2.9	-0.7	-1.4	...	...	...
On Euro deposits	4.3	4.6	2.2	2.7	-0.8	-0.8	...	...	...
On Japanese yen deposits	0.9	1	1	0.4	--	-0.3	...	...	...

Source: WEO (2009).

2.2.2 Weakening Prospects are Depressing Commodity Prices, which could Help Expedite the Recovery

Weakening global demand is depressing commodity prices. Oil prices have declined by more than 50 percent since their peak, retreating to levels not seen since early 2007. The fall in commodity prices reflects the major global downturn, the strengthening of the U.S. dollar, and the financial crisis — despite the decision by OPEC to reduce production. In line with market developments, the IMF's baseline petroleum price projection for 2009 has been revised down relative to the October WEO, from US$ 100 to US$ 68 a barrel. Similarly, metals and food prices have fallen from their recent peaks. While this eases the burden on households in advanced economies and emerging economies in Europe and Asia, it lowers growth prospects in many other emerging economies that depend on commodity exports.

The combination of stabilizing commodity prices and increasing economic slack will help to contain inflationary pressures. In the advanced economies, headline inflation should decline to below 1.5 percent by the end of 2009. In emerging economies, inflation is also expected to moderate, albeit more gradually. However, in a number of these countries, inflation risks are still manifest, as higher commodity prices and continued pressure on local supply conditions have affected wage demand and inflation expectations (WEO, 2009).

2.2.3 Global Economic Recovery could be Delayed in the Face of a Number of Uncertainties

Given the recent dramatic reversal in the price of oil and other commodities, the gradual thawing of credit markets, the monetary easing that has already been set in motion and the large amounts of fiscal stimulus committed to by the G-20 countries (G-20 Communiqué, 2009) likely to be enacted soon, a robust global recovery should be expected by the end of 2010. Nevertheless, the outlook for the world economy is highly uncertain, and the timing and pace of the recovery depend crucially on:

- **How rapidly sufficient liquidity is created through monetary easing in order to support growth.** Expansionary monetary policies are needed to support aggregate demand both this year and next. However, with the impact of monetary policy weakened by financial system problems and with interest rates in key economies already approaching zero, there is little room for creating liquidity through this venue. Innovative credit policies also may be needed in some economies (Lipsky, 2009).
- **How rapidly sufficient fiscal stimuli and liquidity injections are implemented and actually help in stabilizing global financial markets.** The discretionary fiscal stimulus being provided by G-20 countries should have a significant impact on labor markets. Assuming that it raises GDP growth by two percentage

points, about 20 million jobs would be saved in G-20 countries alone. Moreover, according to IMF analysis, one-third of the beneficial growth impact of the anticipated 2009 fiscal action stems from international spillovers (Lipsky, 2009).

However, although the discretionary fiscal stimulus being provided by G-20 countries is sizeable, its falls short of the 2 percent of aggregate GDP in 2009 and 2010 recommended by the fund to stimulate growth by the end of 2010 (IMF Survey, 2009b). Also, some countries may not have sufficient room to implement expansionary fiscal policies because of an already high budget or current account deficits.

- **The implementation of outward-oriented trade and financial policy measures by all countries (IMF Survey, 2009b).** Eighty years ago, three major policy mistakes turned the stock-market crash of 1929 into the Great Depression of the 1930s: a tight monetary policy, a restrictive fiscal stance and a wave of protectionism that paralyzed the world's greatest wealth-creation machine, the exchange of goods and capital across national borders. This time, central bankers and politicians around the world are avoiding the first two mistakes (Schmieding, 2009). Nevertheless, delays in implementing the agreed commitments could result in a further intensification of the negative feedback loops between the real economy and the financial system, leading to an even deeper and prolonged recession (Ram, 2009).

With regards to protectionism, there is still a rising risk that a collapse in cross-border commerce could critically deepen and prolong the downturn. Countries are not shutting their borders to trade in the old-fashioned way through tariffs, import quotas or other instruments of economic torture. Even the approaching avalanche of national subsidies to national producers, which can distort global competition as badly as tariffs do, is not the major threat to watch. At least in Europe, the key risk stems from an abrupt reversal of financial globalization. As stricken banks strive to bring money home, some of the cross-border flows of liquidity that grease the global production process are drying up.

While much attention has focused on the need to offer more stimulus spending, greater funding for the IMF and putting in place financial regulations, for many emerging countries it is more an issue of increasing protectionist policies (Ram, 2009), be they trade or financial. A World Bank study by Gamberoni and Newfarmer (2009) identified a number of practices by countries that restrict trade at the expense of other countries. Since G-20 leaders signed a pledge in November 2008 to avoid protectionist measures, several countries, including 17 of the G-20, have implemented 47 measures that restrict trade at the expense of other countries. Tariff increases comprise only about a third of these protectionist actions for these countries, and a half for other developing countries. Since the beginning of the financial crisis, officials have proposed and/or implemented roughly 78 trade measures, according to the World Bank's monitoring list of trade and trade-related measures. Of these, 66 involved trade restrictions, and 47 trade-restricting measures eventually took effect. These measures have a significant negative effect on particular exporters that are shut out of markets (Gamberoni and Newfarmer, 2009).

For example, Russia raised tariffs on used automobiles, and Ecuador raised tariffs on more than 600 items. Non-tariff measures include such policies as Argentina's imposition of non-automatic licensing requirements on auto parts, textiles, televisions, toys, shoes and leather goods. Indonesia now requires that five categories of goods (including garments, footwear, toys, electronics, food and beverages) would be permitted in only five ports and airports (Gamberoni and Newfarmer, 2009).

In some countries, tightening standards have slowed imports, note Gamberoni and Newfarmer (2009). These include, for example, China's import ban on Irish pork as well as rejection of some Belgian chocolate, Italian brandy, British sauce, Dutch eggs and Spanish dairy products, and India's ban on Chinese toys. Export subsidies contravene the draft Doha modalities. This did not prevent the EU from announcing new export subsidies on butter, cheese and milk powder. Less obviously, both China and India have increased the rebate on the duty drawback system for exporters, and, although the subsidy component is a matter of discussion, the timing of these measures raises questions.

Subsidies proposed for the automobile industry have proliferated and total some US$ 48 billion worldwide, mostly (US$ 42.7 billion) in high-income countries. In addition to the US direct subsidy of US$ 17.4 billion to its three national companies, Canada, France, Germany, United Kingdom, China, Argentina, Brazil, Sweden and Italy have also provided direct or indirect subsidies. In addition, Australia provided support to its car dealers, and South Korea and Portugal supported their component suppliers. To the extent that the industry is laden with excess capacity, these subsidies impede exit and delay adjustment. Even worse, subsidies may be linked to requirements that companies preserve domestic employment, even at the cost of shutting more efficient plants abroad in developing countries. Moreover, to prevent this, governments have had to react to the policies of neighbors — for example, Canada has matched the subsidies the US

gave Detroit automakers to ensure that Canadian plants of American producers would remain open.

These measures are similar to protectionist measures resorted to in the 1930's that were directly responsible for the downturn at the time. World Bank President Robert Zoellick remarked that "Economic isolationism can lead to a negative spiral of events such as those we saw in the 1930s, which made a bad situation much, much worse" (Gamberoni and Newfarmer, 2009).

In their World Bank report, Gamberoni and Newfarmer (2009) note that while a repeat of the 1930s-style tariff wars is remote[4], the new form of protectionism could still play out in Depression-era style. If a few major nations favor their own industries at the expense of foreigners, invariably so will others, producing rounds of retaliation. That could choke off trade and slowdown further the global engine of growth. The IMF already predicts a 2.8 percent decline in trade in 2009.

The impact of financial protectionism on the world economy is even worse. According to Soros (2009), "When history is written, it will be recorded that — in contrast to the Great Depression — protectionism first prevailed in finance rather than trade." After the failure of Lehman Brothers in September 2008, the system broke down and was put on artificial life support. National governments in Europe and elsewhere have gone out of their way to support their banks. Among other measures, both Europe and the United States in effect guaranteed that no other important financial institution would be allowed to fail.

This step had unintended adverse consequences: many other countries, from Eastern Europe to Latin America, Africa and south-east Asia, could not offer similar guarantees. As a result, capital fled from the periphery to the center. The flight was abetted by national financial authorities at the center who encouraged banks to repatriate their capital. In the periphery countries, currencies fell, interest rates rose and credit default swap rates soared (Soros, 2009). These developments will not help in the recovery of global growth.

A second way countries protected their banks was by curtailing their cross-border lending even more than their domestic activities, deeming their exposure to foreign markets as more uncertain than their business at home. European governments, such as Britain's, have told their banks to lend consumers and businesses at home. But the more governments try to prop up local lending, the greater the urge for banks to reduce their exposure to risks elsewhere. Such national shelters inclined banks to bring assets home (Schmieding, 2009). According Britain's Prime Minister Gordon Brown, the withdrawal of banks from a number of emerging-market countries with a weak domestic-banking system is the first stage of financial mercantilism that will lead eventually to the kind of trade protectionism experienced in the past (Davis, 2009).

The third way countries implement financial protectionism is by financing fewer investments and exports with other countries. Such a policy will only curtail cross-border financial flows, thus creating a trade protectionist impact similar to that of the 1930's. It is also self-defeating because trying to maintain credit at home does not prevent an economic slump if a country's trading partners abroad cannot get the short-term finance they need to buy its exports. And if the export machine slows down, domestic investment into export-oriented industries will follow suit. (Schmieding, 2009).

A fourth way countries are currently implementing protectionism is through the very bailout packages designed to stimulate a country's economy. For example, UK banks receiving bailouts were encouraged to redirect lending toward the home market. Another example is the French plan to support banks that included conditions on lending to airlines that might cancel orders for Airbus planes. Baldwin and Evenett (2009) describe this kind of protectionism as "murky." Because of the lack of transparency, countries have used bailouts in retaliation to other countries' measures. President Sarkozy remarked: "The situation in Europe means that you cannot accuse any country of being protectionist when the Americans put up $30 billion to support their automotive industry" (Baldwin and Evenett, 2009, p. 5).

[4] According to Gamberoni and Newfarmer (2009) this is because countries are far more interdependent through supply chains, imported inputs and services. Export interests are far more powerful than before relative to pure import-competing industries. Producers for the domestic market are more reliant on imported inputs, and production chains link global markets through a web of trade in parts and components. The simple average of trade-to-GDP is today 96 percent compared to 55 percent in 1970, and parts and components trade, an indicator of supply chains, has more than doubled as a proportion of total trade.

BOX 2.1: Guide to the Causes of the Global Financial Crisis

- A prolonged period of low interest rates and easy credit led to rapid growth in low quality lending in the housing market in many countries. This caused a boom in the housing market that lent itself into an unsustainable asset price bubble.
- Global imbalances reflected in large account surpluses and deficits further contributed to the growth of international liquidity, and the search for yield added pressures on financial intermediation.
- Over the past 10 years the financial system expanded massively and created new instruments (such as securitization, credit default swaps) that appeared to offer higher rewards at lower risk. Flawed market incentives, in the form of very low interest rates, allowed the rapidly growing financial innovation boom to create large high-risk concentrations of subprime mortgage backed securities that were widely bought by many banks and financial institutions and added to their balance sheets.
- It was believed that these innovations were beneficial because they transferred and spread out banking risk to non-banking institutions.
- Regulation was "light-touch," based on the assumption that financial market discipline would root out reckless behavior and that financial innovation led to a more efficient allocation of risk, not concentrating it.
- This would have been true if these risks had been transferred to agents with well diversified portfolios. However those risks were concentrated in undiversified portfolios of large non-banking institutions such as AIG or Lehman Brothers (Dewatripont, Freixas, and Portes, 2009).
- These papers were widely traded in the secondary market, gaining their value from the secondary market sales during the housing boom.
- They were even given investment grade ratings. Institutions with substantial holdings of these securities that backed the sub-prime mortgages were also given investment grade ratings by rating agencies.
- During these developments, policymakers failed to sufficiently take into account growing macroeconomic imbalances that contributed to the buildup of systemic risks in the financial system and in housing markets. Central banks focused mainly on inflation, not on risks associated with high asset prices and increased leverage. At the same time financial supervisors were preoccupied with the formal banking sector, not with the risks building in the financial system.
- The housing bubble burst when the subprime mortgage papers — and consequently the securities that backed them — lost their value as home owners defaulted on their mortgages which they would not have got in the first place had credit been "less easy."
- Banks and other financial institutions owning the mortgage backed securities made huge losses, especially with the collapse in confidence of the credit ratings of structured securities as a basis for valuing and trading these securities (Dewatripont, Freixas, and Portes, 2009).
- Transparent markets suddenly became opaque because the financial instruments were complex. As information became scarce, markets collapsed and the "(Akerlof) no-trade equilibrium was inevitable" (Dewatripont, Freixas, and Portes, 2009, p. 2).
- A rise in credit defaults forced many governments to directly inject massive funding to save these financial institutions.
- The sharp deterioration in the equities markets undermined the balance sheets of all bank and non-bank institutions.
- At the root of the crisis was the optimism that was brought about by a long period of prosperity. This optimism led to risks in the global economy not being assessed as carefully as they should have been.

2.3 RECENT DEVELOPMENTS IN THE EGYPTIAN ECONOMY AFTER THE FINANCIAL CRISIS: JULY - DECEMBER 2008

2.3.1 Egypt is Better Placed than Many Other Countries to Confront the Global Financial Turbulence

As discussed in Section 2.1.1.1, Egypt's economy has fundamental strengths that helped it weather the direct and first round effects of the financial crisis. Direct financial channels of contagion are limited, reflecting:

(i) Strong GDP growth that left the economy in prime form just before the onset of the global turmoil.

(ii) Other long-standing factors dampening Egypt's integration in the global financial system.

These two attributes served to put Egypt in a better place than many countries to weather the global financial turbulence and worldwide recession.

Egypt's robust growth rates have been spurred by buoyant domestic demand, as shown in Figure 2.3. The advantage of domestic-led growth is that it helps reduce susceptibility to cyclical swings in the external sector. Japan is a recent example of the perils of export-dependent growth. According to Oxford Analytica (2009) Japan, once seen as relatively immune from the financial system shock in the early stages of the crisis, was the worst hit among the OECD economies from the financial crisis. The sudden collapse in Japan's economic prospects has been one of the most remarkable features of the global financial and economic crisis and has exposed the dangers of a country's extreme export dependence. In particular it revealed Japan's vulnerability to the falling external demand in China. China overtook the U.S. in 2008 as Japan's largest trading partner (because of the slump in Japanese exports to the U.S.), but this has proved to be a source of weakness rather than strength.

Second, financial sector reforms introduced and implemented in the past few years have brought about a resilient banking sector. Egypt's banking system is also underpinned by sound regulations that strictly limit banks' levels of integration with the global system and have served to avoid the toxic exposures that now weigh on many banking systems.

2.3.2 The Crisis has Exposed and Heightened Egypt's Pre-Existing Macroeconomic and Other Vulnerabilities

In Section 1.1.2 the underlying vulnerabilities of the Egyptian economy were discussed. This section explores how these macroeconomic vulnerabilities will compound the impact of the crisis and delay the economic recovery. In addition, Egypt's growing openness increased the contribution of the external sector to growth at the expense of the domestic economy during 2007-2008 (MOF, 2009a), thus increasing its vulnerability to external shocks. According to Dewatripont, Freixas, and Portes (2009, p. 1), "… a systemic crisis involves two pillars: macroeconomic fragility and contagion" — two pillars that existed in the Egyptian economy by the end of June 2008, a few months before the onset of the global financial crisis.

Following the financial crisis, the balance of risk seems to have shifted from inflation to growth, particularly private sector growth; while the sustainability of the fiscal deficit, the limited fiscal space and how to finance additional spending to support growth and the monetary/fiscal policy mix remain big problems. Contagion from the advanced economies to Egypt spread rapidly through trade and investment links.

2.3.2.1. Growth, Unemployment and Inflation

Egypt's economic slowdown began before the onset of the crisis, as early as the first quarter of 2008-2009 (July-September 2008). In an effort to combat spiraling inflation, the Central Bank pursued a tight monetary policy in 2007-2008. As a result, Egypt's economic growth slowed to 5.8 percent compared to 6.5 percent during the first quarter in 2007-2008. In addition, against the background of the financial crisis, real GDP growth further declined to 4.1 percent in the second quarter of 2008-2009 (October-December 2008), from 7.8 percent in the corresponding quarter of 2007-2008.

The global economic contraction and financial crisis will continue to affect Egypt's economy. Continued turmoil in global financial markets points to an extremely challenging growth environment in 2009 and 2010. The tight global credit conditions and slowdown experienced by all regions of the world has been compounded by erosion of investor and consumer confidence. As a result, prospects for Egypt's economy for this and next year are expected to be considerably less favorable than envisaged in June 2008, although the high contribution of domestic demand to growth provides the economy with a reasonable cushion in the short term. As a result, the worsening of the international financial conditions has affected Egypt's economy to a lesser degree than the rest of the world (IMF, 2009c). However, because external demand has recently been contributing more to growth, the economy is being affected through the external sector (international trade and foreign direct invest-

ment channels). The pass-through of the crisis from external demand to domestic demand has reduced all components of demand: lower exports, lower consumption (as lower remittances) and lower investment (lower FDI).

Chami, Hakura and Montiel (2009) report in a study of 70 countries, including 16 advanced economies and 54 developing countries that there was robust evidence that remittances have a negative effect on output growth volatility of recipient countries. Thus, the fall in remittances should precipitate impact of the crisis on poverty. This presents a hard challenge for the government, for they must resort to an already stressed and limited set of policy instruments, such as fiscal policy, to counter the resulting adverse economic and social impacts of lower remittances.

In his speech in April 2009 to the People's Assembly, Prime Minister Ahmad Nazif indicated that economic growth, as a result of these developments, will be a little over 4 percent in fiscal year 2008-2009. According to Beltone (2009a), the government's projection of 4 percent real growth for 2008-2009 could be overly optimistic given the indications of a drop in domestic and external demand growth since September 2008[5]. Prime Minister Nazif added that the outlook for 2010 is also highly uncertain, hinging critically on global and regional growth prospects, and if the global economic slowdown continues, then growth might dip below 4 percent in the 2009-2010 fiscal year.

While domestic demand comprises the lion's share of GDP growth, 2007-2008 saw an increase in the contribution of external demand to growth, thus increasing the economy's vulnerability to external shocks. The key channel for the transmission of the financial shock to the real economy has therefore been from external sources of growth, such as service remittances (Suez Canal receipts, workers remittances, tourism) and international trade. Foreign direct investment, which has played an increasingly important role in Egypt, has slowed rapidly as international investors scaled back or postponed their investment plans as financing conditions tightened. Construction activity and foreign investment are also slowing rapidly as external investors cut back and financing conditions tighten.

The slowdown in FDI will have an enormous impact on the Egyptian economy. Over the past four years Egypt had enjoyed a significant wave of investment from its Gulf neighbors as they looked to diversify their assets. In the 12-month period ending in June 2007, the six Gulf Cooperation Council (GCC) member states had poured a total of US$ 2.5 billion into Egypt for new ventures and market expansion. The United Arab Emirates, for example, has a strong presence in the country's telecom sector, following the US$ 2.9 billion purchase by Etisalat in 2007 of a mobile operator license, while the National Bank of Kuwait bought a 99.77 percent stake in Al Watany Bank of Egypt. The UAE became the third biggest foreign investor in Egypt, with investments worth US$ 2.9 billion at the end of 2008. More recently, Dubai Group acquired a 49 percent stake in an Egyptian glass manufacturer in partnership with the Cairo-based private equity firm Citadel Capital. The Kuwait Fund for Arab Economic Development (KFAED) also announced it would be significantly increasing its investments in Egypt, with a loan of US$ 105 million to the state-owned West Delta Electricity Production Company to expand a power plant in Abu Quir, about 40 km east of Alexandria. Additionally, the Libyan government announced its intention to increase its investment in the Egyptian economy up to US$ 10 billion within the next two years (OBG, 2009).

In addition, external sector data show a fall in export demand that has widened the current account deficit.

Table 2.5: ***Select Items From the Balance of Payments (in billions of US dollars).***

	2004-2005	2005-2006	2006-2007	2007-2008	Jul-Dec 2007	Jul-Dec 2008
Suez Canal	3.3	3.6	4.2	5.2	2.5	2.8
Tourism	6.4	7.2	8.2	10.8	1.5	1.5
Remittances	4.3	5	6.3	8.6	4.1	1.95
Portfolio investments	0.83	2.7	-0.94	-1.4	-1.7	-4.2
FDI	3.9	6.1	11.1	3.2	7.76	4
TOTAL	18.7	24.6	28.9	36.4	14.2	6.1

Source: MOF (2009a).

Data for the first half of the fiscal year 2008-2009, in Table 2.5, show that private remittances and FDI flows took the brunt of the shock. Private remittances were more than halved compared to July-December 2007, while FDI tumbled by nearly 50 percent. To date, there has been no decline in tourism receipts as feared. Growth in tourism receipts in the first half of 2008-2009 was stagnant compared to the previous year. The cut in discretionary spending by tourists is not evident yet because this period was the holiday peak and for which bookings had been made in advance. According to the Ministry of Tourism, data for July-December 2009 will better reflect the magnitude of the impact on the industry. In the meantime Suez Canal receipts showed some increase.

[5] Data not available to author.

The overall impact is that total current receipts from these sectors has declined by more than 50 percent, from US$ 14.2 billion during July-December 2007 to US$ 6.1 billion during July-December 2008. The significant impact on workers' remittances reflects the extent of the crisis in the Gulf. The fall in FDI flows will affect investments in construction and buildings, which contributed some 0.58 percentage points of private sector growth in 2007-2008. They will also impact real estate investments whose contribution to private demand jumped from 0.15 percentage points in 2006-2007 to 0.83 percentage points in 2007-2008. Together these two sectors contribute 1.4 percentage points of growth. In other words, a 50 percent fall in FDI flows alone could cost growth 0.7 percentage points of private domestic demand. There is a risk that the strong contraction of FDI will need to be offset by a larger increase in public spending. According to a World Bank report in 2008, Egypt's growth correlates with growth in OECD countries; for every percentage point increase in growth in OECD countries, there is a 1.25 percentage point increase in Egypt's output. As growth in OECD countries cools down, Egypt's growth rates could retreat by more than a proportionate amount through the external sector channel. Because of the magnitude of the FDI loss, it will be difficult to offset it all by public expenditure without incurring a large current account deficit.

Further declines in the rate of growth are expected to come from agriculture, as the fall in global agricultural prices may cause the contribution of agriculture to growth to retreat further this year.

Portfolio outflows have accelerated. Data for July-December 2008 show that outflows during these six months are four times the outflows of the entire year of 2007-2008 (Table 2.5).

International trade will be a major channel for economic slowdown. Manufacturing constitutes some 1.15 percentage points of growth. Data reflecting the full brunt of the fall in external demand on the growth of the industry is not available. However, garment exports in particular could face pressure due to sharply lower retail demand in the United States and the European Union. Growth of the trade deficit, shown in Table 2.6, slowed down during July-December 2008, reflecting largely a halving in exports growth, while imports growth retreated marginally, despite the drop in FDI and in food and energy prices. Any significant slowdown in the export sector is likely to weigh heavily as well on the domestic economy through a reduction in demand for services, transport and construction.

Table 2.6: *Select Items from the Current Account (in billions of US dollars).*

	2004-2005	2005-2006	2006-2007	2007-2008	Jul-Dec 2007	Jul-Dec 2008
Current account balance	2.9	1.8	2.3	0.9	-0.3	-2.5
Of which the trade balance	-6.4	-7.2	-8.2	-10.8	-11.3	-14.6
% change in trade balance	-33.3	-15.4	-35.8	-43.6	-74	-29.2
% change in exports	31.4	34.1	18.9	33.6	22.5	12.6
% change in imports	32.2	25.6	(26	37.6	41	39.3

Source: MOF (2009a).

Unemployment, has marginally declined from 8.9 percent to 8.8 percent between 2006-2007 and 2007-2008 (IMF 2009c), despite strong growth during these two years, and will rise, as announced by Prime Minister Ahmad Nazif in his April speech to parliament, as growth slows down to 4 percent or below as projected (see 2.3.2.2 below). The ECR 2008 discussed in detail the reasons behind the catatonic movement in unemployment rates. Egypt's macroeconomic strategy gives incentives to manufacturing and other high-technology capital intensive industries that do not absorb Egypt's unskilled labor force. Slower growth will invariably increase unemployment, and impact incomes and poverty. However, lower inflation rates will also raise real incomes.

Inflation is expected to continue to moderate during 2009, aided by soft world food and fuel prices. But structural impediments in the economy are maintaining local food prices at levels higher than those consistent with international commodity prices. According to CAPMAS (2009), urban headline inflation in Egypt has continued to decline on an annual basis, registering 12.1 percent in March 2009, compared to 13.5 percent in February and a peak of 23.7 percent in August 2008. Annual inflation also declined to 11.6 percent in March, from 14.2 percent in February. Annual food inflation, previously one of the main culprits for the spike in inflation in 2008, also declined on the national, urban and rural levels, registering 12.8 percent in March, compared to 14.4 percent in February.

Since February 2009, however, the monthly changes in inflation continue to reflect inflationary pressures emanating from food price changes. Domestic food prices have recently been higher, despite the decline in international food prices. On a monthly basis, both urban inflation and food inflation picked up: Urban

monthly inflation rose by 1.25 percent in March 2009, compared to a monthly increment of 1.03 percent in February. Food inflation rose by 2.5 percent in March from February 2009, compared to a monthly increment of 2.4 percent in February.

The rise in prices of dairy products was one of the reasons behind the rise in monthly inflation. Dairy producers have been negotiating with the government to receive a subsidy to reduce their prices, given their higher cost of production, compared to imported products. To the extent that this issue has not been resolved yet, dairy product prices could continue to be above international prices — which have been declining since mid-2008 — through April. Demand on food products is healthy in Egypt, and vendors might not be inclined to reduce their prices (Beltone, 2009b). High food prices risk increasing poverty as food comprises some 60-80 percent of the incomes of the poor (Lustig, 2008).

Despite the higher food prices on a monthly basis, the strong base effect should lead to the downward trend in annual inflation, until inflation reaches single digit levels by mid-2009 and should fluctuate below 10 percent until the end of 2009 and early 2010. Average inflation should go down to between 6 -7 percent during the same period, and should rebound in 2010 as international commodity prices pick up (Beltone, 2009b).

However, many of the fundamental forces behind the price surge in 2007-2008 are still in effect and could once more cause a spike in prices after the global economy recovers. Demand from emerging and developing economies will recover. In the oil market, the constraints underpinning the sluggish supply response to high prices could resume, which would again put upward pressure on prices. (IMF, 2008).

2.3.2.2. Fiscal Policy and Egypt's Stimulus Package

According to the Ministry of Finance (2009a), the budget deficit will be, as projected, 6.9 percent in June 2009, including the fiscal stimulus package (see Table 2.7). This is a downward revision from a previously indicated deficit of 7.2 percent, and could imply a growth rate lower than 4 percent for 2008-2009 (Beltone, 2009a).

In order to stimulate economic growth, the Ministry of Finance is spending an additional LE 13.5 billion or 1.34 percent of GDP by June 2009 (Table 2.7). The recently announced stimulus plan aims to support growth, boost public investment by front-loading existing projects and simplifying budget execution procedures, ensuring social security and accelerating poverty reduction.

To evaluate the package in terms of magnitude and effectiveness, a careful look at the new expenditure items of the budget and the announced fiscal package is in order.

In his speech to Parliament in April, Prime Minister Ahmad Nazif announced that the budget deficit is projected to widen to 8.5 percent of GDP in June 2010. Revenues are expected to drop by 22 percent to LE 224 billion as the budget incurs tax revenue losses from output decline. Total expenditures will drop by 10 percent to LE 323 billion. Spending on subsidies will fall to LE 73 billion from LE 132 billion, due to lower commodity prices. The 45 percent saving from subsidies was used to raise wages by 13 percent in 2009-2010, while spending on health and education will be increased by 16 percent and 18 percent respectively.

BOX 2.2: Public Debt Schedule

The Ministry of Finance announced its public debt schedule for April-June 2009, with issues totaling LE 93 billion in treasury securities, compared to LE 100 billion in the preceding quarter. The ministry plans on issuing LE 93 billion, with LE 53 billion worth of securities maturing, rendering net new offerings of LE 40 billion in the last quarter of the fiscal year. This compares with net new offerings of LE 31.5 billion in January-March 2009.

The released schedule also indicates the ministry is planning on issuing more treasury bonds during April-June 2009, worth LE 24 billion, compared to LE 12 billion in January-March 2009. It also plans to issue one-year maturities in April-June 2009 worth LE 21 billion, versus LE 17.5 billion in the preceding quarter. It will also reduce issuances of three-months, six-months and nine-months during the last quarter, thus lengthening the maturity of the yield curve.

Source: Ministry of Finance

Given that Egypt must make additional public expenditures to stimulate growth and create jobs, and given that it already has a high budget deficit and limited fiscal space as discussed earlier, the gain from the reduction in subsidies should not have been spent on wage increases, and should have been better prioritized. The increase in wages also came at a time when inflation is going down and real incomes are increasing.

According to an IMF report (Spilimbergo et al, 2009), in order to satisfy the objectives of longer term growth and stability, a fiscal stimulus package must focus on measures that create employment, are effective, well targeted and temporary, such as enhancing the social safety net and accelerating existing high quality public investment projects. For a fiscal stimulus package to be effective in terms of increasing output and creating jobs, it must have the following characteristics (Spilimbergo et al, 2009, IMF report):

- Timely (as there is an urgent need for action),
- Large (because the drop in demand is large),
- Lasting (as the recession will likely last for some time),
- Contingent (to indicate that further action will be taken, if needed),
- Sustainable (to avoid debt explosion in the long run and adverse effects in the short run), and
- Diverse (8th European Regional Meeting, 2009).

A fiscal stimulus package must also be diverse, targeting several sectors of the economy, as there is uncertainty regarding which measures will be most effective. It is difficult to calculate the precise magnitude of the stimulus package because many countries are already implementing expenditures.

The speed and duration implementation, not the size of the package, will have significant consequences for growth and employment. Measures to support demand must aim to produce immediate results and be of limited duration. One type of stimulus that could be implemented immediately would be automatic stabilizers such as raising the level or duration of unemployment benefits, or widening eligibility for benefits, expanding welfare payments or social safety nets. This type of measure has the advantage of being targeted at disadvantaged groups and the fiscal cost of such measures automatically declines when poverty levels fall back to the pre-crisis levels.

Expenditure on public works programs or social expenditures take longer to implement. Speed of implementation can be accelerated by focusing attention on upgrading maintenance and repair of existing physical infrastructure or bringing forward construction activities and social expenditure programs. In addition, there can be acceleration of public transport projects for which design and building permissions have been obtained. Another option is that of front-loading investment projects and starting new ones if the downturn continues.

Employment-intensive measures such as renovation of buildings could employ small businesses to carry out this kind work, which would also create employment for the lower income groups who are more likely to spend the extra income, not save it.

Public expenditure is more effective than tax cuts because of the potential to boost the economy in the long term. Spending on education, research and development, and other labor-intensive social services such as health will increase the productivity of the economy in the longer term, with implications for the competitiveness of the economy. Tax cuts will lead to higher disposable income but it is unlikely that all of the increase in income will be spent immediately as most people will save a portion of the tax cut, saving purchases until the economic climate improves. Reductions in corporate tax rates, dividends and capital gains taxes, providing unconditional subsidies to firms, or the introduction of special incentives such as accelerated depreciation for enterprises will reduce companies' debt and improve their balance sheets, but will not increase investment expenditure, aggregate demand or employment. Thus any social spending will have a larger impact on output and employment than general tax cuts. Raising the disposable income of the poor through targeted cuts to them (such as earned tax credits and lump-sum tax rates targeted at low-income groups) will allow them to spend their money and thus raise aggregate demand. However, consideration should be given to support enterprises facing large employment reductions.

Table 2.7: *Egypt's Fiscal Stimulus Package (in LE million).*

TOTAL VALUE OF PACKAGE	**13,532**	**(1+2)**
Investment Expenditure	**10,832**	**..... 1**
In general budget sector	**10,232**	
• *Potable water and sewage projects*	7,030	
• *Building roads and bridges*	1,000	
• *Domestic development projects in various governorates*	1,000	
• *Building basic health care centers*	400	
• *Building schools*	150	
• *Others*	652	
In economic authorities	**600**	
• *Improving the efficiency of railways*	400	
• *Execution of infrastructure projects for the development of East Port-Said port*	50	
• *Improving the capacity of Red Sea ports*	150	
Current Expenditure (In Subsidies)	**2,700**	**..... 2**
• *Increasing competitiveness of Egyptian exports*	2,100	
• *Supporting industrial zones in the Delta*	400	
• *Supporting infrastructure for internal trade*	200	

Source: Ministry of Finance

Looking at Egypt's fiscal package (Table 2.7), 20 percent of the stimulus is current spending, the bulk of which is in the form of tax benefits and subsidies to enterprises. It is not directed to the lower income groups who are more likely to spend the additional income, but to corporations who are more likely to save it. Only LE 400 million or 15 percent of these current expenditures are being spent on maintaining employment in these enterprises. While the measures in the package were mainly aimed at propping up demand through tax breaks and subsidies to employment, and at providing assistance to the unemployed, they do not reduce the short-term benefit of the fiscal stimulus. But they do diminish its long-term impact because the package will not contribute to higher growth.

Otherwise the package satisfies other conditions set by the IMF report (Spilimbergo et al, 2009, IMF report). The bulk of the package (LE 10.8 million) has been directed to sustainable physical infrastructure spending that creates jobs and that will have lasting effects on domestic productivity — and hence competitiveness — in the longer term. In the face of sliding world demand, this spending is critical if Egypt is to protect its export market shares. The scope for increasing the competitiveness of Egypt is large, and policies directed at improving the availability of high quality infrastructure that serves to lower the transaction cost of private investment is commendable. The spending was directed to existing projects that were front-loaded, so the impact is likely to be timely.

However, the increase in the wage bill is not a sustainable stimulus. The package could also be more diverse, including other spending to improve the longer term competitiveness of the economy, by improving the business environment and the quality of labor. In addition, the current spending directed to supporting enterprises should have been directed to lower income groups or projects that employ small enterprises. These two target groups are more likely to spend the money and stimulate domestic demand, while the bigger enterprises are more likely to save it.

The size of the package (1.3 percent of GDP) may not be commensurate with the drop in demand, especially with public debt on a stable decreasing path (MOF, 2009a). Economic growth, including the impact of the fiscal stimulus package, will be 4 percent by June 2009. The minimum growth rate consistent with a constant unemployment rate is 5.5 percent (Favero, Giavazzi and Missale, 2009). In a recessionary global environment there should be no concerns about inflation or fears about crowding out the private sector. On the contrary, public investment will crowd in private investments. But while a larger fiscal stimulus might seem warranted in the face of fears that recession could become deeper and longer, both inflation and interest rates in Egypt are already high. The short-term economic stimulus must not jeopardize medium-term economic stability, which remains critical for Egypt to resume robust economic growth and make progress in poverty reduction.

Another "stimulus" measure that should be noted here is that the Ministry of Finance has postponed the introduction of the value-added tax in order not to undermine private consumption spending.

The financial crisis has many negative implications for the sustainability of the fiscal deficit. The fiscal consolidation plan announced by the Ministry of Finance in 2006 aimed at reducing the budget deficit to 3 percent of GDP by June 2012. Before the financial crisis hit the world and Egypt, domestic debt was expected to go down steadily to reach 48 percent of GDP by 2012. Since then GDP growth estimates have declined dramatically, fiscal spending has to go up to stimulate economic activity, and the question becomes whether the fiscal deficit would be sustainable under the new deteriorating macroeconomic conditions. More importantly, the questions become where will additional sustainable spending come from, given the highly rigid budget and tight fiscal space? How will the additional spending be financed, without increasing public debt unsustainably? An increase in the budget deficit will inevitably increase public debt. This is a challenging test for the monetary/fiscal policy mix.

2.3.2.3. Monetary/ Fiscal Policy Mix

As discussed in detail above, the government and Central Bank have taken measures to mitigate the impact of the financial crisis, including the adoption of a fiscal stimulus plan and marginal easing of monetary policy. However, the mix of policies that needs to be adopted is challenging for a number of reasons: (i) fiscal space is limited; (ii) inflation is still relatively high and while subsiding lately, there are upward pressures on food prices (see Section 3.21.1); (iii) nominal interest rates are high but real rates are negative; and (iv) growth is slowing down quickly and needs a boost from expansionary fiscal policy and monetary policies.

In such a slow-growth, high-inflation and interest rate environment, coupled with pressures for the depreciation of the pound, any fiscal spending will entail more public debt and further widening of the current account deficit (in view of the decline in all current account receipts, as shown in the previous section). The question for the monetary/policy mix is how can Egypt finance the current account deficit in the face of the ongoing decline in current receipts without incurring external or domestic borrowing?

So far the Central bank has financed the widening deficit through gradually depleting Net International Reserves (NIRs) (Table 2.8). Egypt's NIRs fell in March 2009 to US$ 32.2 billion, from US$ 33.1 billion in February 2009, and from its peak of US$ 35.03 billion in October 2008 (MOF, 2009a). The NIRs loss in March 2009 is the biggest since NIRs started to decline in October 2008 and the biggest decline since June 1996.

The Egyptian pound weakened to LE 5.73 per US dollar, from 5.64 per US dollar. The steady fall of NIRs since October 2008 was largely in response to foreign exchange market intervention to prevent the devaluation of the pound. The loss came from lower capital inflows following the financial crisis, lower returns on the reserves in international financial markets, and additional investment outflows due to foreigners' divesting in fixed-income and equity markets (Beltone, 2009b). As confidence dipped with the emergence of depreciation pressures, risk perception rose, prompting foreign investors to reduce their exposure to Egypt by selling treasury bonds. As a result, portfolio outflows started taking place even before the onset of the financial crisis (Table 2.5).

As the current account widens, some depreciation could help finance the growing deficit in combination with the depletion of reserves. While depreciation creates potential inflationary pressure, the real debt falls, the burden of debt is somewhat eroded and the depreciation facilitates current account adjustment (Dewatripont, Freixas, and Portes, 2009). Given that Egypt has very low tolerance for borrowing from abroad to stabilize balance of payments, it would be better to split the burden of financing the current account between NIRs depletion and a depreciation of the pound. If the depreciation bears the full burden of financing the current account, the inflationary impact would be large given the lax fiscal stance needed to implement the fiscal stimulus package. This would lead to higher interest rates anyway and credibility problems.

Favero, Giavazzi and Missale (2009) add that since only partial depreciation would be allowed to take place, the interest rate must remain high. In other words the optimal response is a mix of expansionary fiscal and contractionary monetary policy. First, expansionary fiscal policy brings employment back to its potential level, and second, tight monetary policy reduces the capital outflows that would otherwise lead to an unsustainable exchange rate regime with repercussions on inflation and credibility. A weaker pound would help ward off pressures to increase the public debt, and at the same time allow the Central Bank to keep interest rates high in the face of the mixed movements in inflation. It would also support external sector competiveness. There is a fear that given the confidence crisis and the aversion to risk that has partially infected Egypt, an expansionary monetary stance might not stimulate the economy. Hindsight from India's experience — an economy similar to Egypt in many ways — of an accommodative monetary policy has failed to revive the economy. Successive interest rate cuts did not lead to cheaper lending as had been hoped. Banks remained reticent to lower lending rates, and small and medium sized businesses complained of a severe stoppage of credit (Lamont, 2009, Financial Times).

Because external debt indicators are low, a second scenario would be to split the burden of financing the current account between depreciation, a contractionary monetary policy and the depletion of reserves.

Table 2.8: *Net International Reserves and Net Foreign Assets (June-December 2008)*

$US Billions	2008						
	Jun.	Jul.	Aug.	Sep.	Oct.	Nov.	Dec.
Net International Reserves	34.6	34.7	34.8	35.0	35.0	34.4	34.1
Net Foreign Assets	56.8	55.8	54.7	50.6	47.0	44.7	45.0

Source: CBE

2.3.3 The Crisis has also Exposed Policy weaknesses such as the Resort to Protectionist Measures

In response to falling global steel prices and strong competition from imports, Egypt's steel producers announced another round of price cuts in early March, averaging LE 300-550 (US$ 55-100) per ton. Manufactures lowered their ex-factory price from LE 3,400 per ton to LE 3,050 per ton, less than half the price in mid-2008. Falling steel prices reflect the global reduction in construction activity. Nevertheless, Egyptian producers continue to charge higher prices than their competitors abroad. This is partly a result of the relative strength of the domestic construction sector, with building activity remaining buoyant in Egypt. Moreover, the market is dominated by one firm and the other firms tend to follow. However, Egyptian steel firms face strong competition from importers, notably from Turkey and Ukraine, where large currency depreciations have led to a concomitant reduction in their export prices.

The government has responded to lobbying from within the domestic steel industry by imposing a 10 percent import tariff on cold-rolled, flat-tin sheets, on top of existing duties, to stabilize the local market price. This follows a similar move to put anti-dumping duties of LE 500 per ton on imports of white sugar, in addition to the existing 10 percent tariff, to protect the local sugar industry from unfairly priced imports. There have been calls for similar protection for Egypt's cotton sector, involving subsidies and a temporary ban on imports. Cotton production has fallen by around a half during the current growing season owing to high input costs, falling global demand and higher prices for alternative crops such as wheat, corn and vegetables. In late March, the Minister of Trade and Industry announced an extension to the export ban on rice that will remain in effect until October 1, 2009. The ban was introduced in April 2008 for a period of one year as a measure to boost supply and lower prices on the domestic market. Rice export fees were also increased from LE 300 to LE 1,000 for a few authorized exporters.

2.4 OUTLOOK RISKS AND POLICY CHALLENGES FOR EGYPT: CONCLUDING REMARKS

The financial crisis is putting severe strains on the four pre-existing vulnerabilities of the Egyptian economy discussed in Section 1.2. The economy has faced for a number of years the risks of a large fiscal deficit, limited fiscal space and rising inflation. Egypt's strong economic fundamentals are also being stress-tested by the global financial crisis as world growth slows down, pulling down the Egyptian economy with it. The immediate challenge is to adopt adequate policies in response to the global crisis, while the medium term challenge is to help the economy to emerge stronger, more resilient and more competitive.

As economic activity slows down, the fiscal stance is accommodative to support economic growth, but the expansionary policy is constrained by a high fiscal deficit, tight fiscal space and high inflation. It would be crucial for the government to carefully balance growth and macro-stability objectives for 2009-2010 by (i) adopting the appropriate mix of macroeconomic and financial policies to address near term vulnerabilities; (ii) strengthening government policy choices; and (iii) implementing further structural reforms, in particular those relating to the budget, the diversification of the economy and the labor market in order to strengthen the competitiveness of the economy and its ability to weather future shocks.

In the slow-growth, high-inflation and interest rate environment of the Egyptian economy, coupled with pressures for the depreciation of the pound, any fiscal spending will increase public debt and further widen the current account deficit (in view of the decline in all current account receipts, as shown in the previous section). The question for the monetary/policy mix is how can Egypt expand fiscal spending to spur economic growth and can it finance the current account deficit in the face of the ongoing decline in current receipts without incurring inflation or borrowing (external or domestic)?

In the meantime, Egypt's economic outlook has deteriorated reflecting the global financial turmoil and slowing growth. As global demand continues to slacken, Egypt's healthy growth of recent years is expected to decelerate markedly in 2008-2009, significantly below the earlier projections of 7.2 percent. A growth deceleration to about 4 percent in June 2009 was announced by the Prime Minister in April 2009.

The uncertainties surrounding the outlook of Egypt's economic growth are compounded by the continued weakness in the global environment, despite huge fiscal spending by the US and Europe. Worldwide confidence is low, and the expectations of a global recession are prolonged. The IMF projects the deep global slowdown to continue through 2010 (IMF Survey 2009a); 2009b). A deeper and more prolonged downturn[6] than expected could worsen Egypt's growth prospects, especially in the face of a tight fiscal space that will not give much room for large fiscal spending to support domestic demand and growth. Low short-term external debt, the insulated banking system and a relatively strong balance of payments provide some protection. However, lower exports, Suez Canal receipts and private remittances, especially if combined with reduced capital inflows stemming from deteriorating global financial conditions or investor sentiment, could put more pressure on reserves and the exchange rate.

Egypt's economic recovery could therefore be delayed until 2010-2011, after the rest of the world has recovered[7] . Moreover, the pick up in growth will be relatively slow. The period of time it would take for the government's spending on investment projects to have an effect on the economy could vary with the degree of labor-intensity of the projects and the pace with which the government incurs its fiscal stimulus packages. Real GDP growth could dip to as low as 2.4 percent in 2009-2010 (Beltone, 2009a).

The Ministry of Finance has maintained its expansionary fiscal stance to support domestic demand. Nevertheless, economic growth is expected to tumble from 7.2 percent in June 2008 to 4 percent in June 2009. The decline in economic activity combined with the expected decline in remittances will result in a reduction in disposable household incomes that threatens to reverse much of the gains in poverty reduction achieved in recent years. The revised budget for 2009-2010 should therefore be formulated with a view to create the fiscal space necessary for contingent actions that may become necessary to help ease economic challenges to the population. This will

[6] See for example WEO (2009) "Market conditions are starting to respond to … policy actions, but even with their rapid implementation, financial stress is likely to be deeper and more protracted than envisaged in the October 2008 WEO". Also BMI (2009), "we [the UK] remain deep in contraction territory with recovery still looking some way off". And according to Global Insight (2009) "… the full impact on the real economy has yet to be felt. There is little doubt that the economic outlook will get worse - possibly much worse - before it gets better."

[7] The G-20 communiqué of April 2, 2009 announced, based on IMF forecasts, that global growth will resume in 2010 and could go to over 2 percent at the end of 2010.

be challenging in light of likely shortfalls in revenue in fiscal year 2009, and the fact that revenue prospects are likely to be very weak in fiscal year 2010, as well as future years without new changes in tax policy and revenue administration.

In addition, there is little scope for tax reductions given the relatively low income tax rates (20 percent). The room for a fiscal stimulus is also limited, given the tight fiscal space. Egypt cannot afford a big stimulus bill. With little fiscal space or scope for fiscal expansion, Egypt risks becoming a free rider, relying on the spillover effects of strong neighbors, thus delaying its recovery.

Given the limited scope for fiscal spending, any increase in government expenditure driven by the wage bill will push the deficit above its long-term sustainable level and will limit the implementation of investment spending that increases the productivity of the economy down the road. Increases in current spending can pose risks for fiscal sustainability, macroeconomic stability and for competitiveness, if the wage increase extends to the rest of the economy.

Egypt can sustain a large fiscal deficit in the short term as long as its balance of payments can afford it. However, we have seen that the current account is quickly deteriorating. The crisis has thus underscored the need to implement longer term structural reforms, in addition to short term "fire-fighting" in the form of a fiscal stimulus to stimulate growth. Fiscal policy over the medium term must be guided by a firm commitment to maintain a sustainable level of public debt and to reinforce public financial management to ensure the efficiency of public spending. In particular, it will be important to ensure that the planned increase in infrastructure spending continues to be financed on a sustainable basis and contributes to lifting Egypt's long-term growth potential. This will require more scrutiny over expenditure quality with a priority toward capital expenditure, improving public infrastructure and developing human capital. Contingency plans should be developed to reduce public spending in the medium term if the global downturn persists beyond 2010.

The impact of additional fiscal spending on inflation could be limited by using a flexible exchange rate, and a mix of expansionary fiscal and contractionary monetary policy. The Central Bank and Ministry of Finance should assess how the recent monetary easing and increased fiscal spending will feed through the economy before relaxing monetary conditions any further. Further interest rate cuts might not be passed on to economic growth and could only serve to create unnecessary depreciation and inflationary pressures. Given the revenue outlook, too much emphasis on increasing growth at the expense of long-term macroeconomic stability could have negative consequences.

Longer-term reforms should address the improvement of the business climate and the implementation of labor-market reforms, including offering support and assistance to workers in the process of reacting to economic evolution. Improved education and training helps workers keep up with technological advances and to upgrade skills. Strengthening social protection measures, such as more effective and targeted unemployment benefits, will ease the transition to stronger growth rates and encourage long-term skill upgrading.

Egypt can no longer afford to wait to improve competitiveness. Reforms should also address the diversification of the economy. Private consumption will no longer drive growth as it has in the past. In the future, Egypt will have to rely more on industry and its services sector to generate jobs and growth. To do this, the economy must improve productivity and lower costs. Ambitious labor and product market reforms are key to tapping new sources of growth.

The financial crisis has shown that with increased globalization, there are huge economic benefits to be reaped through regional and international economic integration, but also risks that need to be mitigated. These longer-term reforms will help improve Egypt's long-term competitiveness and mitigate future risks.

Managing these challenges will enable the Egyptian economy to emerge stronger and more resilient from this exceptionally difficult period. It will be a key near-term test for the government to contain the adverse impact of the crisis on growth and poverty, while preserving the hard-won gains of recent years.

ENCC FRAMEWORK FOR GREATER INTERNATIONAL COMPETITIVENESS

1. Connectivity

Piece-meal reform has run its course. Future national progress in international competitiveness will require a fully synchronised approach where all of Egypt's resources are effectively applied in support of a unified vision and strategy for development. Great strides in international competitiveness can result from increased connectivity. Substantive gains in efficiency can result from adopting a Team Egypt approach to future economic policy and implementation. Government now operates in a networked world, which demands innovative solutions and coordinated action, by both the public and private sectors. The complexity of this environment means there is a distinct advantage in working together for mutual benefit. In responding to the challenge, government needs to act as a single entity, creating an extended, integrated enterprise, especially as experienced by customers and citizens.

Clear vision, common purpose, connected government, enhanced dialog with the private sector and the community, and a framework for cooperation will enable government, business and other agencies to forge new, more connected, more holistic and effective ways of working together. Connecting the drivers of economic development with one another and with the necessary checks and balances to safeguard society is Egypt's challenge going forward. Connectivity can give a quantum boost to competitiveness and provide the basis for balanced growth, where everybody wins. Besides, it's no longer optional — Egypt's competitors are already doing it. ***Cont'd page 99***

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Egyptian Agriculture Competitiveness: New Opportunities and Future Prospects

Amira El-Adawi &
Tobias Bandel

While the global financial crisis has depressed commodity prices, adversely affecting the exports of developing countries like Egypt, other international developments have led to the creation of new opportunities for one sector in particular, agriculture. Growing concern over food security and climate change, both of which can be addressed through agriculture development, have given Egypt even more reasons to focus on boosting the competitiveness of the sector.

Egypt's Agriculture Transformation Strategy aims to capitalize on these new opportunities and build on the country's existing natural resource comparative advantage. Taking productivity and value added as its cornerstones, the strategy seeks to overcome major challenges — including low labor productivity, land fragmentation and inefficient resource use — to generate genuine competitive advantage for Egyptian agriculture. With the appropriate reforms the agriculture sector has the potential to double its growth rate, create 910,000 new jobs and generate LE 150 billion in sector investments over the next 12-15 years.

Sustainable agriculture is another focal area for Egypt. With an emphasis on resource conservation and pollution reduction, organic farming techniques can be cost effective as well as environmentally conscious. They also justify price premiums in European markets where demand for organic produce is on the rise.
These issues among other salient concerns within Egypt's agriculture sector are discussed in more detail in this chapter.

3.1 OVERVIEW OF THE GLOBAL AGRICULTURE SECTOR

Until recently, agriculture suffered from a decline in the perception of its importance as a driver of economic development. This phenomenon was more evident in developed economies as the shift to industrialization and service-based industries took place more rapidly than in emerging economies. The decline of the agriculture sector can be attributed to a number of factors. One such factor is the relatively low and declining returns realized on agriculture investments as opposed to other sectors, limiting the sector's ability to spur economic growth.

Trade barriers further hindered countries' ability to depend on agriculture as an engine of economic growth. Another driver of the decline is associated with the high level of inherent risk within the sector resulting from the volatility and cyclicality in agriculture crop prices and unpredictable weather conditions, which lead to reduced interest and investment in the sector. Finally, the lack of interest in the sector from high-caliber talent served to impede innovation and modernization in the sector. The combination of these factors, among others, culminated in the declining relevance of the agriculture sector as an engine for economic growth over the past few decades.

However, the recent rise in crop prices and concern for food security has spurred a new-found interest in the agriculture sector. This rise can be partially attributed to historically flat agriculture production rates that were suddenly met by a steep and unanticipated rise in food demand. Growth in demand for food is mainly fuelled by growing incomes in heavily-populated emerging economies, such as China and India. It is also fuelled by the coupling of the agriculture sector with the energy industry, instigated by the use of agriculture produce as an alternative source of energy. As a result of these significant changes in the agriculture sector, the world became acutely aware of the impact these changes will have on food security, thus stimulating the international debate about an imminent global food security crisis.

This monumental shift in the agriculture landscape represents a clear opportunity for countries that have a sizable agriculture sector and the necessary resources to respond to shifts in the international market. The global realization of agriculture's role in addressing food security and the global energy challenge is an opportunity that Egypt is well positioned to capitalize on. Egypt's agriculture sector can become both a driver of economic development and a generator of high returns (higher Gross Domestic Product, increased income for small farmers, etc.). Hence there is a strong economic rationale for investing in the improvement of the sector fundamentals in order to enhance its performance in light of this opportunity. Furthermore, emerging economies, such as Egypt, are facing the brunt of the current food crisis, thus developing their agriculture sectors and increasing agricultural food production is an effective tool to address both the current food security crisis as well as the elevation of the agriculture sector's contribution to the economy.

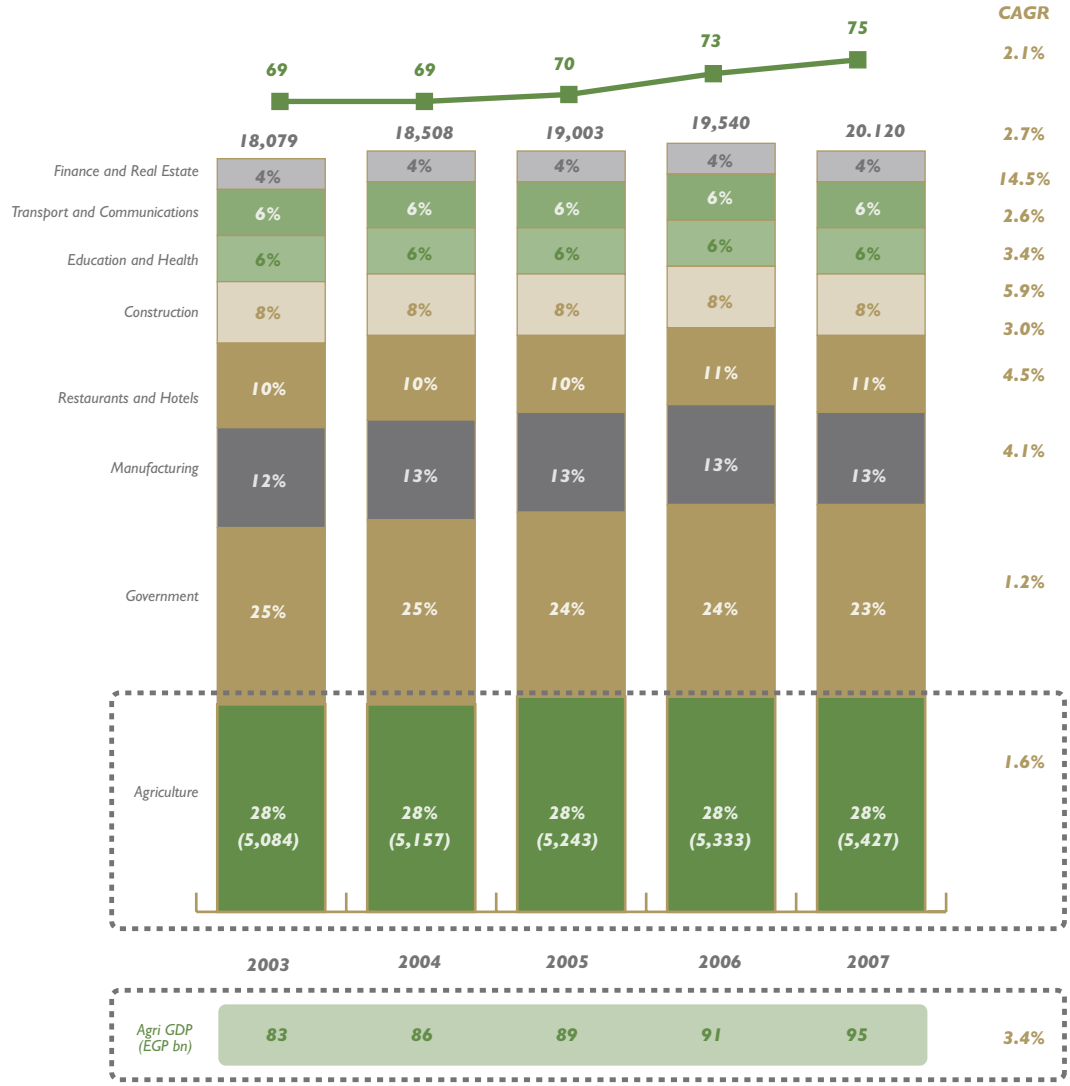
3.1.1 Overview of Egypt's Agricultural Sector in Comparison to Other Agricultural Economies

Egypt's agriculture sector is a vital and integral component of the country's economic fabric. In 2007, the sector employed more than 27 percent of the work force and generated approximately 15 percent of the country's Gross Domestic Product (GDP). Despite its significant economic contribution, the sector's share of national investments has been steadily declining in recent years, reaching 5 percent in 2007, down from 10 percent in 2004[1]. The decline in investment was driven mainly by a sharp drop in public spending, partially mitigated by an increase in private sector investments. This compares starkly to the rising levels of investment allocated towards the manufacturing sector, for example, which grew from 11 percent in 2003, to reach 27 percent of total national investment in 2007[2].

On the external front, Egypt's national trade deficit stood at approximately LE 70 billion in 2006, with agriculture contributing 17 percent to the total deficit[3]. However, closer analysis reveals an improvement in the agricultural trade balance over the past few years, due to an impressive 17 percent annual growth rate in export value, relative to a much slower 2 percent growth in imports. Export growth has been driven by a strong rise in global demand for higher value crops, with the European Union representing over a third of Egypt's agriculture commodities destination markets[4].

[1] Egyptian Ministry of Economic Development (www.mop.gov.eg/investment.htm) (2008)
[2] Ibid
[3] Egyptian Economic Monitor (Ministry of Finance 2007)
[4] Ibid

FIGURE 3.1: *EGYPTIAN EMPLOYMENT BY SECTOR (IN THOUSANDS)*



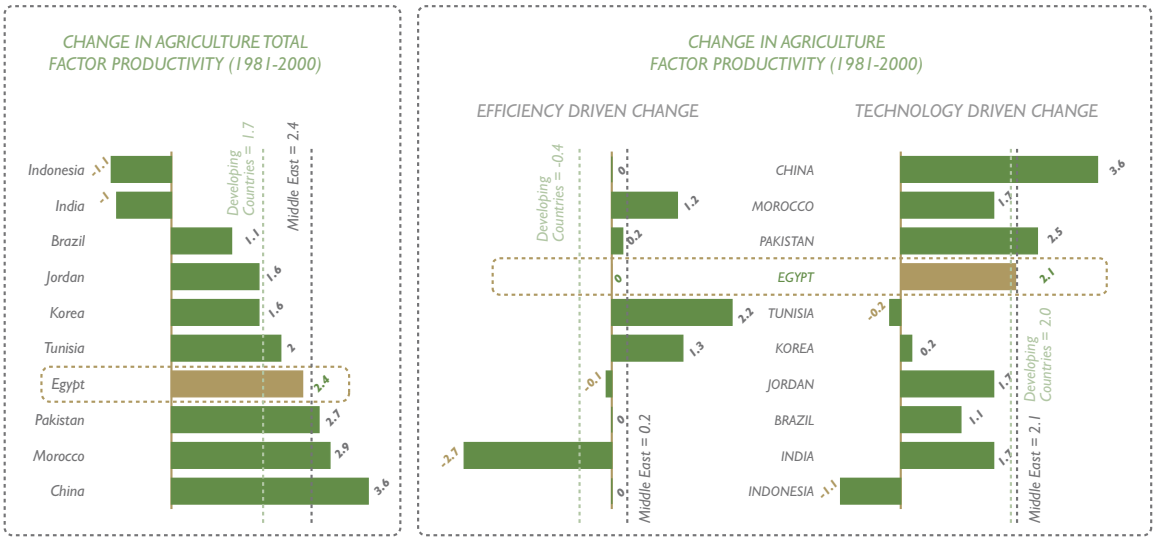
Source: Egyptian Ministry of Economic Development

Egypt's agriculture sector is plagued by low labor productivity, relative to both international benchmarks as well as other domestic sectors. According to the Food and Agriculture Organization (FAO), Egypt's agriculture sector's total factor productivity has undergone limited improvement from 1981-2000, driven almost entirely by minimal technological improvements, with no registered change in efficiency. A multitude of interrelated factors contribute to the sectors depressed labor productivity. One such factor is the sheer size of the labor force. The agriculture sector employs a larger portion of the workforce than any other sector in the economy (27 percent of the workforce in 2007), exceeding 5.5 million workers. The magnitude of the workforce alone exerts significant downward pressure on labor productivity ratios. Another factor is wage levels in the sector. In general, average wages in Egypt fall well below international benchmark country levels. More specifically, agriculture wages are particularly lagging behind those of other countries as well as behind those of other sectors within the Egyptian economy, such as construction and manufacturing. The relatively low wage levels in the sector can be partially attributed to lagging education levels relative to benchmark countries. Domestically, it can be attributed to a combination of

factors such as lower secondary school enrolment in rural agricultural areas, the sectors receipt of a declining share of the country's educated workforce, as well as the sharp fall in government spending on extension services. Another significant factor contributing to low labor productivity is the prevalence of land fragmentation in the sector. Land fragmentation is severe, with Egypt currently ranking seventh worldwide in severity, and represents an obstacle to sector modernization and farmer training. Moreover, the small land plot sizes hinder the ability of farmers to deploy machinery in the field in order to enhance productivity, hence exerting increased downward pressure on overall labor productivity.

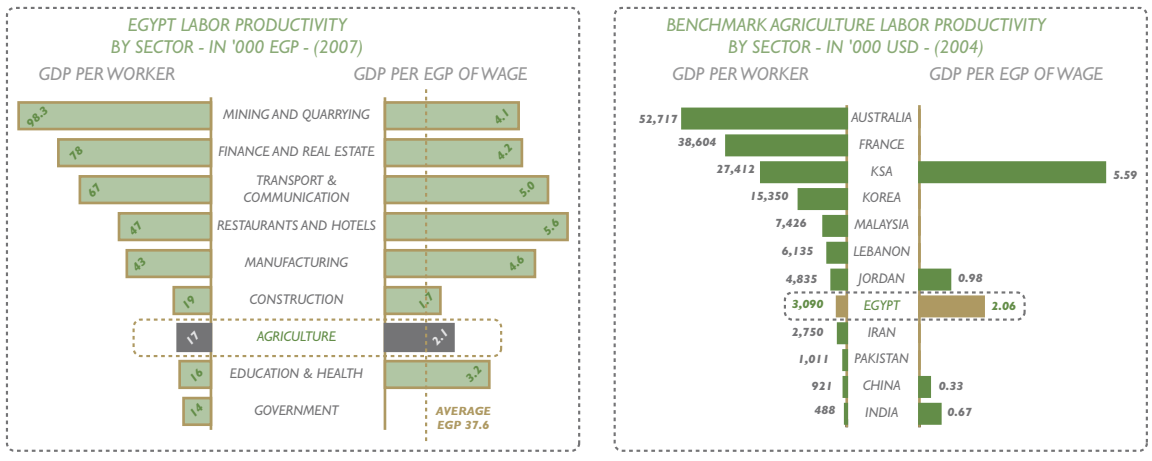
Fully realizing the critical role the sector plays in maintaining socioeconomic stability, the government has made efforts to provide it with a financial support system, in the form of subsidies. One example of such subsidies is the below-market interest rates provided to farmers by the Principal Bank of Development and Agriculture Credit (PBDAC) for agriculture-related purposes. Another example is the government's provision of subsidized agricultural services such as soil testing and land improvement services. Subsidies play a direct role in guiding the behavior of sector stakeholders and hence are a powerful policy tool. However, subsidies also require continuous monitoring and realignment with sector objectives in order to ensure that desired policy outcomes are achieved. Moreover, it adds a heavy burden onto the government's budget. A retreat from some subsidy structures in place has been witnessed recently, such as the elimination of the nitrogen-based fertilizer subsidy in March 2008.

FIGURE 3.2: *FACTOR PRODUCTIVITY COMPARISON*



Source: CAPMAS; WDI Online Database; UNSTAT; "The State of Food and Agriculture 2003-2004" FAO 2004

FIGURE 3.3: *AGRICULTURE LABOR PRODUCTIVITY COMPARISON*



Source: CAPMAS; WDI Online Database; UNSTAT

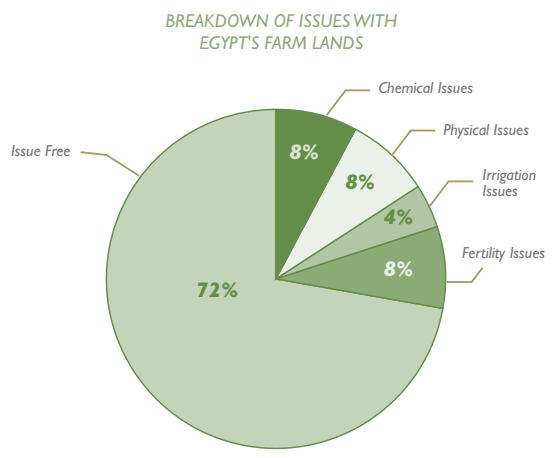
3.2 SECTOR ASSESSMENT

Analysis of factors of production and sector enablers reveals key findings underpinning current sector performance. The following section highlights key sector strengths and weaknesses in light of the analysis of factors of production and enablers.

3.2.1 Strengths

- ***Geographic location:*** Egypt's central location provides a key competitive edge driven by its proximity to key export markets: the EU, GCC and Asia. Egypt's proximity to large trading ports also increases its access to international markets, giving it a significant advantage for agriculture export purposes;
- ***Year-round cropping:*** Favorable weather conditions allow year-round cropping which serves to boost land output and yield, provides a unique window of competition-free sales (local and exports) at times when competing markets are dormant due to weather conditions or different seasons. Furthermore, Egypt's climate band which ranges from fair Mediterranean weather in the north to the sunny warmth of its African south allows the cropping of a wide variety of produce;
- ***Strong production growth:*** Agriculture production has kept up with population growth over the past 15 years, growing at a Compound Annual Growth Rate (CAGR) of 1.8 percent compared to population growth of 1.9 percent. This is matched by a strong sector GDP growth of 3.2 percent[6]. Such high production growth rates are driven by the increasing yields discussed earlier, in addition to the strong land reclamation activities that are creating additional arable land;

FIGURE 3.4: *EGYPTIAN FARM LAND QUALITY*



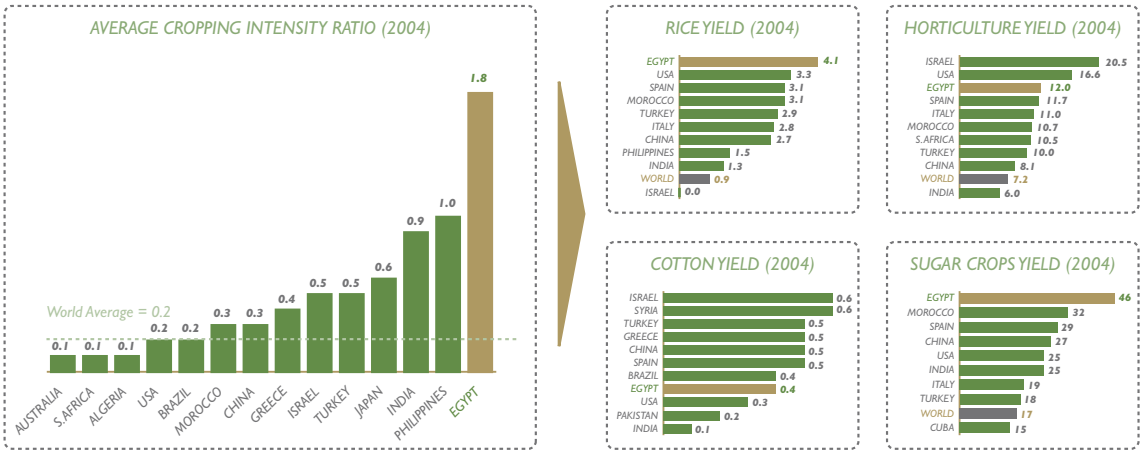
Source: Agriculture Statistics Summary- MARL Economics Sector, Egypt's agriculture Strategy to 2017-MARL

- ***High land quality:*** Fertile land in Egypt is generally of high quality with up to 70 percent of total arable land identified as "issue free" (see figure 3.4), making it ripe for the potential production of premium crops, high quality produce, and organic crops. It is a strong contributor to the sector's high productivity rates;
- ***High land productivity:*** Egypt also benefits from benchmark crop yields, which are not only high, but are still increasing for most crop categories. Furthermore, cropping intensity is ranked among the highest in the world, driven by the age-old farming practices and small farm holdings, which although presenting their own challenges, allow farmers to cater to almost each of their plants individually. Both factors contribute to high land productivity when compared to benchmark countries;
- ***Stable water source:*** The Nile water flow, Egypt's main source of agriculture irrigation, is controlled by the Egyptian government through the Aswan High Dam. Furthermore, international agreements fix Egypt's entitlement to 55.5 billion m3 p.a, which can be stored in Lake Nasser and released over the entire year creating a reliable source of irrigation for agriculture that ensures year-round cropping;
- ***Good water quality at the source:*** Water quality at the source is of very good quality (before deteriorating downstream due to higher concentration of drainage water), which if maintained through improving drainage and limiting waste seepage, provides a great opportunity to further improve crop quality;
- ***Low labor costs:*** Average wages are among the lowest of all benchmarked countries (US$ 29/worker/week, relative to US$ 68 in the Philippines and US$ 51 in Mexico)[7] as well as among domestic sectors. Hence, labor is both cheap and easily accessible. Although this is a temporary strength driven by skill level and productivity, it can nonetheless be very useful in fuelling sector growth;
- ***Low pesticide use:*** Consumption of pesticides is relatively low compared to benchmark countries driven by strong reliance on manual pest control, which can be attributed to high sector labor intensity, low labor costs and small farm area holdings;

[6] CAPMAS Online Databases (2008); Egypt Central Bank Website (2008)

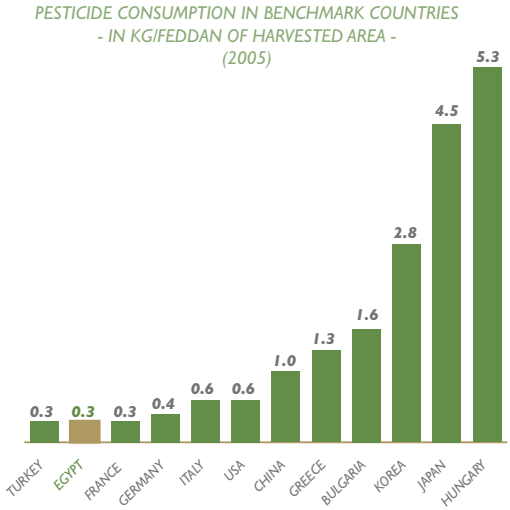
[7] CAPMAS Online Databases (2008) and ILO Online Labour Statistics Database (2006)

FIGURE 3.5: EGYPTIAN LAND PRODUCTIVITY COMPARISON



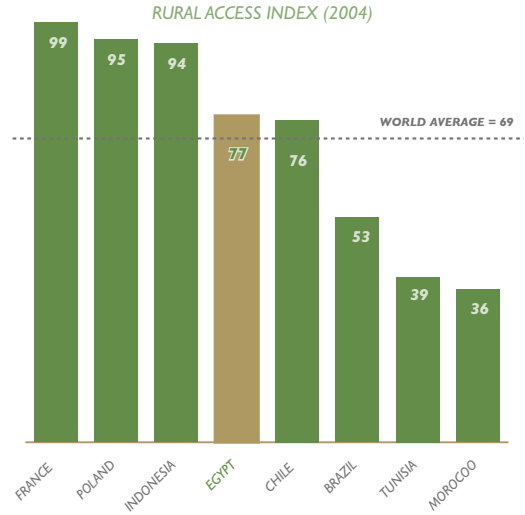
Source: Agriculture Statistics Summary- MARL Economics Sector, FAOSTAT

FIGURE 3.6: COMPARATIVE PESTICIDE USE



Source: Agriculture Statistics Summary MARL Economics Sector, FAOSTAT; Booz Allen Analysis

FIGURE 3.7: RURAL ACCESS/CONNECTIVITY COMPARISON



Source: Egypt Freight Transport Report Q2, WDI Rural Access Index Database (2004), Euromed Road Network Database, CAPMAS

- ***Basic infrastructure availability:*** Despite its logistical constraints, Egypt's basic infrastructure is in place, thus making potential improvements easier and faster to achieve. For example rural accessibility in Egypt is 77 percent, 8 percent higher than the world average of 69 percent, and extension service structure is present in almost every Egyptian village.

3.2.2 Opportunities

- ***International focus on domestic agriculture sector:*** The current global focus on domestic agriculture sectors as a main lever to alleviate the impact of rising food prices, offers a huge opportunity for agriculturally strong nations, like Egypt, to develop their agriculture sectors and use them to secure domestic nutrition, and drive economic growth;
- ***Strong export potential:*** The impressive growth in agricultural exports in Egypt over the past period (54 percent between 2001-2005)[8] and the increasing demand for agriculture produce, at the new food prices, makes strong export growth a

[8] FAOSTAT and UN Comtrade Online Databases (2008)

great potential that Egypt should continue to drive;

- ***Industrialization of agriculture produce:*** Egypt has a huge untapped potential in integrating both forward and backward, along the agriculture value chain to industrialize the agriculture sector. Focus should be on higher value-add, agro-industries with higher profit potential, such as food processing, seed and fertilizer production;
- ***International branding of Egyptian products:*** Another major unmet opportunity for Egypt is the branding of premium grade Egyptian agriculture produce internationally in a manner that secures customer confidence in the quality of the produce they are receiving. This entails identifying key Egyptian agriculture products that hold a strong competitive advantage, developing an accredited product grading system, then branding qualifying produce in a fashion similar to what has been accomplished already with Egyptian cotton;
- ***Further potential for growth in arable land area:*** The Egyptian government plans to reclaim 2.4 million feddans between 2007-2017 compared to only one million feddans reclaimed between 1997-2007. An additional 1 million feddans is also viable for reclamation. The addition of this large area of arable land to the production resources for Egypt will have a huge positive impact on total sector output.

BOX 3.1: Sustainable Agriculture: a Hidden Opportunity for Egypt

The latest International Panel on Climate Change (IPCC) report has proven again that agriculture plays a major role in climate change.[9] Approximately 30 percent of global greenhouse gas emissions are due to agricultural and forestry practices while manufacturing and application of chemical inputs contribute 7.9 percent. Furthermore, the agricultural sector has a 30 percent improvement potential to satisfy a new but prevailing consumer demand. This is the highest improvement potential amongst all consumer goods. Since not only greenhouse gas emissions, but also water consumption, soil fertility and land reclamation are tomorrow's factors for competitiveness, Egypt could significantly enhance the export competitiveness of its agricultural sector if it started now to reshape its industrial, agricultural and export strategy, as stated in the "Overview of Egyptian Agricultural Competitiveness."

In spite of the economic slowdown, the demand for sustainable agricultural commodities increases as their negative environmental impact is minimized.[10] This trend is especially apparent in the United States and the European Union, both among Egypt's main trading partners.[11] Egypt's horticultural exports for example are largely aimed at the European Union, the largest under–supplied market for fresh produce in the world[12] The increasing demand in sustainable and organic food is accompanied by a broad willingness to pay a price premium if certain sustainability criteria are met. The single most important factor in this respect is combined energy/water use, followed by sustainable manufacturing practices and environmentally friendly packaging.[13] A recent study found that 35 percent of the respondents to a survey on climate change assumed that the impact of climate change is at least as bad if not worse than currently communicated by scientists. And 48 percent would even pay more for products with a low carbon footprint. Hence, consumers in the EU and US consider climate change as a real threat and are willing to change their consumption behavior, but they expect the stakeholders of the supply-chain to carry out corrective action, to clean up the products emissions and make the chain's environmental footprint more sustainable. Thus, not only

[9] Cf. IPCC (2007), Climate Change 2007 - Synthesis Report: Summary for Policy Makers, 2007.

[10] TCf. The Hartman Group (2008), The Many Faces of Organic 2008, 2008 and Willer, H. et al. (2008), The World of Organic Agriculture – Statistics and Emerging Trends 2008, 2008, and UNCTAD Website: http://www.unctad.org/Templates/Page.asp?intItemID=3757&lang=1

[11] Cf. European Commission (2005), Annex to: European Neighbourhood Policy, Country Report Egypt, 2005.

[12] Cf. CAADP, FAO, NEPAD (2005), Enhancing Export Competitiveness of Egyptian Horticultural Crops, 2005.

[13] Cf. Capgemini (2007), Future Consumer. How Shopper Needs and Behaviour Will Impact Tomorrow's Value Chain, 2007.

BOX 3.1: Sustainable Agriculture: A Hidden Opportunity for Egypt (Cont'd)

are quality and price determining the competitive landscape of agricultural commodities, but also sustainability is a factor in agricultural competitiveness and can be used to brand Egypt's commodities in premium markets.

Following this new consumer demand, large agricultural companies such as Dole, UniVeg, Dutch Flower Group, Maersk as well as retailers such as Tesco, Walmart, Casino, and Migros are upgrading their environmental standards and promoting their cleaner business practices with consumers. For example, they require emission controlling and mapping across their supply chain, favoring suppliers with low carbon emissions per product unit.[14] As a consequence, it is only a matter of time until these regulations will be included into national legislation and import policies. Furthermore, added value through low carbon emissions lays the basis for higher export prices and margins.[15] This goal can be achieved only by joint efforts by all actors involved, including government and private sector. As the agricultural sector is one of the major driving forces behind environmental impact and resource consumption, measures to reduce emissions accruing from agricultural processes are of utmost importance as they are likely to have a large impact at the aggregate level. At the international level, opening up the Kyoto mechanisms to the agriculture and forestry sectors may stimulate greenhouse gas emission reducing activities, increase farmers' income and attract more investment that benefits sustainable development.[16]

Compared to its main competitor countries, Egypt possesses several natural advantages in maintaining a low-carbon footprint of its agricultural exports. Given the geographical proximity to the European Union, emissions for transportation are low, especially if highly efficient sea freight is used. Furthermore, the favorable climate limits the need to heat greenhouses, and enables Egyptian exporters to supply Europe during the off-season periods in which Europe is lacking adequate supply of fresh fruits and vegetables.[17] Even if there is European supply: whenever sustainability criteria are taken into account Egypt could outperform its competitors due to lower greenhouse gas emissions.

To assess the impact of carbon emissions per stage of production throughout the whole supply chain, carbon footprints (assessments of the total amount of greenhouse gas emissions caused directly or indirectly by an individual, organization, event, or product) expose information on the amount of carbon emissions. A carbon footprint assessment can identify the main emission factors of agricultural production processes. The production and application of chemical fertilizers and the use of packaging material are frequently the two main sources of emissions. With knowledge of the main sources of greenhouse gases, individuals, companies and regulatory bodies are enabled to change their behavior in a targeted way towards more sustainable practices. This instrument could hence be used to promote sustainable farming practices. The elimination of the subsidies on nitrogen-based fertilizer in the first quarter of 2008 was a good starting point.

[14] *Cf. Stringer, R., Umberger W. (2008), Food Miles, Food Chains and Food Producers: Consumer Choices in Local Markets, 2008.*

[15] *Cf. GTZ (2006), Achievements and Impact of the Citrus Improvement Program (CIP) in Egypt, 2006.*

[16] *FAO Committee on Agriculture (2001), Climate Variability and Change: A Challenge for Sustainable Agricultural Production; available at: http://www.fao.org/DOCREP/MEETING/003/X9177E.HTM#P152_15446 and UNCTAD/UNEP (2008), Organic Agriculture and Food Security in Africa, 2008.*

[17] *Cf. CAADP, FAO, NEPAD (2005), Enhancing Export Competitiveness of Egyptian Horticultural Crops, 2005.*

BOX 3.1: Sustainable Agriculture: A Hidden Opportunity for Egypt (Cont'd)

There are three steps through which the public and private sector leadership in agriculture can work together to reduce greenhouse gas emissions:

1. Assess the level of emissions,
2. Implement operational changes to reduce emissions, and
3. Adopt practices to offset emissions.

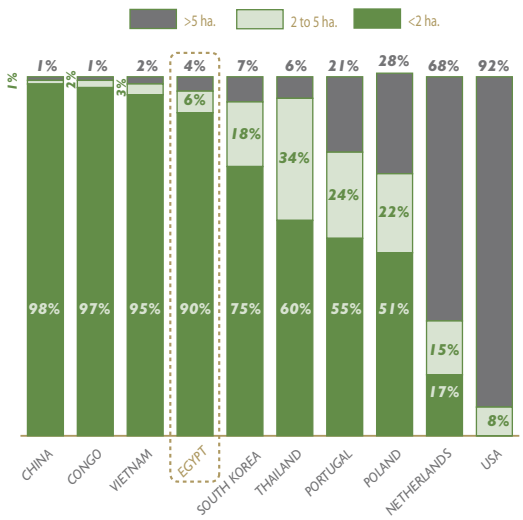
To lower emissions, the first step is to identify comprehensive carbon footprints that trace and record the environmental effect of each product per unit of production. Such product-cycle assessments focus attention on the most influential parts of the supply chain and provide a basis for optimizing the environmental performance of the entire production and distribution system.

Once emissions have been assessed, the sector can pursue measures to reduce emissions at the farm, sectoral and national level. At the national level, integration of sustainability criteria into applied policies requires more than isolated agri-environmental measures. A comprehensive assessment of existing farm support policies and their impact on environmental issues is required. As a consequence, sustainable solutions will be cheaper than non-sustainable since the main reasons for the low costs of non-sustainable farming, namely unjustified incentives, are abolished.

3.2.3 Weaknesses

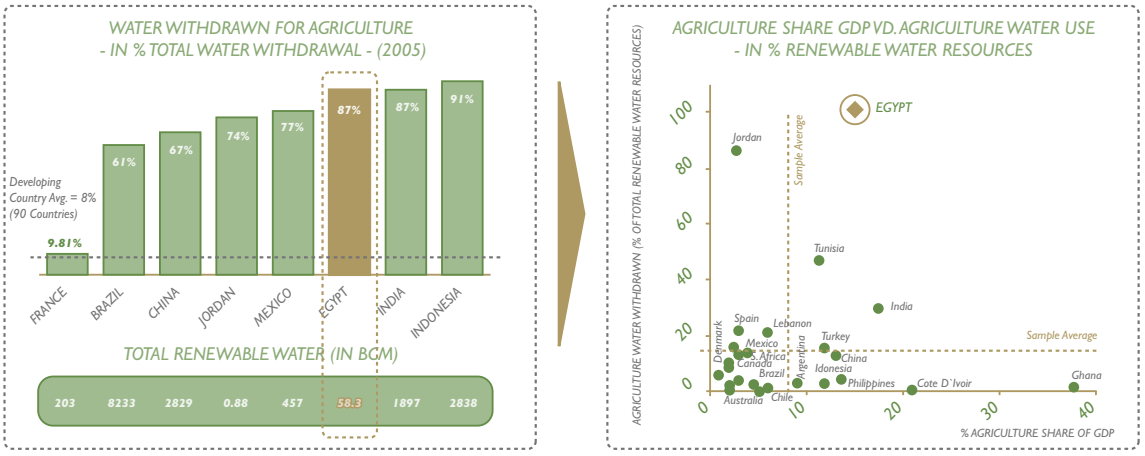
- ***High land fragmentation:*** Land fragmentation is severe and represents an obstacle to sector modernization, automation and farmer training. Egypt currently ranks seventh worldwide in the severity of land fragmentation;
- ***Inefficient water use:*** Egypt does not charge farmers for the usage of water in agriculture, and the Ministry of Water Resources and Irrigation bears all management, maintenance and operations costs of water utilities and infrastructure. The lack of water pricing and water usage regulations in old land has led to the prevalence of inefficient surface irrigation in 71percent of arable land. Furthermore, limited enforcement of water distribution plans leads to inefficient water allocation;

FIGURE 3.8: *FARM LAND FRAGMENTATION COMPARISON*



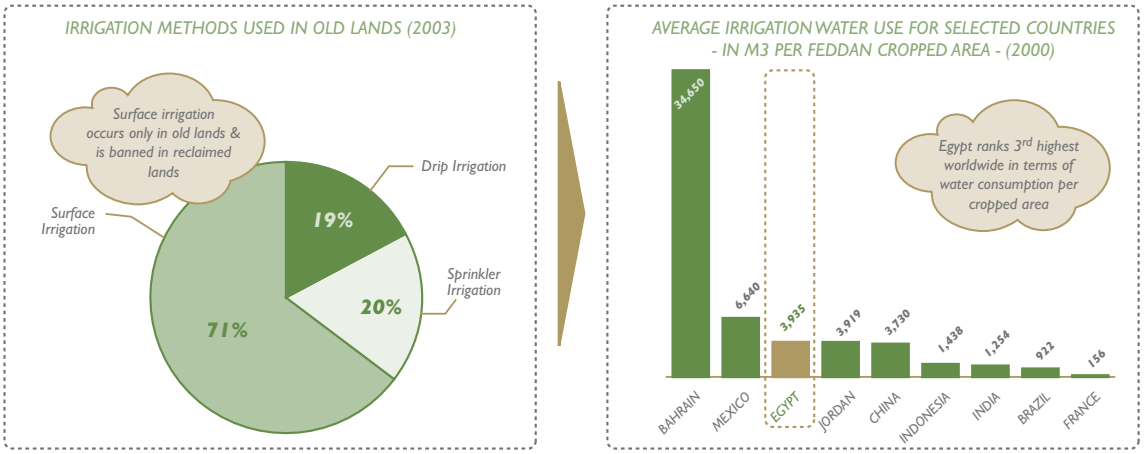
Source: Small Farms: Current Status and Key Trends (2005)

FIGURE 3.9a: WATER USAGE COMPARISON



Source: AquaStat; OECD; WDI 2003

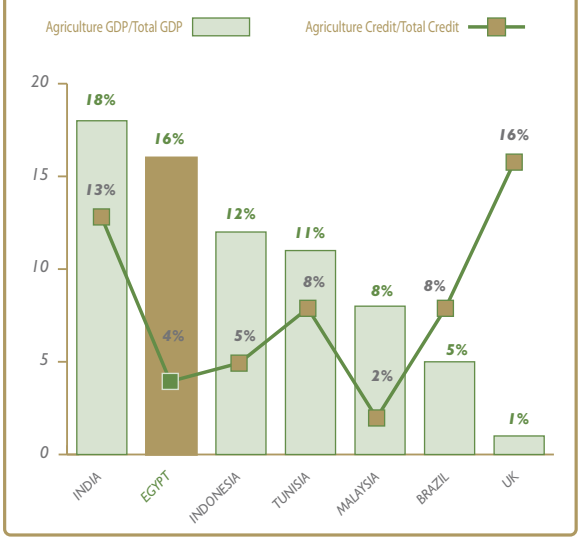
FIGURE 3.9b: WATER USAGE COMPARISON



Source: AQUASTAT

- ***Water contamination:*** Extensive use of fertilizers as well as industrial emission of pollutants contaminates water flowing further down the Nile and into irrigation channels;
- ***Limited farmer education and training:*** Education level of agricultural labor is lower than national average (partially driven by low access to education in rural areas). The lack of focus on farmer training hinders the skill development of agriculture labor and limits sector development;
- ***Low labor productivity:*** Agriculture labor productivity is the third lowest among Egypt's sectors, and amongst the lowest in the agricultural economies (US$ 3,090/worker, relative to Australia's US$ 52,717, or Malaysia's US$ 7,426). Low sector wages and benefits (health insurance, pensions, etc.) discourage skilled labor from participating in the sector, and hence make enrolment in agriculture-related education less attractive;
- ***Low investment levels:*** Despite high contribution to GDP (15 percent) and employment (27 percent), sector share of national investments has steadily declined from 10 percent in 2004 to reach only 5 percent in 2007;
- ***Sub-optimal credit sector:*** Credit supplied to the sector is not aligned with farmer needs and is hence underutilized and less effective;
- ***Non-targeted subsidies:*** Generic subsidies limit the government's ability to use financial levers to drive sector strategy;

FIGURE 3.10: *AGRICULTURE CREDIT COMPARISON*



Source: CBE, PBDAC, FAOSTAT, WDI, International Central Banks

- ***Long-outdated legislation:*** Most agriculture laws still assign operational responsibilities and activities to the public sector, thus hindering private sector participation. Most sector laws were drafted in the 1950s and thus reflect socialist ideologies that no longer fit current government strategies, for example: restrictions on maximum land ownership per person, family and company; and the assignment of most operational responsibilities and activities to the public sector;
- ***Inconsistent legal enforcement:*** The fact that legislation is old, and includes numerous clauses that are no longer aligned with current government direction, leads to inconsistent enforcement, creating legislative confusion. Equally important is the lack of a comprehensive database of laws and decrees to which investors and sector participants can refer to understand sector legislation. When coupled with the existence of thousands of decrees that address agricultural activities, this constitutes a strong barrier to serious investors who are driven away by the risk of operating under legislatively ambiguous conditions;
- ***Institutional inefficiency:*** The lack of efficiency increases overheads, reduces accountability and negatively affects the government's ability to effectively enhance sector performance. Duplication of some tasks in multiple, uncoordinated entities wastes the state budget and reduces accountability. Fragmentation of other tasks among several entities leads to inefficiencies and also reduces accountability, especially since coordination is limited. In addition, the lack of organizational entities responsible for some of the main strategic goals (such as export promotion or water resource optimization, etc.) seriously limits the ability of the sector to initiate or execute the needed transformation initiatives and programs. Meanwhile the existence of public sector entities engaging in operational activities (such a equipment rental, sales and distribution of seeds and fertilizers, etc.) distracts government efforts away from conducting their core functions and crowds-out the private sector, especially if such activities are conducted at subsidized rates;
- ***Poor supply-chain infrastructure:*** Poor quality road networks adversely affect product quality and increase product losses. The limited reliability of railways and waterways has led to a dominance of roads as the single mode of freight transport. The poor quality of the road network (due to uneven and bumpy roads) adversely affects product quality, increases product losses and reduces the efficiency and reliability of access to resources and markets. The supply chain network also lacks: refrigerated trucks and cold storage chains, which hampers efficient distribution of fragile produce such as strawberries; efficiently located logistical aggregation which increases product handling and magnifies losses; and knowledge about post-harvest produce management. The missing know-how amplifies the damage as produce is mostly packed and stored in basic wooden cages (untreated wood) without provision for fragile agricultural produce. Finally, markets suffer from additional shortcomings since traditional retail markets are heavily underdeveloped, with few hypermarkets and advanced supermarket chains. Most local markets for produce (especially outside the city) are open-air markets, where crops are displayed under the sun where they are highly impacted by weather conditions and pollution;
- ***Lack of community development in new land:*** Basic infrastructure development in reclaimed land is behind schedule, leading to substandard living conditions and making it more difficult for farmers to relocate;
- ***Limited research capability:*** More than 80 percent of researchers are based in Cairo, as opposed to rural governorates. Moreover, research-center budget cuts are targeted at reductions in research spending, with limited impact on overhead expenses. Research and development efforts are almost exclusively limited to public entities, with almost no participation by academic institutions or the private sector;

FIGURE 3.11: *COMPARISON OF MACHINE USAGE IN AGRICULTURE*

Source: FAOSTAT

- ***Limited mechanization:*** The use of machinery to increase efficiency and productivity is not prevalent in Egypt since low labor costs and large family sizes encourage farmers to rely on manual, family labor that is in essence free. This can also be partially attributed to land fragmentation, which eliminates the economies of scale benefit of purchasing machinery/equipment. As a result mechanization is often limited to the use of basic low-end machines that are either affordable, or whose rental demand is guaranteed, leading to low rates of adoption of innovative new technology, except in some very large land holdings in reclaimed land. Moreover, since most machinery is invented and produced in developed countries, they are mostly designed to operate in large farming estates, and thus do not operate efficiently (operationally or economically) in the small farm holdings of Egypt;
- ***Limited services capacity and limited private sector participation in services:*** Reliance on public sector services places a heavy financial and administrative burden on the state, and results in limited capacity for land improvement services that does not meet demand;
- ***Low product quality:*** Sub-optimal product quality resulting from inadequate supply chain infrastructure and limited quality control limit the country's export potential and product image;
- ***Limited data availability and reliability:*** Sector data is limited and difficult to access in a comprehensive and reliable format.

3.2.4 Threats

- ***Urban creep:*** The lack of urban planning coupled with weak enforcement of the ban on construction in arable land has led to the emergence of rural slums, which threaten the preservation of Egypt's arable land;
- ***Politically driven changes to water availability and stability:*** Political risk with Nile basin countries create a potential threat to government reclamation plans, especially since to meet the current reclamation targets, Egypt would have to reduce per feddan irrigation or increase water supply over the next 10 years;
- ***Regional and international competition:*** Increasing regional and international agriculture competitiveness poses a threat to Egypt's export market share and future growth, especially with quality issues hindering Egypt from meeting its full export potential.
- ***Rapid population growth:*** Current population growth rate in Egypt exceeds that of the world average and puts upward pressure on the country's ability to meet the consumption needs of its population;
- ***Impact of new pests and diseases on crop yields:*** New pests and diseases are a serious threat to crop yields and can be transported to Egypt from other countries in the region;
- ***Impact of climate change on production practices and quantity:*** More extreme fluctuations in weather conditions over the past three to four years have been witnessed, adversely affecting crop yield.

3.3 THE WAY FORWARD FOR AGRICULTURE IN EGYPT

Recognizing the great potential of the Egyptian agriculture sector, the Egyptian government has formulated a comprehensive Sector Transformation Strategy that aims to build on the numerous strengths of Egyptian agriculture to unleash its real economic potential. The strategy focuses on gearing agricultural production towards supporting and enhancing agri-industrial production, thus generating break-through socioeconomic benefits at the national level, and creating strong economic multiplier effects driven by the links between the agriculture sector and the industrial sector.

The socioeconomic benefits of the strategy include:

- A national agriculture crop gross domestic product (GDP) growth rate of 5.25 percent per annum (vs. 2.16 percent historical growth) and LE 345 billion in cumulative incremental agriculture crop GDP through the year 2020, resulting in an agriculture crop sector GDP of LE 112.7 billion;
- A national agri-industry GDP growth rate of 8.2 percent per annum (vs. 5.2 percent historical growth) and LE 168 Billion in cumulative incremental agri-industry GDP through 2020, resulting in an agri-industry GDP of LE 56.2 billion;
- A notable growth in national employment, adding 910,000 new jobs in agriculture, and 830,000 new jobs in agro-industry by 2020;
- An increase in average labor productivity, reaching LE 28,632 per sector worker in 2020 (vs. a 2006 productivity of LE 17,147 per worker);
- Cumulative sector investments amounting to LE 150 billion in the agriculture sector and LE 83 billion in agri-industry, through to 2020 (based on previously discussed initiatives);
- A significant improvement in sector trade balance, reaching a surplus of LE 26.2 billion in 2020, versus a deficit of LE 8.60 billion in 2006;
- A food security level of 82 percent, in-line with global standards and best practices;
- Finally, all this can be achieved while increasing small farmer profitability annually by 6.43 percent, resulting in average profits of LE 19,126 per/farm (average farm size is 1.7 feddans) per year for small farmers.

To tie all elements together and increase the sector's competitiveness, the government has developed a transformation strategy that will utilize the sector's strengths to mitigate the threats and will leverage the opportunities to compensate the weaknesses. The strategy will achieve the socio-economic gains discussed earlier and introduce a holistic sector strategy that focuses its efforts on six main strategic objectives:

3.3.1 Optimize Access to Physical and Financial Resources:

This strategic objective is focused on the promotion of sustainable management of physical resources, which entails improving water allocation, enhancing efficiency of water usage, increasing arable land area and improving its quality. It also directs agriculture production towards the desired crop mix through a set of targeted incentives, subsidies and better access to credit. This could be achieved through a set of initiatives:

Protection and Expansion of Arable Land

- *Increase arable land area* through the development of a land reclamation master plan (to be established in coordination will relevant ministries) and a rural residential expansion master plan. Also needed are new initiatives to promote public sector investment in basic infrastructure and private sector investments in land and on-farm infrastructure.
- *Maintain and improve the quality of arable land* through the implementation of a national plan for the delivery of land services.

Water Utilization Optimization

- *Improve water allocation mechanisms* by formalizing the Water User Associations operating manual and extending it throughout the nation, in addition to the continued evaluation and implementation of new water-saving methods.
- *Improve irrigation efficiency* and the irrigation infrastructure of old lands.

Subsidy Reform

- *Drive desired sector behavior* where subsidies can be used create a certain crop mix or encourage land consolidation.

Credit System Reform

- Simplify lending processes, adjust credit offerings according to farmer needs and enhance credit risk analysis and monitoring.

3.3.2 Realize Productivity Gains and Increase Scale Effects:

This objective focuses on achieving productivity gains by increasing attractiveness of the sector to a high-skilled workforce, overhauling research and development (R&D) practices, as well as upgrading the knowledge and skills of farmers through targeted extension services. It also addresses reduction of sub-scale agricultural practices by mitigating effects of land fragmentation and building scale in cooperative operations. Initiatives include:

Farmer Horizontal Integration

- *Consolidate land holdings* by creating a land exchange, purchase and re-allocation program, in addition to a new land consolidation fund.
- *Prevent further land fragmentation* though the evaluation and enforcement of a legal limit on minimum farm size.
- *Mitigate effects of land fragmentation* and encouraging group farming through reformed agriculture cooperatives and private-sector investments in low cost machines.

Human Capital Development

- *Plan and rollout new extension program* including the revamping of infrastructure and extension center outreach, and launching a new Extension Services program.
- *Attract high caliber talent to the sector* by changing national education curricula to improve sector image and creating an Agriculture Leadership Program.

Strengthening and Aligning R&D

- *Reform R&D management and incentives,* which entails the redistribution of R&D staff and facilities to agricultural regions and greater involvement of universities in agriculture R&D.
- *Increase investment in R&D* from both the public and private sectors.
- Enforce Intellectual Property Rights (IPR) Legislation on agriculture produce.

3.3.3 Restructure Sector Governance:

This strategic objective focuses on the restructuring of governance and reform legislation within the agriculture sector with the aim of enabling the implementation of policies, streamlining of regulatory and policy-making activities, and capacity building within the Ministry of Agriculture and Land Reclamation. It also addresses the promotion of partnerships with the private sector, civil society and academia for governance and control activities. Initiatives include:

Government Organization Reform

- *Create institutional partnerships* such as the Agriculture Modernization Center and the Agriculture Product Quality Control System with the private sector and formalize the Irrigation Council in coordination with the Ministry of Irrigation and Water Resources.

Legislative Reform

- *Reform legislative environment* and modernize existing agriculture laws in accordance with new sector strategies.

3.3.4 Attract Private Investments in Value-Addition Opportunities:

This strategic objective focuses on the development and marketing of a portfolio of private investment opportunities in agriculture and the simplification of the related investment procedures. It also addresses the increase in private sector investments in sector developmental and clustering activities (e.g. extension services, transport, manufacturing of supplies, downstream industries).

3.3.5 Enable Access to Markets and Capture Higher Price Premiums:

This strategic objective is focused on the improvement of the quality of agricultural produce on domestic retail shelves by enforcing packaging, transport, and storage and hygiene standards. It also addresses ways to upgrade land, railway, and waterways transport infrastructure and the development of multiple produce markets and the enhancement of market integration of small farmers. Finally, means of encouraging the growth of agriculture exports are also addressed. Initiatives include:

Supply Chain Infrastructure Enhancement

- *Develop packaging capabilities* namely, define and enforce packaging, storage and hygiene standards.
- *Enhance national storage networks* via strategically located collection points and storage facilities.
- *Upgrade transport infrastructure* by improving quality and accessibility of major agriculture trade routes, as well as enhancing waterway and railway infrastructure.

Market Enhancement

- *Develop produce markets,* which will require infrastructure for multiple produce markets throughout the country, an agriculture financial commodity market and new crop-insurance mechanisms.
- *Enhance market integration* by formalizing contract farming mechanisms and introducing technology-based information access.

Post-Harvest Agricultural Enhancement

- *Encourage higher value-adding activities in* particular, defining a post-harvest strategy that encompasses things like agro-business, retail and wholesale trade.

Export Promotion

- *Consolidate Egypt's export promotion capacity* by coordinating and institutionalizing public and private sector efforts within a broader governance framework.
- *Brand Egyptian agricultural products* as premium quality.
- *Improve access to international markets* via trade agreements, international distribution offices and logistics networks.
- *Realize full export potential* through structural modernization of production, developing the potential of small farmers in Upper Egypt and new R&D practices.
- *Fully liberalize the agriculture sector* including the review of trade-limiting policies and subsidy revisions.

3.3.6 Carbon Reduction:

This strategic objective focuses on the greater institutionalization of climate change mitigation measures. National policies have yet to directly address the climate change threat. There is a need for market based incentives or new legislation supporting sustainable agriculture, renewable energy and energy efficiency projects. The creation and, more importantly, the effective implementation of a National Strategy for Sustainable Development is an important and necessary step in this direction. Initiatives include:

Reform of Legal Infrastructure

- *Subsidy reform* to promote organic agriculture and biogas producing farms to increase biofuel competitiveness vis-à-vis traditional fossil fuels.
- *Innovative forms of regulation* moving beyond command and control or market-based mechanisms toward voluntary agreements, information-based mechanisms and cooperative environmental governance.

Research and Development

- *R&D investments* in biomass and biogas production techniques.

ENCC FRAMEWORK FOR GREATER INTERNATIONAL COMPETITIVENESS

2. Productivity

Releasing the locked-up wealth creation potential of Egypt is not just about productivity of human labor or technology, or a combination of both. It is first and foremost about the capacity to visualize and materialize high-value new applications for existing assets. Equally it is about the leadership to mobilize alternative uses for land, natural, human and other national resources, so as to convert comparative advantage into competitive advantage and create huge additional value in the process. Coordination of stakeholders on national mega projects, synchronized development of the road system, logistics infrastructure, regulatory reform, sea and air transportation, telecoms and the hi-speed IT network are all examples of broadly based productivity gains which could completely change the face of Egypt.

Key to achieving this is a skill-set of creative thinking, clear vision, cooperation and above all leadership. These need to be connected to a strategy which combines education and training within the labor market, leading to productivity gains at the sector and enterprise level. It is not enough to shovel coal faster into the engine if the ship is heading for an iceberg — that is merely moving faster toward disaster. What is needed is the right quality of vision and leadership, so that increased workforce productivity can be directed to maximum national effect. ***Cont'd page 121***

Enhancing Egypt's Performance through Responsible Competitiveness

Darin Rovere, Nadine El-Hakim, Alex MacGillivray

Egypt's competitiveness depends in part on following a "responsible" development path, meaning staying away from short-term profit-seeking and promoting investments that utilize resources efficiently and respect the environment, as well as worker and consumer rights. Responsible competitiveness is an integral part of competitiveness as global markets increasingly reward responsible behaviour of firms. Improvement in responsible competitiveness requires systems that engage actors including civil society, government and business.

According to the rankings, Egypt currently demonstrates responsibility as a means of complying with international requirements. However, recent policies and voluntary actions of businesses position Egypt to move along the path to leadership and innovation in this area. There have been improvements in the areas of consumer protection, regulating markets, worker rights, and expanded corporate social responsibility practices.

This chapter reviews Egypt's progress on the responsibility path and recommends actions that can enhance Egypt's position. The chapter concludes with the need for stronger engagement of stakeholders across government, civil society and the business sector, which can be realized by an effective National Sustainable Development Strategy process (NSDS). Potential for success of a NSDS are described in detail, demonstrating the economic as well as social and environmental returns of this paradigm shift.

4.1 INTRODUCTION

"Responsible Competitiveness is no longer a luxury for the rich. It is a development path that compels us to use our human, natural, and financial resources efficiently while moving forward to realize a prosperous life for all."

Maged George, Minister of State for Environmental Affairs

Egypt strives to foster a prosperous society where all members are able to attain a high quality of life. The ambitious objective of prosperity with equal opportunity requires strong, sustained economic growth underpinned by responsible management of Egypt's environment and careful stewardship of the country's human and natural resources.

Sustained economic growth is achieved by attracting productive investments that lead to higher productivity and increased competitiveness of Egyptian businesses in international markets, and enhanced employment opportunities for Egyptians. However, higher productivity alone will not directly lead to a prosperous, equitable society. Increased productivity and competitiveness must be coupled with active leadership to: protect and develop the skills of the workforce, provide health care and other social services and safety nets, and manage the environment and natural resources for long-term sustainability. This is responsible competitiveness.

To promote responsible competitiveness, Egypt must support innovative collaboration between policymakers, business leaders, and civil society to create effective systems and programs.

This chapter reviews the current state of Egypt's efforts to foster responsible competitiveness. The chapter then considers four critical issues facing Egypt's economy through the lens of responsible competitiveness:

- ***Agricultural Competitiveness:*** As one of the leading non-petroleum export sectors, agriculture is a critical source of prosperity and economic growth. It is a potential export growth engine that is constrained by inefficient use of resources and widespread reliance on unsustainable practices.
- ***Industry Competitiveness:*** There are immediate opportunities to enhance industrial competitiveness by encouraging companies to work together through sectoral alliances and partnerships to develop cost-effective ways of doing business and to identify new markets.
- ***Labor Competitiveness:*** Egypt possesses a strong demographic resource, but is in dire need to use it efficiently. Deploying more researchers in research and development (R&D) and enhancing the quality of local managers and workers are at the top of the agenda. This can be attained by improving the quality of education, ensuring decent and productive workplaces, providing on-the-job training, and eliminating the worst forms of child labor.
- ***Energy- Meeting Needs and Encouraging Innovation:*** Energy needs in Egypt are expected to more than double over the next 15 years. Egypt relies mostly on fossil fuels for its energy requirements, and is increasingly relying on cleaner burning natural gas. Adoption of renewable energy and energy efficient technologies will become essential for Egypt to meet its energy needs. They would also open new market opportunities that are now more realizable in light of the government's plan to gradually reduce energy subsidies. Movement along this path will help Egypt to reduce carbon emissions which contribute to climate change. Egypt currently is among the countries with high "carbon intensity" meaning that it has higher levels of carbon emissions per unit of GDP.

Achieving competitiveness the sustainable and responsible way is not a luxury available only for richer countries. It is an efficient, equitable, and sustainable development path and a key to a better and more prosperous future. This chapter concludes by outlining the key policies required to guide the Egyptian economy along the correct path to balanced and responsible competitiveness.

Egypt's responsible competitiveness is an integral component of its overall competitiveness. By implementing a manageable set of targeted interventions, Egypt can progress in three important directions:

- ***Enhanced "connectivity" as competitiveness cannot be achieved without the concerted efforts of government, business and civil society.***
- ***Enhanced "productivity" of natural, human, and financial resources by efficiently utilizing Egypt's vast supplier base; investing in efficient technology and a more productive and motivated workforce; and better targeting investments and government subsidies.***
- ***Responsibility towards future generations and improvements in environmental performance.***

This can help Egypt to be competitive in the vast growing global markets that reward responsible behavior.

4.2 EGYPT'S POSITION IN RESPONSIBLE COMPETITIVENESS: THE RCI

"It's no exaggeration when I say I checked the top 10 in every indicator. We just asked them, 'What did you do?' If there is any advantage to starting late in anything, it's that you can learn from others."

Dr. Mahmoud Mohieldin, Egyptian Minister of Investment, on the Doing Business indicators[1]

The Responsible Competitiveness Index (RCI) was developed by AccountAbility[2] and partners to benchmark country progress towards responsible competitiveness.[3] The RCI is a composite index, designed to quantify the performance of 108 economies in strengthening the drivers of responsible competitiveness.

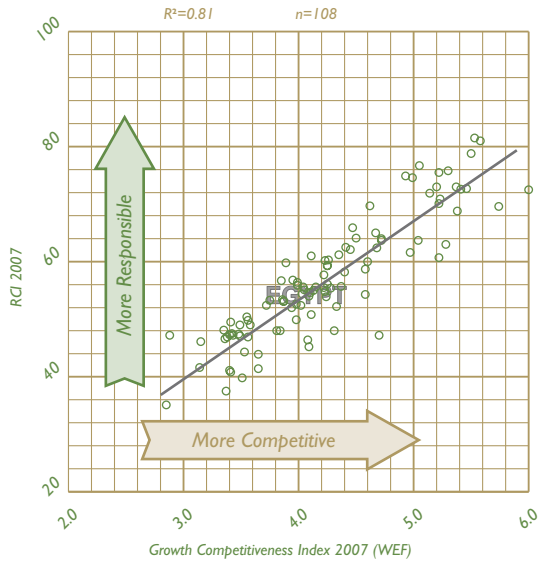
The analysis uses 21 indicators - including hard and soft data - from authoritative sources like the World Bank/IFC, the World Economic Forum (WEF), the International Organisation for Standardisation (ISO), International Labor Organisation and Transparency International. As illustrated in the diagram below, the goal is to capture national progress in promoting responsible approaches to competitiveness by measuring various aspects of policy drivers, business action and social enablers.

FIGURE 4.1: *DRIVING RESPONSIBLE COMPETITIVENESS*

Source: Accountability's Global Responsible Competitiveness Report (2007)

The 2007 edition of the RCI reveals a significant positive correlation between competitiveness and responsibility (see Figure 4.2).

FIGURE 4.2: *GROWTH COMPETITIVENESS AND RESPONSIBILITY*



Source: AccountAbility's Responsible Competitiveness Report (2007) and World Economic Forum's Global Competitiveness Report from 2006-07

On the basis of these results, countries can be categorized into four performance groups: starters, compliers, asserters and innovators. There is a significant relationship between the stage of development and the progress on responsible competitiveness, yet the Innovators category includes some countries that are less financially endowed than others in the Starters and Compliers groups.

- ***Starters:*** Starter countries indicate acceptance and pursuit of responsible competitiveness in policy statements, but their implementation of basic policies and practices is weak. Over 30 of the largest countries are considered Starters including China, Bangladesh and the Russian Federation.

[1] http://www.doingbusiness.org/documents/DB09_About.pdf.

[2] AccountAbility is an international think-tank aiming to hold policy makers and businesses accountable towards society and future generations by promoting responsible competitiveness.

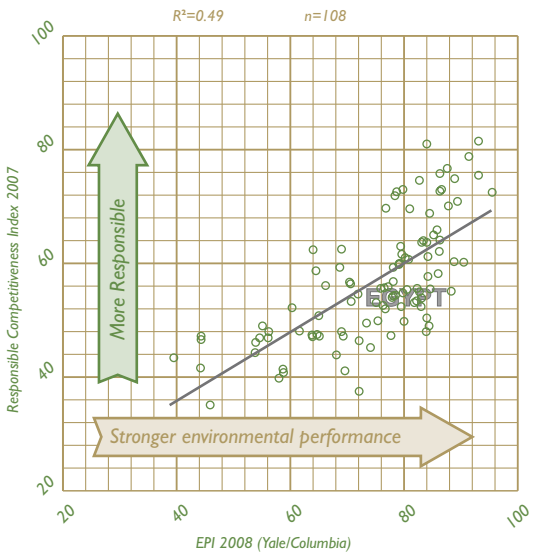
[3] A series of global reports has been produced, in 2003, 2005 and 2007 (with a new study forthcoming in 2009).

- ***Compliers:*** This group, which includes Egypt, is actively striving to meet international standards of quality, labor and environmental protection, in order to further integrate economic activities in international markets. Domestic civil society is not yet a significant player (as counterbalance and collaborator to business) for Compliers. This group enjoys vibrant economic activity and collectively accounts for US$1 trillion in world trade.
- ***Asserters:*** Asserters are actively incorporating responsible competitiveness ideas and practices into their economic strategies. Some of them, like Chile and South Africa, are taking the lead in developing and promoting international standards that deal directly with their economic prospects. By leading, they are also positioning themselves in a favourable position in important industries. Asserters are also building national brands known for embodying responsible business and government practices. This, in turn, is attracting foreign direct investment and promoting global products and corporate brands. For many Asserters, civil society plays a critical role in challenging businesses to uphold a minimum level of standards, but also in collaborating with businesses to find solutions that achieve responsible competitiveness.
- ***Innovators:*** Only 20 countries are grouped into the Innovators category – mostly in Europe and other OECD countries. Innovators are embedding responsible and accountable business practices into the core of their economies. Innovations in responsible competitiveness in these countries are underpinned by relatively well-enforced regulatory systems, actively pursued corporate responsibility strategies, and strong NGOs, media watchdogs and consumers demanding higher standards for responsible management practices.

Egypt ranks 67th in the 2007 Responsible Competitiveness Index. It falls in the same performance group as major export nations like Brazil and India, and scores higher than the Russian Federation. Egypt is the fifth best performing country among those assessed in the Arab World, with opportunities to learn from the United Arab Emirates, Kuwait, Tunisia and Jordan. Egypt scores relatively well in areas like wage equality for similar work and the uptake of the environmental management system, ISO14001, but the country's early progress in these indicators is now retreating at a time when other countries of the region are making more progress.

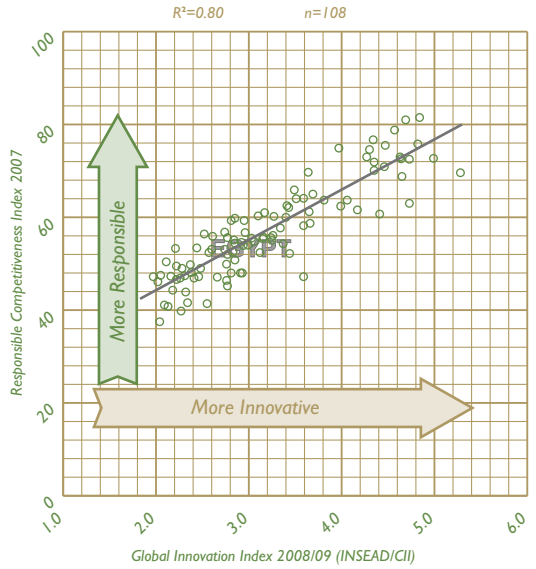
Responsible competitiveness is correlated with both environmental performance (Figure 4.3) and innovation (Figure 4.4). Egypt is recognized for an intense and competitive market and its innovative capacity, with a high-level of businesses using the internet.[4] The challenge and opportunity for Egypt is to create a national strategy and social fabric supportive of business actions which promote sustainable development across the country.

FIGURE 4.3: *RESPONSIBILITY AND SUSTAINABILITY*



Sources: AccountAbility's Responsible Competitiveness Report (2007) and http://yale.edu/epi/2006epi; http://epi.yale.edu/CountryScores

FIGURE 4.4: *RESPONSIBILITY AND INNOVATION*



Sources: AccountAbility's Responsible Competitiveness Report (2007) and www.insead.edu/facultyresearch/centres/elab/document/GIIFinal0809.pdf

[4] The Global Innovation Index 2008/09, INSEAD and the Confederation of Indian Industries.

4.3 CRITICAL NATIONAL ISSUES THROUGH THE RESPONSIBLE COMPETITIVENESS FRAMEWORK

"As we approach the 21st century, it is imperative that we change our general attitude towards the environment, (We must) ...deal seriously with these problems and enforce environmental laws and regulations strictly, without reluctance or hesitation"

President Hosny Mubarak (1997)[5].

4.3.1 Responsible Agricultural Competitiveness

In 2007, the agriculture sector employed over 27 percent of the work force and generated approximately 15 percent of the country's Gross Domestic Product (GDP). This sector constitutes 20 percent of total non-petroleum exports. As the national agricultural export strategy suggests, the regional and international demand for Egyptian agricultural commodities far exceeds the import quotas in destination markets. As internal market inefficiencies are addressed and international trade barriers are gradually reduced, agriculture will be one of Egypt's export growth engines[6].

However, the future of agricultural competitiveness in Egypt will depend on efficient and responsible management of natural resources. Recently, the importance of agriculture as a contributor to GDP has declined whereas other sectors such as construction have expanded. This is due to multiple factors, including limited availability and inefficient use of natural resources. More than 76 million Egyptians are concentrated in 10 percent of the land area, i.e. around the Nile basin, leading to pressures on natural resources and degradation of fertile land.[7] Egypt's land reclamation efforts expanded total agricultural land to over 8 million acres, and seek to add 3.4 million acres by the year 2017. However, these efforts are subject to the availability and efficient use of freshwater resources. Egypt is classified as a "highly water stressed" country, among the lowest 40 percent of the world population in terms of per capita water resource availability. Average available water is less than 900m^3 per capita.

Agriculture consumes over 80 percent of Egypt's water resources, yet Egypt's irrigation water use efficiency is among the lowest 10 percent in the region, with only limited advancement in this area over the past 10 years[8].

Furthermore, Egypt's limited fertile land has been subject to a continuous degradation trend, including salinization driven by inefficient irrigation and water logging, and soil pollution from inefficient use of agrochemicals.

In addition, over 80 percent of Egypt's land is fragmented into land holdings of three acres or less. Small farms often suffer from limited coordination, lack of qualified human resources, almost no export orientation and no knowledge of sustainable agriculture. Knowledge of good agricultural practices does exist among Egypt's agricultural exporters, yet these exports represent less than 10 percent of Egypt's fertile land resources.

This knowledge gap between exporters and the majority of land holders can be closed by responsible efforts on the part of large exporters to "green their supply chain", i.e. to provide technical support to their suppliers to help them practice sustainable agriculture and abide by environmental standards. This work has received significant international support through the United States Agency for International Development (USAID), International Fund for Agricultural Development (IFAD), and other agencies working in this field. The Ministry of Agriculture has provided several leading examples in this area including a high dam lake development project supported by the World Food Programme, which provided an example of sustainable villages based on organic farming, modern irrigation and renewable energy. The Wadi el Rayan project is another example. Supported by the Italian Debt-for-Development Swap, the project enhanced skills and knowledge of farmers in irrigation and sanitation, raised awareness of environmental issues, and linked the production of organic products to traditional and Fair Trade markets.[9] Successful pilot efforts such as these have led sustainable agriculture to be a key element of the of the Egyptian Transformation Agricultural Strategy.

Awareness raised by international interventions has also led major exporters and agricultural companies to realize the benefits of expanding their supplier base to include small farmers. A number of them already provide technical assistance to their suppliers in order to meet environmental and safety produce standards. For example:

[5] President Hosny Mubarak (1997)- Ministry of State for Environmental Affairs, http://www.eeaa.gov.eg/

[6] Industry Modernization Center. 2007. Egypt Agricultural Export Strategy.

[7] Center for Public Mobilization and Statistics (CAMPAS). National Census (2006).

[8] Thivet, G. and M. Blinda. 2008. Improving Water Use Efficiency for Facing Water Stress and Shortage in the Mediterranean. A Blue Plan Report.

[9] http://www.eiecop.org/ambiente2/projects_2/wadielrayan_2.htm

- Heinz has partnered with some 3,000 small tomato growers in Upper Egypt and provides them with training and technical assistance in order to produce tomatoes that abide by environmental and safety product standards.
- Farm Frites, the leading producer of frozen potatoes and vegetables in the Middle East, has extended technical assistance and training to small farmers in order to expand a reliable supplier base. This model has benefits for both parties. The large processor/exporter gets a high-quality product at a competitive price, while small farmers have access to new markets and can use new knowledge and practices for growing crops that meet international health standards. Similar initiatives to those of Heinz and Farm Frites have been undertaken by local supermarket chains, major exporters and food processors.
- "Cotton Egypt," an organization founded through a joint effort between the Ministry of Trade and Industry and the Alexandria Cotton Exporters Association, is an example of public-private partnership in promoting sustainable competitiveness. Cotton Egypt aims to help cotton growers in Egypt to meet the expectations of the international market. Bearing the Egyptian Cotton Logo (ECL)™ signals that the product abides by international standards of quality, environmental consciousness and product safety.

These three examples illustrate how large processors and exporters at the top of the supply chain can engage with small farmers in a mutually beneficial way that both expands market access and upholds international quality and sustainability standards. It is through replication and expansion of such initiatives that Egypt's agricultural sector can efficiently utilize its entire resource base and fulfill its agricultural potential.

4.3.2 Improving Industry Competitiveness

Egypt has a real opportunity to enhance industrial competitiveness through responsible business practices. Immediate opportunities exist to enhance the performance and social impact of the private sector through scaling-up CSR activities, supplier development programs and through effective industry and public-private partnerships. These strategies are enabling industries to create new high-performing clusters, embrace emerging technologies, identify new market opportunities and increase efficiency.

Evidence from around the world shows these types of initiatives can enhance the competitiveness of individual firms and industrial sectors by developing cost-effective ways of doing business and penetrating new markets. Examples include:

- Supplier development programs: The concept of "greening the supply chain" also applies in industry, as 40 percent of the world's largest companies are working with suppliers to improve their performance on key social and environmental issues like health and safety, energy efficiency and carbon footprint. Incorporating social and environmental criteria into public and private procurement and supporting wide-scale training schemes in suppliers could enable Egyptian industry to build competitiveness and address broader societal challenges.
- Issue-specific action: The World Business Council for Sustainable Development (WBCSD), a 200-company coalition, has been working in partnership with businesses for the last 10 years on water management. The program is deepening understanding of responsible water management and looking at how businesses can enhance competitiveness through the responsible use of water, both in core operations and along their supply chains.[10]
- Sector competitiveness: A collaboration of multilateral institutions, trade unions, companies and civil society organizations are working together in countries like Bangladesh, Morocco and Lesotho to improve the productivity of the textile and garment industry through responsible business practices. The Multi-Fibre Arrangement Forum (MFA Forum) was established in early 2004 to address key concerns about the end of the quotas and its social impact on developing countries that were developing a textiles industry. Responsible competitiveness sector programs are also under way in Chile (mining, retail and agribusiness), China (textiles and medicines), Cyprus (finance), Jordan (tourism, construction/real estate and finance) and Central America (various).

[10] Talking the Same Talk: Reaching a Shared Understanding of Key Terms, the World Business Council for Sustainable Development. Taken from: http://www.unglobalcompact.org/docs/issues_doc/Environment/ceo_water_mandate/presentations/Sylvain_Lhote.pdf

BOX 4.1: Sekem's Vocational Training Programme

Sekem is an agricultural group of companies, and a member in the U.N. Global Compact. Sekem founded a non-governmental organization (NGO) to promote biodynamic agriculture in Egypt, resulting in about 2700 hectares applying this sustainable farming approach. The NGO's activities involved research and development, training, extension, technology transfer and other related services.

Responding to the limited opportunities for employment in the formal labor market, Sekem has also established a vocational training centre that provides young people with specific skills for self-employment. Fifty trainees participate each year in a two to three year program that trains them in every aspect of their chosen profession. When they graduate, they are sufficiently skilled either to start their own business or find employment.

Trainees are encouraged to gear their studies to the conditions and market needs that can be expected to exist when they graduate. Through intensive applied course work the students are immediately involved in production. Thus, practical skills take precedence over theory. Training by professional teachers both foreign and local, takes place in fully equipped workshops. The training offered includes biodynamic agriculture, carpentry, textiles, electrical work and metalwork. The Sekem University focuses on economic, social and cultural empowerment of people to allow them to contribute to their country's development through science. The university will not only offer qualifications in key areas that are vital to the continuing development of Egypt, but will also incorporate Sekem`s philosophy and ideals.

Source: Sekem Corporate Social Responsibility Report to the Global Compact Initiative

4.3.3 Improving Labor Competitiveness

Productivity depends on a skilled and motivated workforce. Egypt already has strong potential compared to other countries of the region[11] due to its strong demographic resources.

Significant investment in human resources is needed. Deploying more researchers in R&D, enhancing the quality of local managers and ensuring decent and productive workplaces are now at the top of the talent agenda. On-the-job training, safe workplace practices and enabling women to participate on equal terms and fair wages are all necessary to ensure high morale and increased productivity.

Unemployment in Egypt is about 8 percent, with youth unemployment at over 17 percent[12]. Youth unemployment is probably the most widely felt problem in rural Egypt, explaining the number of corporate social responsibility programs which have adopted this goal as their main mandate. Increased corporate investment in training and preparing youth with skills demanded on the market is a key contribution for Egypt's responsible competitiveness.

[11] Ranked first in the Middle East according to the 2007 Heidrick and Struggles Talent Index, http://www.weknowglobaltalent.com/gti/window/meti.

[12] Assaad, R and G. Barsoum. 2007. Youth Inclusion in Egypt: In Search of Second Chances. Wolfenson Center for Development, Brookings Institution.

BOX 4.2: Outsourcing in Egypt

Egypt is becoming an internationally desirable country for outsourcing. It has built competitive advantage as an attractive destination for companies looking to increase cost-efficiency by moving operations for specific business functions like human resources, customer-related services and administration to a low-cost destination. Egypt's strong performance was recognized by the National Outsourcing Association as a recipient of the prestigious award 'Outsourcing Destination of the Year' in October 2008 and it currently ranks as the most desirable country in Africa and the Middle East in AT Kearney's authoritative Global Services Location Index.[13]

The global economic downturn is spurring companies to make supply chains more cost-efficient. The demand for quality outsourcing solutions so far appears to be surviving in these turbulent times, but companies are demanding different types of offerings from outsourcing destinations. A recent global report by the International Institute for Sustainable Development and AccountAbility[14] showed that companies are increasingly concerned about the social and environmental footprint of outsourced jobs, and that major economies are looking to compete through offering accessible e-waste facilities, energy efficient data-centers, improved staff training and 'green' buildings.

Egypt is in a good position to refine its outsourcing offering to meet these changing demands. Its core strengths – technical graduates, a multilingual workforce, a good understanding of Western businesses and the connection between universities and businesses – provide a strong platform from which to build. Already there is evidence that Egypt is gearing up for this agenda. The Information Technology Industry Development Agency (ITIDA) is working to improve working practices through a collaboration between 100 local IT firms,[15] the Ministry of Communications and Information Technology and the United Nations Development Programme to develop community telecentres that increase IT capacity in small and medium-sized enterprises.[16]

Outsourcing and information technology will 'lead to a renaissance in Egypt' according to the former ITIDA Chief Executive, Mohammed Omran.[17] The challenge now is to ensure this renaissance promotes dynamism across all areas of the economy, supports social development and reinforces environmental security.

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[13] National Outsourcing Association names Egypt best offshoring destination, August 2008, available at: http://www.itida.gov.eg/images/NOA percent20Awards percent20October2008 percent20draft_1.pdf; Offshoring for a long-term advantage, 2007, AT Kearney available at: http://www.atkearney.com

[14] Towards Sustainable Outsourcing: A Responsible Competitiveness Agenda for IT-Enabled Services, International Institute for Sustainable Development and AccountAbility, March 2009. Available at www.accountability21.net

[15] ITIDA to launch a capacity building programme for 100 Egyptian IT companies http://www.itida.gov.eg/images/2008 percent2008 percent2010 percent20Capacity percent20Building.pdf.

[16] Sustainability Revisited: Egypt IT Clubs, Telecentre Magazine taken from http://css.escwa.org.lb/ictd/17-19DEC08/d1.pdf.

[17] Egypt wants a bite of Indian Call centre market, August 2007. Taken from: http://business.maktoob.com/News-Details-20070423120777-Egypt_wants_a_bite_of_Indian_call_centre_market_.htm

4.3.4 Meeting Energy Needs and Encouraging Innovation

Energy needs in Egypt are expected to more than double over the next 15 years. Egypt relies mostly on fossil fuels, but is increasingly relying on cleaner burning natural gas. Adoption of renewable energy and energy efficient technologies will become essential for Egypt to meet its energy needs. It will also be essential in air quality improvement. Cairo residents suffer from poor air quality, particularly with regards to total suspended particulates (PM2.5 resulting mostly from fuel combustion, i.e. vehicle and factory emissions[18]). Energy efficiency will both improve industry productivity and air quality, which will have a major impact on prosperity, health and life expectancy.

The government's plan to gradually reduce fuel subsidies over the next few years will encourage adoption of energy efficiency. If complemented with additional policies and wide-scale programs to promote energy efficiency, it can also significantly enhance air quality. Measures would include taking energy-inefficient cars (some of which are 30 years old) off the streets and promoting greater use of fuel-efficient public transport, particularly since transportation contributes to 17 percent of total carbon emissions. The Cairo pilot project that aims to help replace up to 30,000 old taxis through soft loans is a commendable initiative.

Energy efficiency will also help Egypt to reduce its carbon footprint. Egypt may be among the lower emitters of greenhouse gasses (GHGs), contributing just 0.5 percent of the world's CO_2 emissions. However, per unit of GDP, Egypt's GHG emissions intensity is among the highest in the region.

Egypt has gradually increased gasoline and diesel prices by approximately over 80 percent since 2004. It is no longer at the extreme in international rankings of fuel subsidies. The government is committed to further reducing subsidies which currently benefit mostly large consumers. The government is also committed to phase out electricity and gas subsidies for Egypt's 40 top energy intensive industries which represent more than 40 percent of total energy consumption over the medium term.

This energy subsidy reform program is expected to mostly impact heavy industries, some of whose profit margins reach up to 30 percent. In order to minimize the inflationary effect of fuel subsidy reduction, the government has implemented a number of measures. For instance, a new tax law subjects industry to a simplified tax.[19] Also, the anti-monopoly law of 2005 prevents the few market-dominating heavy industries from passing on the entire burden of the added cost to the consumer.

Fuel subsidy reduction is typically feared to increase food prices and affect food security. As Egypt suffers from an average poverty rate of 19.7 percent (reaching 50 percent in the poorest villages)[20] and a relatively high malnutrition rate among women and children, this potential effect is particularly concerning. Low income households spend almost 70 percent of their income on food and with rising food prices there is a risk of developing a phenomenon of hunger. The government recognizes this risk, made apparent by the 2007-08 food price crisis brought about by rising international fuel costs, and plans to partly redirect savings from energy subsidies to food safety nets and enhancements in agricultural production.

This all implies that the government will need to conduct careful analysis of the economic, equity and fiscal implications of the reform package to ensure that the macroeconomic gains from an energy subsidy reduction will not be offset by tax revenue reduction due to slow economic growth and will not leave the poor population in Egypt vulnerable to high inflation that could result in increased inequality

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[18] Egyptian Environmental Affairs Agency. 2006. Egypt State of the Environment Report.

[19] Egyptian-German Joint Committee on Renewable Energy, Energy Efficiency, and Environmental Protection. http://www.jcee-eg.net/reee.asp?sublinkID=26

[20] UNDP. 2008. Egypt Human Development Report.

BOX 4.3: Promoting Renewable Energy

Promoting renewable alternative sources of energy is a top priority for Egypt. Recognizing that the country is facing dwindling reserves and rapidly increasing domestic consumption, the government in its 2006 Egyptian Energy Policy lists the promotion and wide scale adoption of renewable energy sources as a core goal.

The New and Renewable Energy Authority (NREA), a government agency founded in 1986[21], supports this goal and is focused on assisting international and national investors to scale up renewable energy projects to a commercially viable size. NREA and its partners introduced solar and wind power in Egypt. The first commercial wind farm in the country was opened in 1993[22] and the first large wind park (156 km^2)[23] was established in Zafarana on the Suez coast in 2001[24].

Building on this impetus, in April 2007 the Supreme Council of Egypt launched the Long-Term Plan for Wind Energy, aiming to meet 20 percent[25] of Egyptian electricity needs with renewable sources, with 12 percent[26] to come from wind energy. To encourage investment in the sector, the government offers incentives such as tax breaks and guaranteed off-take by the Ministry of Electricity and Energy.

Not only does wind energy lead to a reduction in CO_2 emissions, but government plans for the large scale creation of wind farms are intended to generate sustained employment. According to a 2006 study for the Industrial Modernization Centre by Cairo University there is a significant opportunity to build competitiveness not just by installing renewable energy technologies, but also by manufacturing them locally, with the opportunities especially attractive for solar heating and biomass, where technologies are appropriate for local manufacturing.

[21] New and Renewable Energy Authority http://www.nrea.gov.eg/english1.html

[22] Economics of Renewable Energy in Egypt http://www.dena.de/fileadmin/user_upload/Download/Veranstaltungen/2007/07/4.1._Financing_wind_park_projects_in_Egypt_NREA_Mohammad.pdf

[23] Economics of Renewable Energy in Egypt http://www.dena.de/fileadmin/user_upload/Download/Veranstaltungen/2007/07/4.1._Financing_wind_park_projects_in_Egypt_NREA_Mohammad.pdf

[24] New and Renewable Energy Authority http://www.nrea.gov.eg/english1.html

[25] Economics of Renewable Energy in Egypt http://www.dena.de/fileadmin/user_upload/Download/Veranstaltungen/2007/07/4.1._Financing_wind_park_projects_in_Egypt_NREA_Mohammad.pdf

[26] Economics of Renewable Energy in Egypt http://www.dena.de/fileadmin/user_upload/Download/Veranstaltungen/2007/07/4.1._Financing_wind_park_projects_in_Egypt_NREA_Mohammad.pdf

Source: New and Renewable Energy Authority http://www.nrea.gov.eg/english1.html

These four challenges are therefore also opportunities with one underlying theme in common: the emergence of markets that reward fair, sustainable and productive business practices, or responsible competitiveness. In each case, there is a direct link between ethical, environmental, and social actions and: i) the corresponding microeconomic impacts for companies, clusters and sectors and ii) the macroeconomic competitiveness impacts for Egypt. By applying the responsible competitiveness lens to four critical issues facing Egypt's economy, this section has focused on new opportunities and challenged existing strategies. The next section outlines a new pathway for the country to raise its responsibility performance in tackling its highest priority competitiveness challenges.

4.4 A RESPONSIBLE COMPETITIVENESS PATHWAY FOR EGYPT

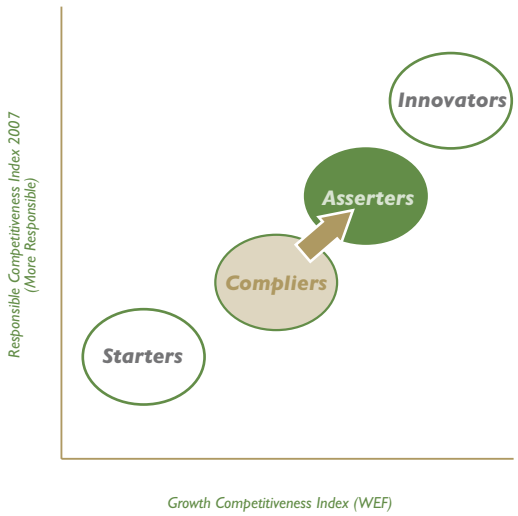
"Preserving the environment is not an entertainment or luxury any more, it has become crucial to protect our resources for the coming generations".

***President Hosny Mubarak*[27]**

Egypt has an exciting opportunity to make significant strides on the national issues discussed above. By advancing responsible competitiveness, Egypt can make significant headways on competitiveness in agriculture, industry, energy, and labour markets.

By advancing policy, business action and civil society engagement, Egypt can leapfrog from a mid-performing country in responsible competitiveness to a high-performing one. Assuming the country works within a coherent and ambitious strategy, it has the potential to graduate from the Compliers group, which contains a large group of Latin American, Eastern European, Arab World and Asian countries, to join the more exclusive group of Asserting countries, ranging from Chile and Costa Rica through SE Europe and a number of Gulf states, to Korea and Thailand.

FIGURE 4.5: *THE COUNTRY CLUSTER CONCEPT*



Sources: AccountAbility's Responsible Competitiveness Report (2007) and World Economic Forum's Global Competitiveness Report from 2006-07

This is an ambitious and challenging transition, which would enable Egypt to proactively assert its responsibility credentials in regional and global markets. Given the strong correlations between responsible competitiveness and key economic, social and environmental variables, this is also a compelling opportunity. The strong relationships between responsibility and competitiveness remain complex and insufficiently understood, but we can say that each percentage point of progress towards responsible competitiveness corresponds to an improvement in their prospects of achieving:

- A significant uplift in innovative capacity and worker motivation, with spin-offs for business performance and the potential for social entrepreneurship;
- Clear improvements in environmental performance, with associated benefits on health (from better air quality) and quality of life and;
- An increase of US$1,000 GDP per capita at PPP.[28]

In other words, this is not an agenda about performing well on yet another international index. This is about securing real, sustainable development objectives.

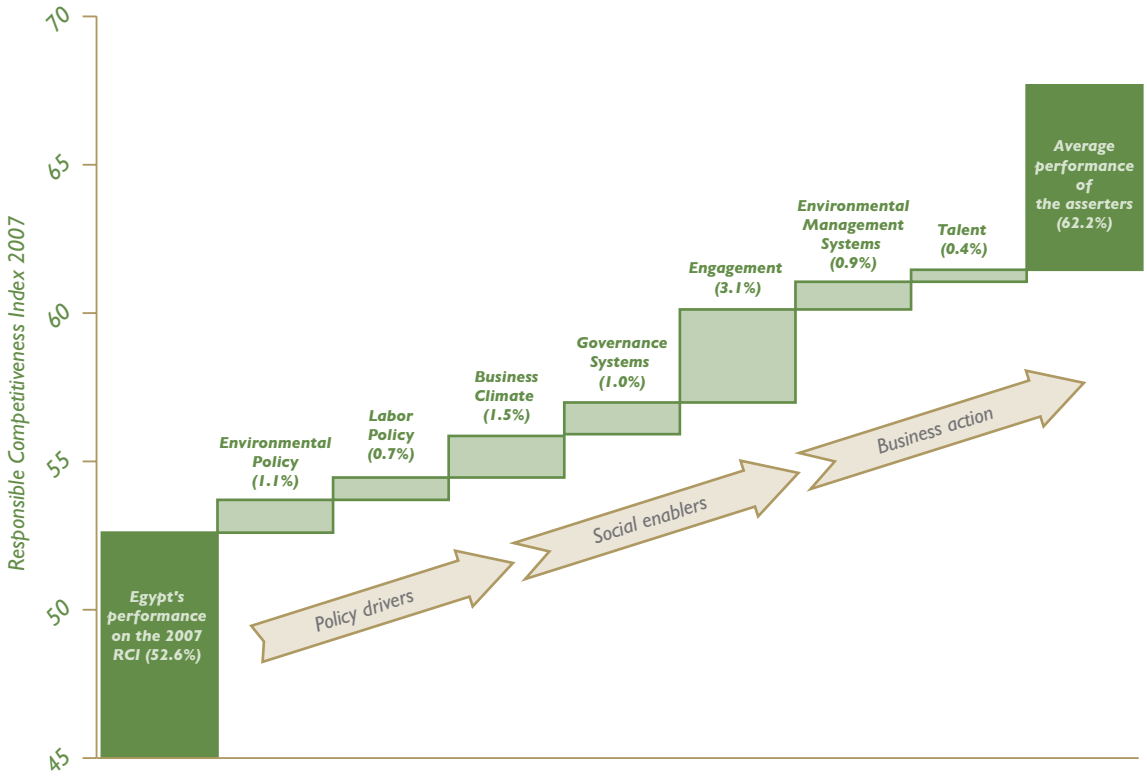
In Asserter countries, export businesses are 'makers not takers' of global sustainability standards and guidelines like organic certification, ISO26000 and the Principles for Responsible Investment, which means they are confident entrants into emerging global markets. The tone of stakeholder relations in labor-intensive sectors like textiles, moves from adversarial to collaborative, with productivity gains and reduced costs from labor disputes and worker turnover. Business culture builds on compliance systems to embrace creative ideas for new products and services. Corporate social responsibility transforms from an elite club of larger global market-facing businesses into a shared endeavour inclusive of SMEs throughout the supply chain. Energy efficiency becomes a norm, not a pilot program. Effective transport systems enable mobility, cities become more liveable, public health improves, and healthy life expectancy increases.

To many countries, particularly in the global downturn, the idea of aiming this high may seem unrealistic; a task to leave until the recovery. However, our analysis shows that Egypt's pathway can be broken down into a manageable set of targeted interventions, building on what is already underway. Taken together, they will enable Egypt to make the transition, starting immediately.

[27] The Ministry of State for Environmental Affairs Report http://www.eeaa.gov.eg/english/reports/GovPlans/BehiraGEAPen.pdf

[28] There is a difference in RCI score of 28.5 percent and a difference in GDP per capita (PPP) of $29304, making the value of 1 percent improvement about $1025.

FIGURE 4.6: *EGYPT'S PATHWAY TO THE NEXT LEVEL OF RESPONSIBLE COMPETITIVENESS*



Sources: Author's own analysis

Figure 4.6 shows seven steps that Egypt can take to raise its performance on responsible competitiveness to a higher level, from the level of the Compliers, to the level of an average Asserter, with the goal of achieving the economic, social and environmental benefits that accompany such progress. From Egypt's current score of 53 percent (on the 2007 RCI), the pathway analysis shows that the gap of 9 percent to the average score of Asserter countries can be closed.

Primary responsibility for these key steps can be divided amongst policy drivers, social enablers and business action. The following sections review the specific options available at each stage of this pathway.

4.4.1 Government Policy Interventions

4.4.1.1. Environmental Policy

Egypt was one of the pioneers in the region in adopting environmental legislation. The government has shown international commitment to environmental issues by signing, ratifying and participating actively in the three Rio Conventions. Domestically, the national environmental law pulls together key national actors to meet Egypt's international commitments. The law designates the Egyptian Environmental Affairs Agency (EEAA) for implementation. A challenge for environmental agencies in many countries is securing adequate financial resources. The EEAA receives one of the lowest budget allocations of all ministries and national agencies. Despite this constraint, the Agency is energetic in its efforts to enforce regulations (see section on environmental management below).

A key measure that would propel Egypt along the path to Asserter is the development of a National Sustainable Development Strategy (NSDS). The NSDS would set out a new framework to address challenges such as climate change and develop Egypt's vision for a low-carbon prosperity plan. The NSDS would replace the National Environmental Action Plan, which was developed as a means to implement the law, but ended up as an ambitious list of projects that the Government is expected to carry out with limited resources. A NSDS would allow more active engagement by all stakeholders (government, business and civil society).

4.4.1.2 Labor Policy

There is significant potential for adopting sound labor policies and stronger enforcement. The ILO calculates that unsatisfactory health and safety alone is responsible for some 4 percent of global GDP.

Rigidity of labor policy has been a long-standing issue in Egypt, a situation which has not helped the sky-rocketing unemployment situation, particularly towards the end of the 1990s. The 2003 Labor Law (Law 12/2003) made a serious attempt to resolve the

constraints in the labor market and to loosen the constraints on employers and employees alike. While primarily issued to facilitate the privatization process, the law also attempted to loosen overall labor market rigidity.

For instance, the law legalized and protected the rights of workers to organize strikes as a negotiation tool, with protection from retaliation by employers. This legal right, coupled with rising inflation and worsening financial conditions, opened the gate for a flood of worker strikes concerning pay, benefits and working conditions. Strikes over this time period have been somewhat effective as they led to serious negotiations between employers and employees and to improvements in working conditions. In addition, the labor law established the National Council for Wages, entrusted with setting a minimum wage. The council is expected to make a major shift in setting minimum wage, as it will be determined by market forces according to the cost of living, prevailing prices and market salary levels. The council has already ruled to set the minimum increase from year to year at seven percent. Further pursuit of such initiatives will enhance Egypt's performance in setting a responsible labor policy.

Employing work ethics is a prerequisite of responsible competitiveness. There are over two million working children in Egypt, 70 percent of them earn seasonal wages in the agricultural sector. The new child law regulates the growing phenomenon of child labor.[29] The law sets a minimum age for engaging children in different types of work, which is no less than 15 in full-time employment and no less than 12 in seasonal employment. Its executive regulations describe the types of jobs that a child maybe engaged in, ruling out the worst forms of child labor. The law also requires insurance for the working child, provision of seven days more annual leave than the adult worker and setting a maximum of six working hours per day.

Egypt could achieve a 0.5-1.0 percent uplift in its RCI score by improving the law enforcement, and further upgrading labor practices to the levels exhibited in target countries. Two immediate opportunities include:

- Some sectors such as textiles are now vulnerable to mass lay-offs as a result of tightening global competition and reduced demand. There is an emerging body of good practice on more responsible ways to restructure, which offer useful lessons for Egypt;
- In common with many Complier countries, enforcement of health and safety regulations is a priority, and this entails continuous improvement of a team of workplace inspectors. The Egyptian Organization of Industrial Safety and Environment can also deepen its participation in the International Association of Labour Inspection (IALI).[30]

4.4.1.3 Business Climate

Previous chapters have noted the performance and challenges for doing business, as measured by the World Bank and IFC in their Doing Business reports. Among the key challenges for Egypt are the bureaucratic obstacles businesses face in paying taxes, which although not as extreme as Brazil's, are still a weak factor in the country's responsible business climate.

Egypt improved its international performance in economic freedom significantly from 1994 to 2008, as measured by the Heritage Foundation and The Wall Street Journal. Although the country suffered a modest reverse in its 2009 score compared to 2008, it is poised to join the ranks of 'moderately free' countries in the top half of the index if it can advance again next year by two points. This jump is achievable if Egypt makes progress in property rights and anti-corruption (the latter a shared commitment from government, business and citizens).[31]

Building a more responsible business climate has been and will remain a major focus for policymakers, with the potential for at least 1.5 percent uplift in responsible competitiveness performance. However, building a responsible business climate is not simply about reform of tax and other regulations. Policymakers also need to focus on supporting enterprises, for example:

- Create spaces for entrepreneurs to exchange ideas and find opportunities, either at a national, regional or sector-specific level. One interesting example is the 'matchmaking' event organized by the United Nations Industrial Development Organization's (UNIDO) Investment Promotion Unit (IPU) in November 2008 in Cairo, where more than 110 companies interested in replicating innovative agribusiness solutions held 350 bilateral meetings. Potential partners found common interest in access to finance, technology transfer and trade capacity building;[32]
- Promote 'sunrise sectors,' such as in eco-tourism/responsible travel. Egypt already offers more holidays in this emerging sector than countries like Greece and Jordan, according to UK specialists, Responsible Travel, with noteworthy developments in the oasis resort of Siwa and along the Red Sea;[33]

[29] Child Law (law no. 12 for the year 1996, amended by law no. 126 for the year 2008).

[30] http://www.iali-aiit.org/iali/html_en/welcome.html

[31] http://www.heritage.org/Index/Ranking.aspx

[32] http://www.unido.org/index.php?id=6519&tx_ttnews[tt_news]=313&tx_ttnews[backPid]=6&cHash=9d4898e185

[33] http://www.responsibletravel.com/TripSearch/Africa_Middle percent20East/Country100089.htm

BOX 4.4: Egyptian Social Entrepreneur Assists Small Farmers in Menia with Business Development

Ahmed Dakrouri is a social entrepreneur, supported by the global Ashoka Foundation. He is empowering small farmers in some of the most impoverished districts of Menia, Upper Egypt, by developing a comprehensive agricultural system that produces international export crops which will dramatically increase farmers' income and revitalize entire regions. His aim is to transform subsistence level peasants into successful farmers making their own decisions about what to grow, how many acres to plant and what prices to accept.

The first element of his program is to create, in collaboration with the farmers, a new and comprehensive agricultural system. New crops for export, such as basil and fennel are harvested and processed to add more value. Specific examples of new export opportunities include: processing dried basil, extracting oils from crops and ultimately selling completely fresh crops via a continuous cold chain from the Upper Egyptian farm to the German supermarket. By having alliances and contracts with export customers, the profit from the middlemen will shift primarily to the farmers with a share going to Development Citizen Organization (CO) for social investments in the region.

The second element is to empower farmers to make their own decisions and to take control of their destinies instead of having the government or middlemen tell them what to do. Dakrouri has formed a Farmers' CO which includes every farmer who participates in the program. The group has begun organizing activities and acquiring greater agricultural skills and knowledge through technical courses taught by the farmers with successful experiences with the export crops. This rapid growth will not only improve the income of each farmer, but will create enough wealth in the region to enable more social and economic investment.

Source: http://www.ashoka.org/fellow/4315

4.4.2 The Role for Civil Society: Engagement

Harnessing the creativity of civil society in building responsible competitiveness is a challenge across the Arab World, as well as for countries ranging from Singapore to Bangladesh. Civil society engagement in the competitiveness agenda means more organizations (NGOs and media groups) are empowered to hold businesses accountable. It also means consumers are able to help companies innovate by demanding better, more sustainable products and services.

Egypt has one of the most sophisticated and influential media sectors in the region, while being carefully supervised. A confident media that understands business responsibility and is prepared to challenge wrongdoing as well as celebrate good practice is crucial to forming broader civil society engagement.

The Egyptian government has issued a number of laws and set up institutions that are still in their infancy, but certainly a step in the right direction. The Consumer Protection Law no.67 of 2006 guarantees consumer rights of health and safety during normal product use; rights to obtain correct information about purchased products; rights of free choice of good-quality products; rights to personal dignity and respect of religious values; rights to bring legal actions against violators of the above rights and to seek compensation. The law established the Consumer Protection Authority, as a public authority overseeing implementation of the law. The authority works with a roster of local consumer protection associations to implement the law.

Another important new law that compels businesses and markets to be fairer to consumers is the anti-monopoly law (Law no. 3/2005). The law regulates business actions of market dominating firms (firms having more than 25 percent market share). The Anti-Monopoly Agency was created by the law to oversee its implementation.

Egypt's potential in strengthening the social enablers of competitiveness is a significant three percent increase in performance, making this an essential part

of the country's responsible competitiveness strategy. Among promising initiatives that can be replicated or scaled-up:

- The Media Development Program (MDP) in Egypt, founded in 2006 as a public-private partnership, works with media companies and training institutes to improve professionalism and sustainability in the Egyptian media sector. The MDP has four principal objectives: to promote professionalism and training within the sector; to improve the economic sustainability of the sector; to improve the organizational and professional capacity of the sector; and to encourage media policy reform, supported by civil society movements like 'Kifaya.'[34]. Egypt can also learn from the successes of similar initiatives in countries like Brazil and Saudi Arabia. Groups like Instituto Ethos and Tamkeen are proactively engaging with journalists to provide training on key sustainability issues and networking opportunities.
- Despite the rising number of NGOs created in Egypt, many lack the funds and capacity to play an effective watchdog role.[35] Encouragingly, a number of NGOs are trend-setters and could serve as role models for others. Those include the Friends of the Environment (FEA), one of a few civil society advocacy groups in Egypt. This NGO, established in 1990, has won several court cases against the government and the private sector to protect Alexandria's environment. FEA works as a pressure group for environmental protection, taking participatory education and training its central focus. FEA furthers its goals through public hearings, peaceful processions/marches, negotiations and pressure and legal appeals. FEA is interested in creating additional advocacy outreach for its activities by passing on its advocacy strategies and methodologies to other grassroots organizations in Egypt.
- Another leading NGO is the Association for Protection of the Environment (APE) which helps some of the most disadvantaged groups in Egypt, garbage collectors, to capitalize on business opportunities in waste recycling. APE turned this informal community, the "Zabaleen" people, living in shacks in Cairo's most polluted areas with no educational or health services, into a medium for recycling waste on a commercial scale. They helped them to penetrate some of the most elite markets with unique designs of cards, carpets, patchwork quilts and other handicrafts. The NGO also offered health and educational services, training for women and a child care center for the community. A number of other NGOs have partnered with APE in serving the Cairo Zabaleen community, aiming to reduce emissions from solid waste burning. This is in addition to providing the garbage collector communities with adequate food, shelter and training. However, civil society engagement in the climate change debate is limited.

BOX 4.5: Hurghada Environmental Protection and Conservation Association (HEPCA)

HEPCA is committed to lobbying for changes to existing legislation and the introduction of new legislation to protect natural resources. The fight for maintaining the Giftun islands as protected areas and the decree banning shark fishing are examples of advocacy campaigns that have been led by HEPCA. In a five year period, HEPCA has succeeded in changing over 32 laws, articles and decrees. These include the designation of many reefs and islands throughout the Red Sea as protected areas.

In May 2007, HEPCA succeeded in obtaining a new decree from the Ministry of Agriculture and Fisheries to nullify a previous decree that allowed the fishing and exporting of colored reef fish to Europe and other international markets. HEPCA launched a far reaching campaign and worked with other agencies, enthusiastic individuals and major media representatives for this revision of the law.

HEPCA is working with the Governor of the Red Sea, to support a decree to free the Red Sea Governorate of plastic bags. Plastic bags pose a massive hazard to birds, turtles, dolphins and other marine creatures that are killed in alarming numbers each year after swallowing or becoming entangled in plastic bags blown out to sea.

Source: www.hepca.com

[34] Media Development Program (MDP) Egypt http://www.irex.org/programs/mdp/index.asp; Media Sustainability Index – North Africa and Middle East (2005) http://www.irex.org/programs/MSI_MENA/2005/MSI05_MENA_EG.pdf

[35] http://www.cipe.org/publications/fs/pdf/021709.pdf

4.4.3 From CSR to the Sustainability Opportunity

The financial crisis and global economic downturn are causing companies around the world to return to their core values. Responsible business strategies and sustainability are now beginning to pay off. According to a recent paper by consultancy firm McKinsey, "There is a growing, increasingly persuasive, body of evidence suggesting that companies with superior overall environmental management are better-managed companies overall, and thus enjoy above-average profits and stock performance."[36]

Businesses of all sizes in Egypt now have the opportunity to reinforce their core values to drive value creation, and there are at least three opportunities to meet sustainability in the areas of governance systems, environmental management systems and scaling-up their CSR activities. Making CSR deliver benefits is even more crucial in 2009, as many firms in Egypt, as is the case elsewhere, are facing intense pressure from their senior management to reduce the size of their CSR budgets.

4.4.3.1 Governance Systems

Significant improvements in corporate governance have been noted in Egypt in recent years, driven by capital market requirements.[37] Among recommendations made by studies such as the 2004 World Bank/IMF Corporate Governance Country Assessment were: the setting up of a Center for Directors, to help develop a code of corporate governance on the role, duties and functions of the board and the creation of a director of training capability. This has now happened in Egypt.

The country has the potential for at least a further one percent uplift in its responsible competitiveness by going further in its drive to promote good governance. Among the options:

- A continuous effort to ensure the systematic enforcement of new rules on listing and disclosure, which increasingly means not relying on the light regulatory culture favored by the US and UK, but moving towards firmer and more proactive supervision. The recent financial crisis will inevitably lead to significant new initiatives in corporate governance internationally, especially but not limited to financial sector regulation of incentives, risk culture and transparency of accounts.
- Combating corruption remains an important opportunity throughout many emerging markets, including Egypt. Although this scourge is difficult to benchmark, let alone stamp out, estimates by the Inter-American Development Bank are that it costs Latin American economies around 10 percent of GDP.
- The Arab Business Council is reviewing best practices in governance systems in the Arab world, which will generate some practical options including the potential alignment of governance systems more closely with international benchmarks like the OECD Principles.
- Companies to participate in sector-specific governance initiatives that develop guidelines like the UN Principles on Responsible Investment (PRI, finance), MFA Forum (textiles), META (medicine)[38], and Extractive Industries Transparency Initiative (EITI, oil, gas, minerals).

4.4.3.2 Business Environmental Management

Egypt comes in the top half of Yale and Columbia's 2008 Environmental Performance Index (71st out of 149 countries, up from 85th in 2006), in the same cohort as Jordan and Turkey, and within sight of European countries like the Czech Republic and the Netherlands. Egypt's position would rise significantly if it enhanced its environmental performance on only the climate change component of this composite index.[39]

Embedding environmental management in core business practices remains a challenge for many countries, including Egypt. The number of Egyptian businesses adopting ISO14000 (environmental standards) has declined compared to those adopting ISO9000. While ISO9000 certified business doubled between 2003 and 2007 in Egypt, the number of ISO14000 certified businesses dropped in the same time period by 15 percent[40]. The first task is to understand the key reasons why this conversion to ISO14000 is not occurring – cost, complexity or lack of demand in the supply chain – and to take steps to reverse the trend. Taking environmental systems to the next level gives the potential for at least 1 percent uplift in responsible competitiveness. Among the activities that will support that move are:

- Harmonize and apply Egyptian and international standards, under the remit of the Egyptian Organization for Standardization and Quality (EOS), notably ISO's environmental management system (ISO14001) and the new guidelines for corporate responsibility (ISO26001), and maintaining a public database of certified products and establishments[41];

[36] Climate Change and the investor, McKinseydigital, February 2009. Found at: http://whatmatters.mckinseydigital.com/climate_change/climate-change-and-the-investor

[37] http://www.worldbank.org/ifa/rosc_cg_egyp2.pdf

[38] Medicine Transparency Alliance. For more information see http://www.dfid-healthrc.org/MeTA/index.html

[39] http://yale.edu/epi/2006epi; http://epi.yale.edu/CountryScores

[40] 2007 ISO survey by the Int'l Organization for Standardization.

[41] http://www.eos.org.e g/Public/en-us/Quality/International+Systems+Achievers/

- Take to scale the energy efficiency code for new residential and commercial buildings, developed by the Ministry of Electricity and Energy in partnership with the Ministry of Housing. This code is mandatory and enforced by ministerial decree[42];
- Encourage more sustainability reporting among companies, through engagement with the best international practices embodied in initiatives like the Global Reporting Initiative, as well as through domestic sustainability awards, now happening across the Arab World (from the Saudi Responsible Competitiveness Index to Dubai's Arabia CSR Awards)[43];
- Develop initiatives that include fiscal incentives (eg. grants, tax rebates) for companies or industrial zones that achieve environmental certification or meet social standards; and expand the role of informal clusters, business clubs, sector associations and chambers of commerce in providing education, training and tools for SMEs.

4.4.3.3 Promoting Talent

There is the potential for at least a 0.5 percent increase in the RCI score by better supporting and promoting a talented workforce. This is especially the case given Egypt's strong demographic base. Options to promote the talent base include:

- Support initiatives to help align the skills agenda with business needs, like the Alexandria Business Association's work with the government since 1999 to support a more labor-oriented technical education system, strengthening the quality and relevance of training, and linking it more directly to entry-level jobs[44];
- Ensure equal pay for equal work and support gender-sensitive working arrangements. Egypt has a stronger record than some other countries in the region on ensuring that businesses draw from the skills offered by the female workforce, but additional efforts will further boost Egypt's RCI performance;
- Support initiatives that act as national information access points and can emphasize the importance and utility of web-based information to rural audiences. In 1998, the UNDP opened the first Technology Access Community Centers, a strategy aimed at integrating ICT into sustainable development. Today, the UNDP in partnership with the Ministry of Communications and Information Technology has expanded this initial program and now operates a range of initiatives in community telecenters including; ICT for Micro, Small and Medium Enterprises, ICT for Illiteracy and The Mobile ICT Unit. The large scope and various dimensions of this national strategy are particularly innovative and unique to Egypt[45].

4.4.4 Summary: From CSR Tools to Sustainability Strategy

As outlined above, a responsible competitiveness agenda for Egypt is more ambitious than just promoting corporate social responsibility. CSR is a term that is widely used in Egypt, covering a wide range of approaches and activities. While its scope is expanding, it most commonly refers to corporate philanthropy[46], with a growing focus on voluntary business actions in environmental and social management systems and basic codes (common in Complier countries). Among Asserters and Innovators, businesses begin to integrate social and environmental goals into their core operations, actively supported by the government and receptive to the desire and demands of civil society. This can be captured by the term sustainability.

Sustainability is the integrated management of economic, environmental and social performance with the aim of creating maximum value for both the business and its stakeholders. Sustainability management is active at the Asserter level, and particularly the Innovator level. For Egypt to shift from Complier to Asserter, the business community must evolve its current understanding of CSR, towards adopting sustainability management in its core operations. Although we have not assessed the potential cumulative effect, this is the single-most effective overarching action that could be taken by Egyptian business to both enhance responsible competitiveness and contribute to sustainable development. The following table helps capture the difference in approach between traditional CSR practices and the sustainability management approach:

[42] Ministry of Electricity and Energy; Egyptian Electricity Holdings Company, Annual Report 2005-2006
http://www.moee.gov.eg/English/eng-takrir2005-2006.pdf

[43] http://rci.org.sa; http://www.arabiacsrawards.com/newsdetails.php?nid=381

[44] http://www.unido.org/fileadmin/import/69447_CSRI_08.pdf

[45] Sustainability Revisited; Egypt IT Clubs; Karim Kasim and Purvi Shah Telecentre Magazine; September 2008
http://css.escwa.org.lb/ictd/17-19DEC08/d1.pdf

[46] Iskander, L. 2007. Business Solutions for Human Development. Report by UNDP/Egypt and the Ministry of Investment.

Table 4.1: ***The Breakthrough Opportunity – Shifting Business Mentality from CSR to Sustainability***

Responsible Competitiveness Cluster	Old approach: CSR		New approach: Sustainability	
	Starter	Complier	Asserter	Innovator
Summary	Focus on philanthropy and investment in community	Compliance with law; beginning of achievement of management system certificates	Focus on performance enhancement; better response to wider range of environmental and social issues affecting business value	Strategic level impact. E.g. Product/service innovation that incorporates environmental/ social advantages
Strategic Orientation	Unrelated or peripheral to business strategy	Risk mitigation	Increasingly recognize benefits to both risk mitigation and opportunity creation	Core to business strategy, product and service innovation, and value creation
Planning Orientation	Ad-hoc community philanthropy	Structured philanthropy	Stand-alone corporate responsibility department	Integrated across business planning
Level of Concern	Assigned lower managers	Specialized middle managers	Culture of sustainability begins to spread throughout organisation	Senior management, board, and throughout
Value Proposition	Give back to society, some reputation	Harm/risk mitigation, reputation management	Cost reduction, risk reduction,	Next wave of human innovation, core driver of economy, next mega-trend opportunity
Management Orientation	None	Meet baseline regulatory requirements or certificate requirements	Performance focus	Next step in management excellence
Policy Environment	Government policies are narrowly focused on setting minimum environmental, economic and social performance levels; minimum enforcement leads to consistently poor business performance		Government policies can support transition to sustainability as a competitive advantage. Businesses aim to operate at many times above regulatory levels, focus is on policies that strengthen competitive advantages versus worst offender baselines	
International Standards	None	Are adopted to achieve certificates and reputation	Are integrated into the company's value proposition	
Impact of Financial Crisis	Community philanthropy reduced	Number of certifications decreases / delayed.	Good governance, operational efficiencies, higher productivity, client loyalty all contribute to relative outperformance against peers	Stand-out integrity attracts new clients; company able to invest/ innovate to serve market, while competitors stuck

Source: Author's analysis

4.5 RECOMMENDATIONS: TOWARDS A NATIONAL STRATEGY FOR EGYPT

This chapter has reviewed Egypt's competitiveness challenges and opportunities through the lens of responsible competitiveness. The conclusion is that Egypt is well positioned to make significant progress in enhancing its responsible business practices. In doing so, Egypt stands to benefit from a significant uplift in competitiveness, innovative capacity and talent – all strong predictors of increasing wealth per capita. It will also improve environmental performance, with associated quality of life benefits.

Indeed, a number of new initiatives and institutions have been set up to promote sustainable development. In parallel, a culture of business responsibility is proliferating in Egypt. Those are indications of progress towards responsible competitiveness. However, Egypt's next stage of development is for its local markets to reward responsible behaviour of firms. This implies local pressure on firms to innovate in the area of environmental protection and to respect worker and consumer rights.

How can these diverse initiatives collectively advance responsible competitiveness? This requires an agenda of concerted efforts.

A ***National Sustainable Development Strategy*** (NSDS), sets the stage for effective action towards responsible and sustainable competitiveness. It is based on the concept of "strategic and coordinated action towards operating an adaptive system that continually improves." A NSDS is a process rather than a document. It is not a government plan, but rather a forum where the combined innovations from government, the business sector and civil society will yield goals and strategies that enhance sustainable development.

A NSDS is an appropriate forum for addressing many of the impending challenges facing Egypt's progress to a more responsible competitiveness, as well as planning for and implementing the following recommendations:

1. Adopt policies to enhance performance of sustainable markets

The potential size of sustainable markets is much greater than what Egypt has realized to date. They promise greater employment opportunities and an increased contribution to economic growth. However, their expansion depends on enabling policies. More specifically, the government needs to push forward the specific below-mentioned policies in order to realize progress in the areas of sustainable agriculture, clean energy and sustainable industry.

- **Reward responsible behaviour by encouraging greater utilization of the Clean Development Mechanism:**

  The Clean Development Mechanism (CDM) represents an opportunity for expanding sustainable agriculture, if the government gains approval by the Conference of Parties of the United Nations Framework Convention for Climate Change to include sustainable agriculture alongside forests, afforestation and reforestation projects under the CDM. This would enable agriculture-based countries, such as Egypt and other African nations, to benefit from returns on carbon trading. The additional income generated for farmers under CDM would represent a financial incentive for wider adoption of sustainable practices.

The Clean Development Mechanism (CDM) is an arrangement under the Kyoto Protocol allowing industrialized countries with a commitment to reduce greenhouse gas emissions to invest in projects that reduce emissions in developing countries as an alternative to more expensive emission reductions in their own countries. Under this mechanism, projects that reduce carbon emissions, such as energy efficiency, or increase carbon sequestration, such as afforestation, would be allowed to sell "carbon credits" to purchasing industrialized countries.

The CDM is supervised by the CDM Executive Board under the guidance of the Conference of the Parties of the United Nations Framework Convention on Climate Change.

Source: http://unfccc.int/kyoto_protocol/mechanisms/clean_development_mechanism/items/2718.php

Agriculture is now a major carbon emitter, due to unsustainable practices such as burning of agricultural waste and the use of polluting liquid fuels in the operation of agricultural machinery. However, transformation to sustainable agriculture means a transformation from a carbon emitter to a carbon sink. According to FAO (2007), sustainable agriculture in 48 developing nations has the potential of mitigating the emissions of 390 gigatons of carbon dioxide equivalents over 10 years[47].

In general, programs by the government to inform people of the CDM would have a positive impact, not only on agriculture but also on wider use of renewable energy, energy efficiency and sustainable industry. Mechanisms could be included to ensure that the CDM application is carried out to benefit SMEs in an equitable manner.

- **Enhancing consumer protection:**

  The reason behind the expansion of global green markets is largely consumer demand. As consumers become more aware of the benefits of green products and the threats posed by unsustainable production practices on their societies, they tend to demand environmentally friendly products. However, this important market driver will not flourish in Egypt without a mature system for consumer protection. Egypt's recognizable efforts to date in the area of consumer protection need to be harnessed to serve the environmental sector.

- **Price reforms and anti-monopoly policies**

  As demand for energy increases, continuing to subsidise and secure hard currency for fuel will be an unreasonable burden on the government. The government is planning to reduce subsidies on heavily polluting fuels over the coming few years. This will automatically expand the energy efficiency and renewable energy market in Egypt. Egypt's current share of this 1000 billion euro market is negligible. The United Nations Environment Programme estimates that about 20 million jobs will be created in this market alone worldwide. Egypt's share of this growing job market will also likely grow.

  Fear that removal of energy subsidies will increase local prices can be mitigated by ensuring that antimonopoly measures are taken. The efforts that the government made in this area are commendable and should be strengthened particularly as major macroeconomic reforms are implemented.

- **Targeted subsidies/fiscal incentives**

  Savings from energy subsidies, which have so far mostly benefited the rich, should be redirected to more targeted uses. An efficient and expanded food subsidy system should be given priority. Also, fiscal incentives for the benefit of sustainable production should be considered. Various schemes are currently available in the agriculture sector such as soft loans to farmers and subsidized services such as soil testing and land improvement services. Subsidies exist for the industry and agro-industry sector through the Industry Modernization Program that provides technical assistance, facilitates access to finance, and provides targeted financial transfer for equipment purchase. Successful targeted subsidies need to continue until they achieve their intended goals.

2. Promoting business action

Business action is not only investment but also innovation. It has been proven that, when markets reward responsible behavior, firms, irrespective of their size, tend to invest in innovative ways to become responsibly competitive. Much of Egypt's competitiveness depends on business action. Business action can benefit significantly from:

- Greening the supply chain: as suppliers receive assistance from their – mostly larger – clients to enable them to respond to market responsibility demands.
- Business development services: services that are provided by the business sector for the business sector to enable it to position itself well in the local and global markets. As firms adopt new practices in the areas of responsibility they will need further guidance on how to re-position themselves.
- Sustainability reporting: meaning firm-level transparent disclosure of its performance in the area of responsibility. This allows businesses to compare themselves to peers and competitors and make plans accordingly.

3. Enhancing labor competitiveness

Realizing Egypt's competitiveness potential depends in large part on a well-functioning labor market. Egypt needs to take various steps in this area including:

- **Enhanced higher education and on-the-job training for environmental service providers**

  Egypt's advancement in the world market is limited by the quality of its higher education. Despite the richness of Egypt's demographic base, the required cadre of environmental service profession-

[47] FAO. 2007. The State of Food and Agriculture: Paying Farmers for Environmental Services.

als is limited. Higher educational establishments do not include environmental services as part of their curricula, as the subject is fairly new and they do not have a sufficient faculty to cover the subject. Faculties of Agriculture are a case in point, as the rate of enrolment has significantly gone down in recent years, even though higher education in agriculture has received donor support in recognition of the sector's strategic importance for Egypt. Similarly, energy service providers who can conduct energy audits and design cost effective energy efficiency schemes are very limited in the local market. Demand will increase for those services as the above policy agenda is implemented. It will also increase in the region as countries advance, thereby creating significant opportunities for outsourcing environmental services to Egypt. Those opportunities cannot be realized unless support is extended to higher educational establishments and in-service training to ensure the quality of services provided on the market.

4. Proper enforcement of the labor law

Education and training are only two prerequisites for Egypt's competitive labor markets. Other important working conditions are realized and embodied in the new labor law, such as setting minimum wages; requiring fair and equitable treatment irrespective of religion, gender or race; and regulating child labour among others. Measures to enforce occupational health and safety standards are an essential component of responsible competitiveness. Enforcement of those measures is of utmost importance to allow Egypt to properly utilize its demographic resource base and to progress on its path to international competitiveness.

ENCC FRAMEWORK FOR GREATER INTERNATIONAL COMPETITIVENESS

3. Responsible Competitiveness

Past decades have seen decision makers become increasingly concerned with mitigating the social and environmental ramifications of economic growth and urbanization. Sustainable development, placed on the agenda of the international community in 1987 through the Brundtland Report, has been the paradigm used to balance conflicting social goals, particularly for developing countries where immediate needs brought about by high levels of poverty, unemployment and disease have shortened planning horizons. Today responsible competitiveness offers countries like Egypt a new framework through which to turn mounting threats such as climate change into opportunities for growth. Responsibility is all about innovation, ingenuity and resourcefulness — maximizing productivity while simultaneously preserving resources and ensuring a more equitable distribution of gains. Green industries like renewable energy, sustainable agriculture, eco-tourism and new forms of industrial ecology offer vast and underexploited potential for value added. With more integrated thinking and coordinated action, Egypt could leapfrog ahead to be a global frontrunner in any one of these promising industries.

4.6 CONCLUSIONS

It is clear from the nature of the recommendations above that they cannot be implemented single-handedly by one ministry or even through the actions of the government alone. They require Egypt to harness all of its innovative powers in order to come up with creative solutions and means of implementation. This requires a forum that will provide freedom and authority to the various stakeholders to come up with solutions and implement them, backed up by the government. The authority of government, the innovation and investments of the business sector and the watchful eye of civil society are all essential ingredients in the recipe for Egypt's competitiveness.

This is the new power that a National Sustainable Development Strategy would bring to the picture. The benefits of this paradigm shift are numerous. They include but are not limited to:

- A new framework, replacing the National Environmental Action Plan, which was founded initially as a means to implement the law, but ended up as an ambitious list of projects that the government is expected to carry out with limited resources.
- More active engagement of all stakeholders (government, business and civil society). New challenges such as climate change require entirely new policies and partnerships. Egypt will want to develop its own vision for a low-carbon prosperity plan.
- New activities to promote industry innovation and collaboration, helping Egypt to meet environmental standards while capitalizing on multi-billion pound markets that will enhance investment and create employment opportunities.
- New strategies and programs to be collaboratively developed, such as sustainable trade strategies. Nations are looking to export collaborative standards for products meeting particular environmental criteria, with countries like China, India and South Africa recently announcing new standards or product labels in the areas of forestry, green buildings and fair-trade wines. AccountAbility's work with Chinese partners on a Sustainable Trade Strategy for China has demonstrated how this type of labelling can build trust in brands, influence the perceptions and actions of international consumers and increase foreign direct investment. Egypt has an opportunity to build on its internationally acclaimed status as one of the world's most recognizable national brands by adopting this type of labeling system.[48]

By initiating its own NSDS process, Egypt can benefit from other countries' experiences, such as the United Kingdom and South Africa, as well as from its own rich portfolio of initiatives and policy measures identified in this chapter. Strategic coordination significantly improves the policy coherence and systems integration across overlapping mandates. This is therefore a foundation which could enable Egypt to make a leap from the Compliers cluster, into the Asserters and in some areas, possibly into the Innovators cluster. Other countries that have succeeded in this transition have benefited from very significant economic, social and environmental upsides.

The success of the NSDS relies on the seriousness of the exercise. Successful NSDS processes occur when countries align the budgetary process as well as trade and investment plans to the NSDS, to ensure that government and civil society resources are well mobilized and business investments are soundly made. In short, the NSDS is a comprehensive approach that demands high level strategic leadership; excellent systems (legislative underpinning, links to the budget process and independent benchmarking and monitoring); and thorough processes to engage stakeholders (civil society groups and linkages to the sub-national and sectoral levels).

To conclude, Egypt has real potential to advance its global competitiveness. The country's success in doing so will to a significant extent be determined by its ability to convert the competitive challenges it faces into sustainability opportunities. In this chapter, the responsible competitiveness framework was used to help assess these opportunities. This benchmarking makes the case for strong coordination of the three key influences on national performance: policy drivers, business action and an engaged civil society. This is an agenda of continuous benchmarking allied to an ambitious national strategy. It is to be hoped that Egypt seizes this opportunity to advance.

[48] Egypt named again as the world's best brand for history, Travel Daily, December 2008. Taken from: http://www.traveldailynews.com/pages/show_page/28256; AccountAbility's China's Sustainable Trade Strategy: Market Mechanisms to Promote Sustainable Trade is currently unpublished.

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[49] Views expressed in this report are solely those of the author and do not necessarily reflect the position and policies of the World Food Programme or the United Nations.

ANNEX

EGYPTIAN NATIONAL COMPETITIVENESS COUNCIL

Led by a group of prominent Egyptian business leaders and academics, the Egyptian National Competitiveness Council (ENCC) is the first non-profit, non-governmental organization dedicated to competitiveness in Egypt. It was launched in February 2004 to shed light on the issue of national competitiveness and enhance Egypt's performance. The ENCC aims to become an instrument of influence on government policies, business climate rankings and public attitudes to make the nation's institutions more globally competitive. The council has the following objectives:

1. Identify, benchmark, monitor, and evaluate Egypt's regional and international competitiveness ranking to determine recommendations that will improve the standards of living for all Egyptians and create a world-class business environment and productive people.
2. Create and release periodical reports on competitiveness rankings that will guide Egypt's development.
3. Communicate and cooperate with stakeholders to create awareness of the competitiveness of Egypt.
4. Initiate and promote sector competitiveness with the aim of raising incomes and improving Egypt's business climate.
5. Help identify and highlight emerging competitiveness and sustainable development issues of national importance.

SUB-COUNCILS

This year the ENCC established three sub-councils: the Travel and Tourism Competitiveness Council, the Human Resources Competitiveness Council and the Agriculture Competitiveness Council.

I. THE TRAVEL AND TOURISM COMPETITIVENESS COUNCIL (T&TCC)

The Egyptian travel and tourism sector contributes an estimated 11.3 percent of Gross Domestic Product and 12.6 percent of national employment. Its importance to the Egyptian economy and large growth potential led the ENCC to dedicate a chapter to it in the Fifth Egyptian Competitiveness Report. The T&TCC was subsequently created to disseminate and build upon the findings of the report and advance the policy recommendations it put forth. In addition, the sub-council's creation was in response to Egypt's low ranking in the World Economic Forum's (WEF) Travel and Tourism Competitiveness Index. Egypt placed 66th out of 130 countries in 2008, down from 58 out of 124 countries in 2007.

The sub-council brings together stakeholders from the travel and tourism sector, including high-profile leaders from the government, academia and private sector, to review recent developments, discuss challenges and propose strategies to enhance its international competitiveness. The mission of the T&TCC is "to assess the factors impeding the enhanced competitiveness of the sector, and suggest solutions for dealing with these impediments. This is done through spreading awareness (inside and outside the sector), advocacy and mobilizing efforts, in cooperation with other stakeholders."

The T&TCC's most recent action plan is outlined in a special chapter in the WEF's 2009 Travel and Tourism Competitiveness Report where Egypt ranked 64 out of 133 countries. The proposed strategy addresses the industry's most salient needs based on the Travel and Tourism Competitiveness Index. The index, a foundation for the sub-council's action plan, provides a closer look at specific deficiencies and obstacles that must be overcome. Based on its findings and the input of industry experts and council members, three main priority areas were identified. These are:

1. Human Resource Development
2. Institution and Capacity Building for Industry Advocacy
3. Environmental Sustainability

Under each of these headings a number of initiatives and activities have been selected for the upcoming year. Short-term tasks related to human resource development will include increasing institutional coordination and assessing the sector's human resource needs. Long-term initiatives will focus on the industry enablers, sector research and monitoring, curriculum design and training provision. Industry advocacy will be tackled through awareness workshops and institutional support to the Supreme Council of Tourism Travel and the proposed Tourism Modernization Center. Finally, a special fund will be created to help promote environmental sustainability in the travel and tourism sector alongside awareness raising seminars and workshops. The chapter noted that the Egyptian experience is not unique and that similar efforts could be replicated in other countries to improve the performance of travel and tourism sectors.

Most recently the T&TCC prepared an update report on the performance of the travel and tourism sector. Authored by Professor Adla Ragab, member of the T&TCC and Economic Advisor to the Minister of Tourism, the report credited the slight improvement in Egypt's ranking in the 2009 Travel and Tourism Competitiveness Report (from 66 out of 130 countries in 2008 to 64 out of 133 countries in 2009) to price competitiveness, government prioritization, affinity to travel and tourism, number of operating airlines, visa requirements and time required to start a business. Areas of decline included enforcement of environmental regulations, poor infrastructure (reflected in road and airport density) and poor-quality human resources. Modifications to this year's ranking methodology were made in order to greater reflect regional contexts — in line with requests made by Egypt among other countries at the 2008 World Economic Forum on the Middle East. However, there is still a need for revised hard data collection techniques than can better reflect the provision of services in Egypt. Finally, the report suggested that reform should continue to focus on the key areas of weakness such as human resource and infrastructure development, as well as increased ministerial coordination to foster more sustainable tourism development.

II. THE HUMAN RESOURCES COMPETITIVENESS COUNCIL (HRCC)

The mission of the HRCC is "to raise awareness, stimulate efforts, and take initiatives to enhance the competitiveness of Egyptian human resources — as a major efficiency enhancing factor in the aggregate competitiveness of Egypt." In other words it seeks to increase understanding, suggest policies and initiate projects that enhance Egypt's human resource competitiveness. This role has become especially important after the 2007-2008 Global Competitiveness Report indicated that weak capabilities of human resources were contributing to Egypt's low competitiveness rank. According to the report, Egypt's ranking in higher education tumbled by 22 places, from 80th to 102nd place. An "inadequately educated workforce" was cited as one of the biggest problems to doing business.

Education at all levels is essential to human resource development, however, the HRCC chose to focus its 2008-2009 activities on higher education. This is because of the unique role played by higher education in creating a skilled workforce and a knowledge economy. Next year, the council will address vocational education and training. At present, the council is spearheading efforts to create a national ranking system for Egyptian universities based on the competitiveness of the graduates they produce. The ENCC is motivated by a lack of independent information in the marketplace on the quality of specific programs. In the midst of expected increased unemployment, businesses face fierce competition for a scarce supply of graduates with proper skills. Better information on the education market in Egypt will aid employers and motivate universities to be more attuned to their needs. This information would help prospective students and pressure institutions of higher education to compete more rigorously. The rankings will also raise the profile of higher education on the nation's economic reform agenda. Initially the ranking system will include the departments of computer science and communication engineering to be expanded upon successful completion of the pilot project. A total of 20 indicators have been selected to evaluate these two programs across the nation's universities related to the quality of academic programs, linkages to industry and the relevance of graduates' skills to the marketplace.

The ranking will be based on indicators for which data is reliable and available. Recognizing that an independent ranking of universities is only one of many ways to gauge university performance, widely used indicators of quality will likely be the easiest to monitor and provide the greatest degree of reliability. Input from academia, government and business will be sought before proceeding with data collection to aid the design and methodology. The Soundness Committee was formed to provide greater stakeholder involvement in the ranking project. It includes Prof. Ali Eldin Helal, Prof. Hussein Kamel Bahaa Eldin, Prof. Sami Abdel Aziz, Prof. Hisham El Sherif, Dr. Adel Danish, Dr. Adel Goher, Mr. Omar Mohana, Mrs. Lola Zaklama and Prof. Ahmed Gamal Eldin. Their first meeting was held to evaluate the indicators and resulted in the addition of several new ideas for the ranking project.

International experience also provides several important lessons to guide the HRCC approach in order to make the ranking exercise beneficial to universities, students, employers and the public at large. The HRCC examined lessons from the US, Europe, Africa, Asia and Latin America, across countries at various stages of economic development. The following principles guided the HRCC's development of indicators: the ranking system must be transparent, use a range of indicators and compare similar programs rather than a university-wide weighted score, be aligned with existing quality improvement initiatives and have simple, objective indicators.

III. THE AGRICULTURE COMPETITIVENESS COUNCIL (ACC)

The ACC was recently created by the ENCC. The new sub-council will focus on issues concerning the progress and competitiveness of Egypt's agriculture sector. In particular it will address several ongoing problems faced by the sector, as well as new challenges as they emerge. Sustainable agriculture is expected to be an important area of discussion given the sector's sensitivity to environmental conditions, as well as its potential for climate change mitigation as a carbon sink. The emerging global food-security crisis has also increased the topicality and importance of establishing an Agriculture Competitiveness Council. Due to the presence of comparative advantages such as land and water resources, Egypt is a prime position to capitalize on growing food demand. But it must first transform its agriculture sector into a source of competitive advantage, a task to which the ACC will dedicate itself.

The present volume of the Egyptian Competitiveness Report (ECR) includes a special chapter on agricultural competitiveness. The sub-council will work on advocating the recommendations announced in this report and setting a more elaborate action plan for the sector. Areas of concern highlighted in chapter 3 of the ECR that need to be addressed include inefficient resource use, high land fragmentation, contamination and institutional inefficiency among others. Like the T&TCC and HRCC, the ACC will reach out to a range of stakeholders to foster awareness, dialog and action. The sub-council has already elicited the support of several influential persons within the sector.

PUBLICATIONS

One of the ENCC's primary activities is the annual release of its flagship publication, the Egyptian Competitiveness Report currently in its sixth year of publication. The report provides an in-depth look at national strengths and weaknesses amidst changing global political and economic landscapes. It also builds on the Global Competitiveness Index, the main competitiveness methodology of the World Economic Forum, offering a critical assessment of Egypt's ranking. Specific sectors or issues discussed in more detail by the report have included industry and manufacturing, SME's and travel and tourism. Authored by prominent scholars, the ECR is a key source of data and information for policymakers, researchers and civil society organizations.

In addition to its annual report, the ENCC will be publishing a series of policy briefs titled Toward Competitiveness. Each brief tackles a different issue related to national competitiveness. The first brief is based on the findings of the November 2008 workshop, "Higher Education Finance and Competitiveness: Lessons and Methods." The author, Mr. Andrew Lewis, is Education Team Leader at the United States Agency for International Development's (USAID) Technical Assistance for Policy Reform II Program in Egypt. Higher education is considered a fundamental pillar of economic competitiveness because of its role in ensuring more even and equitable growth, but also as a critical ingredient in any national system of innovation. It is concluded that a more effective and equitable higher education system hinges upon several key reforms especially with regards to financing. In particular, Mr. Lewis shows how more diversified sources of funding, can be a way to improve quality, free up national resources for scholarships and increase institutional autonomy.

Dr. Ashraf El-Araby, Economic Expert at the Center of Comprehensive Policy Studies at the National Planning Institute is the author of the second policy brief, "Productivity and Competitiveness of the Egyptian Economy." The brief explores the idea of competitiveness as function of productivity rather than resource endowments or relative advantage. It synthesizes the view that a more productive economy is the only way Egypt can move forward in the global economy. According to Dr. El-Araby this will require political will as well as cross-cutting comprehensive strategies at a national level. Most importantly, human resource development needs to become an absolute priority for Egypt. The brief's eight key recommendations stress the need for illiteracy eradication, upgrading of educational quality, and greater higher education and training as part of a national strategic vision to boost productivity.

The third policy brief will be authored by His Excellency Dr. Mufid Shehab, Minister of Legal Affairs and Parliamentary Councils. His analysis sheds light on how the modernization and development of the legal policy could open the gate toward competitiveness. Dr. Shehab argues that Egypt needs to overcome many of the existing institutional rigidities and begin filtering national legislations using the rubric of competitiveness. Key recommendations within this policy brief include: increased consideration of socio-economic ramifications of new legislation, more interdisciplinary legal training at Egyptian law schools, and greater legal innovation and modernization.

WORKSHOPS

The analysis and recommendations of ENCC policy briefs are based on workshop discussions that bring together Egypt's top scholars, government officials and business leaders. Four workshops have been held to date. The topics were Financing Higher Education; Productivity and Competitiveness of the Egyptian Economy; Logistics and Competitiveness of the Egyptian Economy; and The Global Financial Crisis and the Egyptian Labor Market.

The quality of higher education is one of the fundamental pillars of a nation's economic competitiveness. Business leaders know that a key — perhaps the key — to success is the quality of the workforce. The ***"Financing Higher Education"*** workshop was held on November 18, 2008. The speakers included international experts Professor Stephen Heynmenn, Professor of International Education Policy at Vanderbilt University and Professor Bruce Johnston, Professor Emeritus of Higher and Comparative Education at State University of New York. Professor Heynmenn's presentation "International Competition in Higher Education: Implications for Egypt" examined recent global changes in higher education as they relate to access, quality, managerial in-

novation, transparency, accountability, equity and diversity of finance. He emphasized several characteristics of competitive education systems in OECD countries like the United Kingdom, United States, France and Germany. Professor Johnston reiterated several of these points in light of Egypt's higher education system. His presentation "Cost-Sharing in Higher Education: Options for Egypt" brought attention to the need to reduce political opposition currently facing tuition levies and provide suitable financing options. There needs to be reform of higher education governance and financing to ensure better equity for the disadvantaged and better quality for all. Four tangible, near-term steps the government can take to prepare for a future in which students, parents and the private sector will be asked to share the burden of financing higher education include: 1) diversifying sources of finance including expanding the number of private non-profit institutions; 2) targeting public scholarships to students; 3) introducing tuition in national universities along with means-tested student loans; and 4) increasing university autonomy.

The second workshop ***"Productivity and Competitiveness of the Egyptian Economy"*** was held on December 24, 2008. Dr. Ashraf El Araby, Expert at the Macro Policies Center in the Institute for National Planning, presented an overview of "Productivity and Competitiveness." He examined Egypt's current performance and major challenges facing the country's productive capacity. He argued that improved workforce productivity is a crucial step in raising competitiveness. In addition to improving the quality of Egypt's education system, this requires a significant increase of investments in employee training and capacity building. Engineer Hesham Wagdy Abdel Dayem, Director of Technical Assistance & National Programs at the Industrial Modernization Center presented "Productivity and the Manufacturing Process." His remarks focused on the strengths and weaknesses of Egypt's manufacturing sector where, despite recent technological advancement, human resources continue to be inadequate. Final comments and analysis were given by Professor Mohamed Fathy Sakr, Professor of Economics at Cairo University and Advisor to the Minister of Economic Development. It was concluded that several reforms within the education system, local industry and the regulatory framework need to take place before Egypt can reach its productive potential and that only a multifaceted, multi-stakeholder action plan can break the self-reinforcing cycle of low national productivity.

"Logistics and Competitiveness of the Egyptian Economy" was the title of the third workshop held on January 13, 2009. The first of three keynote speakers was Dr. Essam Sharaf, President of the Arab-African Association for Logistics and Transport and Former Minister of Transportation. His presentation, "Transportation, Logistics and Competitiveness," stressed the historical and contemporary importance of the transportation and logistics sectors in Egypt. A brief word from Mr. Abd AlRahaman Awad, Deputy-President of the Arab-African Centre for Marketing and Consulting, provided commentary on Dr. Sharaf's presentation followed by Dr. Farouq Shaqweer, Ex-Executive Director of the African Development Bank, who elaborated on the origins and importance of competitiveness to the Egyptian economy. Finally, Dr. David Maunder, Executive Manger of the Chartered Institute of Logistics and Transportation International, gave the presentation "Developing Human Resources to Achieve Competitiveness in Logistics and Transportation." The main message was that logistics and transportation sectors have a lot to gain from more qualified human resources. The workshop discussion led to the conclusion that the transportation and logistics sectors are both critical to competitiveness and have massive potential for growth. However, Egypt lacks the capital investments and government regulation needed to fulfill this promise.

The most recent workshop, ***"The Global Financial Crisis and the Egyptian Labor Market"*** was held on March 22, 2009. Deputy Director & Lead Economist of the Egyptian Center for Economic Studies, Professor Naglaa El Ehwany, was the first presenter. Her presentation "Current Imbalances in the Egyptian Labor Market and the Potential Impacts of the Financial Crisis" outlined a few of the major challenges facing the labor market in light of global economic downturn. Ms. Dorothea Schmidt, Employment Specialist at the International Labor Organization, followed with a presentation titled, "Measures taken Worldwide to Mitigate the Impact of the Global Financial Crisis on Labor Markets." Her recommendations targeted both unemployed and employed segments of the population. She noted that any measures must be adapted to country needs and means and involove the government, workers and employers. Ms. Iman Zakaria, head of the vocational training unit at the Ministry of Manpower and Immigration, spoke in lieu of Her Excellency Ms. Minister Aisha Abdel Hady. She noted several of the effects of the financial crisis on the labor market and reiterated the ministry's commitment to creating employment and maintaining stability. Finally, Mr. Adham Nadim, Executive Director of the Industrial Modernization Center, gave final remarks on the role of the private sector in managing the labor market.

THE BUSINESS ADVISORY COUNCIL (BAC)

The BAC is a mechanism launched by the ENCC to capture private sector views on Egyptian regulations and inform the regulatory reform process under the Egyptian Regulatory Reform and Development Activity (ERRADA) initiative. ERRADA operates under the Sub-Cabinet Committee of the Productive Sector, chaired by the Minister of Trade and Industry, His Excellency Eng. Rachid Mohamed Rachid. The aim of the initiative is to build an Egyptian regulatory management system of public-private institutions, based on openness and fairness and with the ultimate goal of promoting a competitive economy.

In the current stage, the initiative includes 11 ministries (trade and industry, investment, finance, petroleum, tourism, housing, transport, agriculture, health, administrative development and local development). Twelve units were established in these ministries, overseen by a central coordinating unit. Each undertook an inventory of business related regulations that lie within the scope of their functions and activities. To date, around 28,000 business related regulations have been compiled and placed on ERRADA's electronic database in preparation for their review. A pilot is also being launched in three governorates (Red Sea, Ismailiya and Fayoum) to compile and review business related regulations. The aim of the Review stage is to streamline the existing stock of regulations in order to make them more business-friendly. This is achieved through a process of systematic review which involves examining regulations and producing recommendations to keep, amend or abolish. It is anticipated that half the regulations of participating ministries will be reviewed by June 2010.

The ENCC will continue to coordinate between ERRADA and the private sector throughout the official review stage which began on January 1, 2009. Over time, the ENCC will establish a system for on-going business consultation that will regularly incorporate private sector input into the process of issuing new laws and regulations through regulatory impact assessment (RIA). RIA aims to improve the quality of regulation as policy-making is evidence-based. Regulators are required to analyze and measure the socio-economic impacts, affecting predefined areas, of any proposed regulations. Analysis of proposed regulations should allow for comparative evaluation of options by different stakeholders including regulators and business community representatives.

STAKEHOLDERS AWARENESS CAMPAIGN

A series of public awareness events was launched in March 2009. The series includes special workshops and training programs for various target groups and stakeholders. The aim is to enhance general understanding of competitiveness and inform each group about their role in enhancing the competitiveness of the entire economy.

The first event, a three-day capacity building workshop for media professionals, was held in Ain Sokhna from March 12-14. The topics covered included an introduction to the theoretical framework of national competitiveness and its measurement through the World Economic Forum's Global Competitiveness Index. It included sectoral highlights on the tourism, construction, communication and IT sectors. In addition to ENCC staff, 41 individuals attended a total of nine sessions. Speakers included professors from the Faculty of Economics and Political Science at Cairo University, top media professionals and representatives from the Information and Decision Support Center (IDSC) and Ministries of Tourism and Communications and Information Technology. The workshop was widely covered by the media with more than 30 articles published in the local press.

The second event was for Egyptian parliamentarians. This target group was selected due to the persistence of legal and institutional impediments to Egyptian competitiveness. The workshop, held in Ain Sokhna on April 9-11, addressed the effectiveness of the existing regulatory framework in fostering productivity and economic development. Emphasis was placed on specific issues including the competitiveness of the Egyptian education system, labor market and social security programs. The sessions also stressed the need for policy reform and a national competitiveness strategy spearheaded by the government. His Excellency Dr. Mahmoud Mohieldin, Minister of Investment and His Excellency Dr. Mofeed Shehab, Minister of Legal Affairs and Parliamentary Councils, both attended and spoke at the workshop. Other speakers included distinguished professors and parliamentarians from the People's Assembly and Shura Council representing diverse political parties. Feedback from the event was very positive and signaled a strong interest in continued dialog. There was particular interest in the issue of education reform and human resource development as priorities for competitiveness.