American Chamber of Commerce in Egypt

Impact of the Economic Crisis on Trade, Foreign Investment, and Employment in Egypt

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Arne Klau

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Impact of the economic crisis on trade, foreign investment, and employment in Egypt[1]

1- This report was written by Arne Klau. Valuable comments were provided by Marion Jansen (ILO Geneva), Dorothea Schmidt (ILO Sub-Regional Office Cairo), Magda Shahin (American Chamber of Commerce, Cairo), and Michael Finger (WTO). Research assistance was provided by Salma Amer.

I. Foreword

Keen on continuously providing their constituents and membership with up to date and high quality services, both the International Labour Organization / Sub-Regional Office for North Africa in Cairo and the American Chamber of Commerce in Egypt agreed on jointly undertaking this study on the implications of the global financial and economic crisis on the Egyptian economy.

The study presents Egypt as an example of an emerging open economy responding to the global crisis with considerable success. In doing so, it stresses the interdependence between trade, employment and foreign investment. Blessed with sound prudential regulations and strong banking sector supervision, the Egyptian economy has shown perseverance in the wake of the financial crisis. However, the study also clearly indicates that trade, a sector severely hit, has been a major transmission channel of the crisis. In spite of the unprecedented performance of the trade sector prior to the crisis, whereby exports more than tripled between 2004 and 2008, the recession in the EU and the US has caused Egyptian exports to fall by over 25% in the first half of 2009.

Numerous challenges to the employment policy framework and Egypt's labour market were analyzed with a view to redressing the vulnerabilities in the labour market. While identifying the sectors that were most hit by the global crisis, notably tourism and the textile-industry, the study utilizes the available empirical evidence to reach some noteworthy findings and policy recommendations. In this context, the paper cites that the potential remedy for this dilemma rests on a continuous process of economic reform that integrates all segments of the society in the process of production. In addition, a labour-oriented policy that focuses on creating more job opportunities, especially in the sectors that were hit hardest in the course of the global crisis is a policy-option that is worth serious consideration. This, along with a substantial increase in competitive productivity, mainly via pivoting trade liberalization, will eventually help in eradicating the bulk of the economic discrepancies created by the crisis.

The study represents a pilot-venture for similar future collaborations. The partnership newly forged between AmCham/Egypt and the ILO/Sub-Regional Office for North Africa is indeed a valuable step to tie in the research to the practical needs and experiences of Egypt's business community as the driving force of the economy.

Yousef Qaryouti

Director
ILO – SRO Cairo

Magda Shahin

Director, TRAC
AmCham/Egypt

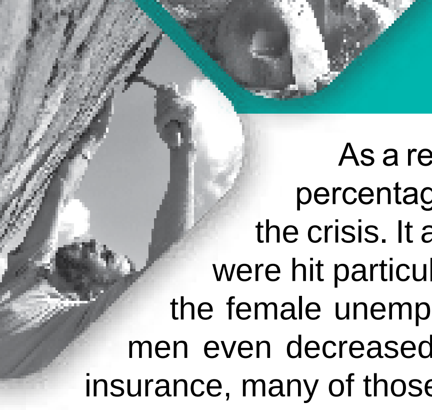
II. EXECUTIVE SUMMARY

Trade and foreign direct investment have played an increasingly important role in Egypt's economy after the economic reform process initiated in 2003 and 2004, and have been one of the main drivers of the strong growth before the crisis. Fuelled by a policy of unilateral and regional trade liberalization, foreign trade expanded rapidly - between 2004 and 2008, Egypt's merchandise exports more than tripled. At the same time, services exports also grew strongly, most notably income generated by international tourism and fees for using the Suez Canal. A relatively liberal investment environment, despite various problems in the business environment, attracted foreign direct investment.

Egypt provides an example of how exports, employment, and foreign investment in an increasingly open emerging economy responded to the global economic and financial crisis. GDP growth rates, peaking at over 7% before the crisis, fell to just over 4%. Egypt's merchandise exports were severely hit by the recession in the EU and the U.S. and experienced a drastic fall during the first months of 2009. Services exports, in particular income from tourism and fees for using the Suez Canal, fell strongly. Inflows from foreign direct investment, which before the outbreak of the crisis were a major contributor to capital formation, fell by nearly 4% of GDP. Remittances from workers abroad decreased drastically, and inflows from official development aid also fell.

Decreasing merchandise and service exports and falling inflows of foreign direct investment have been the main transmission channels of the crisis on the Egyptian economy in general and on the labour market in particular. However, the employment effects of the crisis varied strongly between sectors. The production process of certain export commodities, such as oil, is not particularly employment-intensive, thus the labour market impact of the considerable downturn of petroleum exports was limited. The mechanism is basically the same for Suez Canal revenues – while they are of considerable importance in GDP and fiscal income, the direct impact of their decrease on employment has been limited. Other sectors such as agriculture are important for overall employment, despite relatively low contribution to GDP, but have been shielded from the direct impact of the crisis due to their inward-orientation. On the other hand, more employment-intensive and outward-oriented sectors such as textiles and clothing had to lay off higher numbers of workers although the mere growth effect of the crisis was less pronounced than in other sectors. In the more skill-intensive tourism sector, which was also heavily affected by the global downturn, wage and bonus reductions and compulsory vacation were generally preferred over lay-offs. A fiscal stimulus package, equivalent to some 1.5% of GDP, adopted by the government in spring 2009 has probably prevented a stronger rise of the unemployment rate. Unfortunately, the lack of accurate and up-to-date labour market data precludes a more detailed analysis of the impact of the global crisis on employment up to this moment in time.

Egypt also provides an example where problems, inefficiencies and challenges in the labour market prior to the global crisis were aggravated during the crisis. Egypt's labour market is characterized by strong annual increases of the labour force, with the challenge to integrate some 700,000 new entrants to the labour market every year, mainly due to strong population growth. Other characteristics include the low participation of women, a high share of employment in governmental institutions and in the informal sector, low levels of productivity and wages, and a high level of unemployment, particularly among women and the young. Although a Labour Law adopted in 2003 has introduced more flexibility, it appears that there is a continuous strong disincentive for businesses to employ full-time workers, mainly due to high costs of shedding labour. In addition, important labour market mismatches remain, despite rapidly increasing educational attainments. Furthermore, weaknesses in social dialogue and social protection are a reason for the large lack in decent work opportunities in the country.



As a result of the global crisis, the official unemployment rate increased by about one percentage point, to 9.4%, which brings Egypt back to the levels of five years before the crisis. It appears that vulnerable group such as women, the low-skilled, and the young, were hit particularly hard. In the twelve months following the beginning of the crisis in Egypt, the female unemployment rate increased from 18.8% to 23.2%, while unemployment among men even decreased, from 5.4% to 5.2%. In the absence of a well-functioning unemployment insurance, many of those who lost their jobs end up in the informal sector. Moreover, the labour force increased by only 400,000 between July 2008 and July 2009 (instead of the usual 700,000), indicating that large numbers of people were discouraged from seeking employment or, where possible, opted to stay in the education system. The lack of stronger social dialogue hindered finding solutions to the crisis in tripartite agreements. Given all these developments, Egypt also provides an example where the upward trend of the “classical” indicator of unemployment reflects only to a small extent developments on the labour market during a crisis.

To a certain extent, Egypt is also an example of a country where the limitations of data available prevents a timely and detailed analysis of the impact of the export and investment downturn on the labour market, and in particular on employment by sector. This in turn makes it difficult to base crisis interventions on solid research and to be in a position to develop policy responses to the crisis. Besides pointing out to the importance of reliable and up to date economic data, the study draws some important policy conclusions: While signs of recovery become increasingly evident in Egypt’s economy, undertaking further reforms that continue improving the business and investment climate and support real cost reduction remain of key importance, measures to improve productivity, including further trade liberalization. In addition, the longstanding challenges in the labour market need to be tackled, including strategies to better integrate women and the young. Both strategies together will put Egypt in a stronger position, better prepared for crises in the future.

1. Introduction

1.1 Background and purpose of the study

The global economic and financial crisis has affected Egypt since mid-2008, which has been reflected in the sharp deterioration of most economic indicators. As many other developing countries, Egypt has been affected less by the decline in global lending and other financial transmission channels, but rather through shrinking export income and decreasing remittances. Exports have been severely hit by the downturn in the US and the European Union; after several years of double-digit growth rates, export income declined drastically during the first months of 2009. At the same time, large numbers of expatriate workers returned from abroad, in particular from the Gulf countries, leading to a strong fall in remittances.[2] Thus, Egypt's labour market, which even before the outbreak of the crisis was already in a difficult state, has been facing the prospect to accommodate these mostly low-skilled workers, in addition to increasing local pressure caused by the crisis. As a result, the current slowdown particularly affects the poor and bears the risk to exacerbate social discontent.

Egypt provides an example how exports, employment, and foreign investment in an increasingly open emerging economy respond to the global crisis. This study will start with a brief overview of Egypt's economic situation prior to the crisis. Due credit will be given to various strong points of the economy resulting from the reform process that started in the mid-nineties. In this context, the study will also have a critical look at the availability and quality of economic data in Egypt. This will be followed by a full-fledged analysis of the impact of the crisis on the economy, with particular attention given to trade, employment and foreign direct investment. A sectoral approach will identify those sectors of the economy that were hit hardest. The government's response to the crisis, especially the fiscal stimulus package, will be analyzed. Based on various lessons learned from the crisis, the paper concludes with some suggestions and policy recommendations.

1.2 The data challenge in Egypt

"In the real economy, the effects of the global crisis have not been captured yet, because of lag of availability of data." (Egyptian Economic Monitor, June 2009)

Timely and reliable data to judge the impact of the global crisis on Egypt's economy in general and its labour market in particular is scant. The main national source of employment, labour market and industrial data is the Central Agency for Public Mobilization and Statistics (CAPMAS), which is the only institution that provides comprehensive data on every aspect of the economy.[3] Unfortunately, as at December 2009 many economic data on CAPMAS' website is available only until 2004.

Information on the labour market is available through CAPMAS' quarterly Labour Force Sample Survey (LFSS), which aims at providing up-to-date information, and the Population and Establishment Census, published every ten years (most recently in 2006). Furthermore, CAPMAS issues an annual publication on Wage, Employment, and Working Hours. Unfortunately, only a limited part of the data that is produced by the LFSS is actually publicly available. Data that is produced, but not published include employment by status, employment by economic sector, youth and long-term unemployment.[4] Thus, beyond information contained in the publicly available parts of the LFSS statistics evidence on employment impacts of the crisis is scattered and anecdotal.

2 - According to preliminary balance of payments statistics, net private transfers decreased from US$ 8.4 billion in 2007/08 to US$ 7.6 billion in 2008/09.

3 - Unless indicated otherwise, data in this study are from CAPMAS.

4 - CAPMAS online information available at: http://www.msrintranet.capmas.gov.eg/ows-img2/indecator/wrk_mslg.xls (10 December 2009).

Merchandise trade data is compiled by the General Organization for Export and Import Control (GOIEC). The Ministry of Petroleum keeps statistics on investment in the oil and gas sector, while the General Authority for Investment (GAFI) keeps statistics on all other investments. The Central Bank records figures on quarterly and annual investment flows based on financial records.

Discrepancies between CAPMAS data and data from other national or international institutions are substantial in places.[5] Discrepancies are particularly striking in the case of employment and trade data: For example, CAPMAS indicates that in 2006 total employment in the textiles and clothing sector was 278,267, while data from the Industrial Development Authority indicate that employment stood at 400,384, which is 44% higher than reported by CAPMAS. Discrepancies in trade data are even more striking; for example, textile and clothing exports in 2007 amounted to US$ 652 million according to CAPMAS, but to US$ 2,344 million according to GOEIC. The comparison of Egyptian exports with mirror data of its trading partners also reveals strong discrepancies. Raw cotton exports in 2008 stood at US$ 192 million according to CAPMAS, whereas trading partners report raw cotton imports from Egypt amounting to US$ 401 million for the same year. Discrepancies on labour force estimations are also substantial, with implications for the resulting unemployment rate: While the Ministry of Planning puts the labour force at 20.2 million for 2003, the World Bank estimated its size at 26.7 million.[6]

Furthermore, interpretation of production and trade data is often made difficult by classification departing from international practice, i.e. the Harmonized System (HS) for trade data and the International Standard Industrial Classification (ISIC) for production data. In many cases, no concordance tables to match the systems are provided in case of such departures. In addition, it is difficult to evaluate the quality of production data because no information is available on the percentage of firms that refused to take part in the relevant surveys.

Figures on foreign direct investment (FDI) in Egypt vary according to the source and the definitions employed. There are wide disparities between the three sources (Central Bank, GAFI, Ministry of Petroleum), and none can be considered definitive in assessing overall FDI levels.

Finally, data coverage of certain aspects of economic importance such as Egyptians working abroad is very limited and based on rough estimates. While figures are published on permits issued to Egyptians wishing to work abroad (currently some 1.1 million), no data is available on the number of Egyptians actually using these permits or being laid off in their host countries and returning to Egypt.

5 - El Haddad (2009), p.92.
6 - El Essawy (2007).

2. The crisis and its prehistory

2.1. The years before the crisis: economic reforms and growth

Between 2005 and 2008, Egypt's economy saw the culmination of more than 15 years of market-oriented reform efforts, with growth rate peaking at nearly 7.2% in financial year 2007/08 (Table 1).[7] The economic reforms, which involved privatization, trade liberalization and reduction of red tape, date back to the middle of the 1990s, with the adoption of the Economic Reform and Structural Adjustment Program (ERSAP). The reforms were interrupted at the end of the 1990s, but resumed strongly in 2003 and 2004. While the overarching goal of the reforms was to achieve high levels of equitable growth, they also succeeded in diversifying the growth drivers, away from the traditional, naturally endowed sectors such as oil and Suez Canal, to more sustainable sources such as manufacturing and telecommunications.

Table 1
Main economic indicators, 2003-09

	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09		
						Q1	Q2	Q3
Real sector, annual % change								
Real GDP	4.1	4.5	6.8	7.1	7.2	5.8	4.1	4.3
Nominal GDP	16.2	11.0	14.7	20.6	20.4	25.7	14.0	13.6
% of GDP								
Consumption	84.4	84.3	83.7	83.7	83.8	90.4	89.0	82.3
Investment	16.9	18.0	18.7	20.9	22.3	15.8	21.4	22.4
Exports	28.2	30.3	31.3	30.2	32.8	29.0	24.2	22.3
Imports	29.6	32.6	33.7	34.8	38.8	39.0	34.6	27.4
Prices								
Inflation rate (CPI, %)	10.3	11.4	4.2	11.0	11.7	22.4	19.6	13.3
Exchange rate (LE/US$)	6.16	6.01	5.75	5.71	5.50	5.35	5.52	5.57
Discount rate (%)	8.4	10.1	8.8	8.7	7.0	6.9	7.4	7.1
External sector (% of GDP)								
Current account balance[a]	4.3	3.2	1.6	1.7	0.5	-0.5	-0.8	-0.5
FDI[a]	0.5	4.4	5.7	8.5	8.1	0.9	1.3	0.8

a Quarterly figures for 2008/09 in percent of full year estimated GDP.

Source: Ministry of Finance

The role of investment, both domestic and foreign, as a main driver of growth has been a distinctive characteristic of Egypt's recent growth performance. The share of investment in GDP increased from 16.9% in 2003/04 to 22.3% in 2007/08. Foreign direct investment peaked to a record of US$17.8 billion in 2007/08 (equivalent to 8.1% of GDP), up from US$ 407 million or 0.5% of GDP in 2003/04, with the bulk of funds going to non-oil green field investments, thereby driving investment ratios up from 16.9% of GDP in 2003/04 to 22.3% in 2007/08. Accordingly, Egypt was ranked as the first country in Africa and the second in the MENA region (after Saudi Arabia) in terms of attracting FDI.[8] However, despite the strong and increasing importance of investment between 2003 and 2008, various aspects in Egypt's investment and business environment continue to attract criticism and remain a source of concern (Box 1).

7 - In Egypt, the fiscal year runs from 1 July to 30 June.
8 - UNCTAD (2008).

Box 1: Investment policy framework and business environment

Three main laws govern investment in Egypt: the Companies Law (159/1981), the Investment Guarantees and Incentives Law (8/1997), and the Special Economic Zones Law (83/2002). In financial year 2008/09, a total of 6,291 new companies were established, of which 3,274 under the Companies Law, 2,957 under the Investment Law, and 60 under the Special Economic Zones Law. There is no specific law on foreign investment. Foreign investors may choose to invest either under the Companies Law or the Investment Guarantees and Incentives Law, depending on the types of incentive sought and the areas in which the investment is to be made. There are no restrictions on repatriation of funds by companies, or rules requiring foreign companies to hold foreign currency accounts. Investment, whether foreign or domestic, is managed by the General Authority for Investment and Free Zones (GAFI), established in 1997. GAFI's role has gradually shifted from an investment-regulating to an investment-promoting and facilitating institution. GAFI has been operating a one-stop office for investors since January 2005.

Paradoxically, in contrast to growing investment rates and increasing FDI, various competitiveness indicators describing Egypt's business environment have been low and sometimes even been declining. Egypt's overall ranking in the most recent World Bank's Cost of Doing Business Report, for example, is 106 out of 183 economies; on a number of sub-indicators Egypt's performance is far below other MENA countries. A number of problems in the business environment are directly related to inefficiencies in the labour market (section 4.1.).

Egypt's ranking in *Doing Business 2010*

Indicator	Indicator
Ease of doing business	106
Starting a business	24
Dealing with construction permits	156
Employing workers	120
Registering property	87
Getting credit	71
Protecting investors	73
Paying taxes	140
Trading across borders	29
Enforcing contracts	148
Closing a business	132

Source: World Bank (2009b).

Inflation rates, measured by the CPI, were between 10% and 12% in most years, with the exception of 2005/06 when inflation was 4.2%. Interest rates showed a declining trend, falling from 10.1% in 2004/05 to 6.2% in summer 2008. At the same time, the fiscal deficit was reduced from 9.6% of GDP in 2004/05 to 6.8% of GDP in 2007/08. However, during the course of the reforms, emerging turbulences such as the hike in global food and energy prices, followed by the current crisis increasingly posed a challenge to economic policy.

Despite several years of growth, poverty rates have remained high in Egypt. According to the most recent comprehensive study on poverty in Egypt, 19.6% of Egyptians were "poor" and an additional 21.0% were "near-poor" in 2005.[9] The decline of poverty rates between 2000 and 2005 is mainly attributed to employment growth. As many people are concentrated around the poverty line, increased employment opportunities, even if implying just a small income boost, can lift large shares of the population out of poverty. By the same token, large numbers of job losses have a strong negative impact on poverty rates.

9 - World Bank (2007). A recent UNDP report estimates a poverty rate of 16.6% for Egypt (UNDP (2009)).

As a “crisis before the crisis”, Egypt, one of the world largest food importers, was heavily affected by the global hike in food prices. Between January 2006 and January 2008, the price of imported food items increased by some 60%, while the price of domestic food products grew by about 25%. The impact of the price shock was most pronounced on the middle and lower income groups as these spend larger shares of their income on food items, reaching nearly 60% for the lowest income quintile. Three main staples (oil, wheat, sugar) account for some 20% of their total expenditure. As this brought economic policy under hard pressures, the Egyptian Parliament endorsed a package in May 2008 (Law 114/2008) with the objective of cushioning the impact of the crisis on the lower income groups while maintaining fiscal sustainability (Table 2).

Table 2
Policy measures taken in response to the global price increases, 2007-09
(LE million)

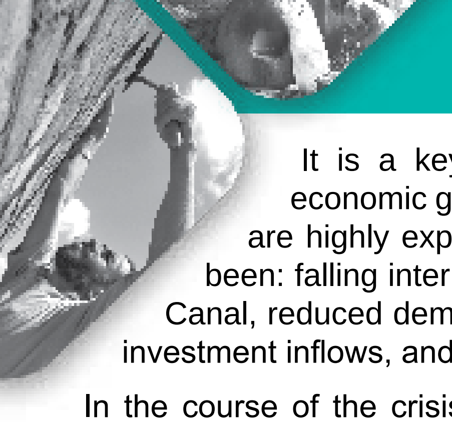
Expenditure	**2007/08**	**2008/09**	**Financing**	**2007/08**	**2008/09**
Increasing monthly take home salary of public civil servants by 30% of base wage	1.1	6.2	Reducing energy subsidies and increasing sales tax on petroleum products	1.3	7.5
Increasing rewards for local government employees	0.4	3.0	Increasing sales tax on cigarettes	0.2	1.3
Disbursing additional quantities of rice, edible oil, and sugar on rationed cards	0.2	1.6	Increasing vehicle licensing and registration fees	0.2	1.1
Increasing monthly pensions by 20% with maximum LE 100	0.6	3.6	Increasing fees on quarries	0.2	1.0
Increasing energy subsidies	4.0		Abolishing tax exemptions for energy intensive industries in Free Zones	0.1	0.6
			Abolishing tax-exemptions on T-bills interest income	0.1	1.0
			Abolishing tax exemptions on profits of educational institutions	0.0	0.9
			Abolishing forward carry-over of losses	0.0	1.0
			Higher tax receipts and dividends from Egyptian General Petroleum Corporation	2.7	0.0
			Other	1.5	0.0
Total	**6.3**	**14.4**	**Total**	**6.3**	**14.4**

Source: Ministry of Finance (2009).

It is evident that most of the measures taken were heavily biased in favour of Egypt’s 5.8 million government officials, while the lower income groups not employed in the public sector only benefited from the package through the reshuffling of energy subsidies and the disbursement of additional quantities of food through rationed cards.

2.2. The crisis in Egypt

Thanks to sound prudential regulations and strong banking sector supervision, the Egyptian economy was immune to the first round effects of the rapid collapse of global financial markets. Nevertheless, signs of weaker economic performance became evident in the third quarter of 2008, when the year-to-year growth rate dropped to 5.8%. The sudden and strong decline of the investment share in GDP from 22.3% in 2007/08 to 15.8% in the first quarter of 2008/09 is particularly noteworthy (Table 1), occurring at the same time when exports started to decrease. The strong increase of domestic consumption, fuelled by the strong growth of the previous years, prevented a stronger fall of the growth rate. In the last quarter of 2009, GDP growth decreased further to 4.2%, the lowest quarterly growth rate in more than five years.



It is a key feature of Egypt's economy that Egyptian and developed countries' economic growth are highly correlated as various key sectors of the Egyptian economy are highly exposed to global economic activity.[10] The main transmission channels have been: falling international prices for oil and natural gas, decreasing transit through the Suez Canal, reduced demand for manufactured exports and tourism services, a decrease of foreign investment inflows, and lower workers' remittances.

In the course of the crisis, Egypt's current account situation deteriorated significantly, with nearly all income categories featuring declines (Table 3, for a more detailed description of trade flows see section 3.2.). The most drastic declines were experienced by petroleum exports, which dropped by over 50%, mostly due to falling international oil prices. Non-petroleum exports (-18.9%) and tourism income decreased less (-3.1%). Remittances of Egyptians working abroad decreased by nearly 9%. The bulk of remittances in 2008/09 came from the U.S. (US$2,269 million), followed by Kuwait (US$1,594 million), the United Arab Emirates (US$1,380 million) and Saudi Arabia (US$976 million).[11] Official transfers, mostly development aid money, also decreased considerably, from over US$ 960 million to some US$ 614 million.

Table 3
Current account, 2007/08-08/09
(US$ million)

	2007/08	2008/09	Change (%)
Current account	**888.3**	**-4,424.3**	**-598**
Goods and services balance	-8,449.3	-12,670.9	-50.0
Merchandise trade balance	-23,415.4	-25,173.3	-7.5
Exports	29,355.8	25,168.9	-14.3
Imports	-52,771.2	-50,342.2	4.6
Services balance	14,966.1	12,502.4	-16.46
Receipts	27,211.0	23,801.3	-12.5
Transportation	7,559.7	7,481.0	-1.0
of which Suez Canal	5,155.2	4,720.6	-8.4
Travel	10,826.5	10,487.6	-3.1
Investment income	3,289.4	1,936.7	-41.1
Government receipts	188.3	252.8	34.3
Payments	12,244.9	11,298.9	-7.7
Transportation	1,,620.1	1,491.9	-7.8
Travel	2,895.3	2,739.3	-5.4
Investment income	1,929.7	1,774.8	-8.0
Government expenditure	1,313.8	1,182.3	-10.0
Other	4,486.0	4,110.6	-8.4
Transfers	9,337.6	8,246.6	-11.7
Net private transfers	8,377.1	7,632.3	-8.9
Net official transfers	960.5	614.3	-36.0

Source: Central Bank of Egypt

After several years of growth, inflows of foreign direct investment into the Egyptian economy experienced a remarkable decrease during 2008/09, dropping by nearly US$ 5 billion (Table 4). The major share of the decrease in FDI inflows has been due to falling investment from the U.S. and European countries, whereas inflows from other source countries even increased in absolute terms, to over US$ 3.7 billion. Regrettably, a sectoral analysis of FDI inflows is precluded by the lack of data. Anecdotal evidence points to the particular importance of FDI in the petroleum sector, clothing and textiles, and tourism.

10 - World Bank (2009).
11- Central Bank of Egypt online information: http://www.cbe.org.eg/Public/All%20Monthly%20Statistical%20Bulletin%20PDF/Monthly%20Statistical%20Bulletin%20Nov%20.2009/48%2032%20-%20Workers%20Remittances%20by %20country.pdf (10 December 2009).

Table 4
Foreign direct investments flows, 2004-09
(US$ million)

	2004/05	2005/06	2006/07	2007/08	2008/09
Total net foreign direct investment	**3,902**	**6,111**	**11,053**	**13,237**	**8,113**
Inflows	**4,135**	**9,098**	**13,084**	**17,802**	**12,836**
United States	2,040	4,554	4,681	6,448	3,515
Europe	695	2,852	2,439	5,105	3,904
Arab countries	189	300	3,298	2,733	1,701
Other countries	1,209	1,392	2,666	3,516	3,716
Outflows	**-233**	**-2,987**	**-2,031**	**-4,566**	**-4,723**

Source: CAPMAS

2.3. The government's reaction to the crisis

In spring 2009, the government introduced a fiscal stimulus package of some LE15.5 million (1.5% of GDP), mostly to finance accelerated investments in public utilities (Table 6). Though the additional outlays were formally ratified by Parliament in March 2009, several projects under the package were already initiated in September 2008, financed through budgeted contingencies. The package was adopted with a view to serving a dual purpose: first, to stimulate domestic demand and preclude a sharp decline in economic activity, secondly to accelerate the execution of crucial infrastructure projects with high social value such as drinking water, sewage and roads. A second stimulus package was under consideration as at November 2009.[12]

The authorities indicated that, although additional spending for the stimulus package was not included in the original 2008/09 budget, the overall budget deficit was not expected to deviate significantly from the target of 6.9% of GDP, due to expected savings in some expenditure items and (notably wages) and improved revenue terms, including higher than budgeted tax receipts.[13]

Table 5
Breakdown of the fiscal stimulus package, 2008/09
(LE million)

	2008/09
Overall package	**15,532**
I. Investment expenditure	**10,832**
1. General budget	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 centres	400
Building schools	150
Other	652
2. Economic authorities	600
Improving the efficiency of railways	400
Executing infrastructure projects for the development of East Port-Said sea port	50
Improving the capacity of Red Sea ports	150
II. Current expenditure (transfers/subsidies)	**2,700**
Increasing competitiveness of Egyptian exports	2,100
Supporting industrial zones in the Delta	400
Supporting logistic areas for internal trade	200
III. Reductions in customs duties and sales tax	**2,000**
Reducing custom duties on some industrial inputs and capital goods	1,500
Temporary lift of sales tax on capital goods	500

Source: Ministry of Finance.

12 - Ministry of Finance, Press Release, 13 November 2009.
13 - Ministry of Finance (2009a).

As part of the fiscal stimulus package, several targeted measures have been adopted to cushion the effect of the crisis on sectors that have been identified as particularly exposed, mainly the textile and clothing (TC) sector and tourism (Table 6).

Table 6
Targeted policy measures of the stimulus package

Trade
Reducing tariffs on specific capital goods and production components that have no local substitutes
Increasing finance for export programs by 50%
Reducing participation fees for specialized international fairs and exhibitions by 50%, doubling the number of participating companies
Tourism
Rescheduling of outstanding debt and providing various loan facilities to projects in the tourism sector
Intensifying joint marketing campaigns with international travel agencies
Concentrating marketing efforts towards emerging economies with high potential
Supporting charter flights programs
Enhancing efforts aimed at introducing low-cost carriers to the Egyptian market
Manufacturing
Waving sales tax on machinery, equipment and capital goods for one year, starting January 2009
Postponing the payment of 75% of industrial land instalments due to the government for one year
Fixing natural gas and energy prices for all operating plants till the end of 2009, and rescheduling of energy connection fees over three years
Enhancing services provided by the Industrial Training Council, the Industrial Technology Centers and the Industrial Modernization Center by reducing contributions by benefiting companies to 50%, so as to better serve 11,500 companies staffed with around one million insured workers
Increasing subsidies to services provided by technological centres to various industries
Decentralizing the process of issuing industrial and operating licenses to the boards of the Industrial Zones at governorate level, and streamlining the required procedures for the renewal of industrial registration
Providing the required approvals for all new non-energy-intensive industrial projects in one day

Source: Ministry of Finance (2009a).

In addition, the Central Bank of Egypt provided monetary stimulus measures by reducing the overnight deposit and lending rates five times between February and July 2009, bringing them down to 8.5% and 10% respectively. Furthermore, with a view to facilitating the access to finance for SMEs, it eased reserve requirements by counting loans to SMEs as reserve requirement holdings of commercial banks.

The adequacy of the stimulus package can be discussed in terms of (i) its impact on GDP and employment, and (ii) its sustainability. The package, at an estimated 1.5% of GDP, has been prudent and limited in size, and, through the increase of domestic demand, may have prevented a further decline in GDP growth rates and sustained employment levels in the short run.[14] With regard to the sustainability of the stimulus package, it should be noted that the scale of the package has taken into account Egypt relatively high public debt ratio of around 60% of GDP, and that it included projects that were already ongoing. While the package has stopped the recent fall of the debt-to-GDP-ratio, from about 80% in 2005, its most likely event is a rise in the debt ratio of some 1% of GDP by 2010.

14 - Assessing the short-term employment impact of the stimulus package, Abdelfattah Moursi and El Mossalamy (2009) find that the package created "between 661.420 and 729.650 new job vacancies".

3. Trade patterns

3.1. The trade policy framework

Egypt's exports benefits from preferential market access to various other countries with which it has concluded free-trade agreements, and to the United States under the QIZ protocol. Egypt is a WTO member, and as such, its TC exports are maximally levied the respective MFN or GSP duties in all other countries. Egypt has concluded free-trade agreements with the European Union (2004), the members of EFTA (2004), Turkey, and other Arab countries. It is also party to the Greater Arab Free Trade Area (GAFTA), and member of the Common Market of Eastern and Southern Africa (COMESA). Tariffs are the Government's main trade policy instrument in the TC sector, although safeguard and anti-dumping measures have been introduced occasionally.

The QIZ Protocol, signed by the Egyptian Government in December 2005 as a countermove to the phase-out of the Multi-Fibre Agreement, is a tripartite agreement between the United States, Egypt, and Israel. Qualified Industrial Zones (QIZ) are designated geographic areas within Egypt that offer specific advantages for exporters. Companies located in the QIZ benefit from tariff-free market access to the United States under certain conditions.[15] In particular, exporters must ensure that 35% of the product's value be manufactured in an Egyptian QIZ, and that 10.5% of the total value must consist of Israeli inputs. As at May 2009, 740 companies had been approved under this scheme, of which 591 were from the TC sector. The majority of the companies are located in the greater Cairo area and in Alexandria.

Imports from countries with which Egypt does not have a free-trade agreement (e.g. United States, China, Japan, Korea) are subject to the most favoured nation (MFN) tariff. The present MFN tariff, which implied strong tariff reductions, was implemented in September 2004 through Presidential Decree 300/2004 and has only undergone marginal changes since then.[16] However, at an average of 20%, Egypt's applied MFN tariff is high by international comparison (Table 7). It comprises twelve rates: 0%, 2%, 5%, 12%, 22%, 32%, 40%, 135%, 600%, 1,200%, 1,800%, and 3,000%; in addition, 11 lines are subject to ad valorem tariffs. Nearly 99% of Egypt's tariff lines are bound at the WTO. MFN tariffs on non-agricultural products (WTO definition) are generally lower, with an average of 12.8%; tariffs on agricultural goods remain high, with an average of 66.4%. The higher average on agricultural goods is strongly determined by average tariffs of over 1,000% on beverages and spirits.

In addition to high average tariffs, it has been observed that Egypt's tariff system is complex, with many exemptions, reductions, and concessions.[17] Exemptions are in place, inter alia, for imports for the establishment of free zones, a drawback scheme, and primary materials for processing. Tariff concessions are in place for imports under the Investment Scheme for Arab and Foreign Funds, of inputs into free zones, by limited-liability and joint-stock companies formed under the Companies Law (Law 159/1981), of assembly industries, and of alcoholic beverages by hotels and tourism establishments. The numerous individual schemes and their wide scope, coupled with the possibility of discretionary decisions, clearly undermine the transparency of its tariff regime. In addition to the complex tariff structure, importers have raised concerns about the efficiency of Egypt's customs and other border agencies.[18]

15 - Otherwise, the US' MFN tariffs on TC products range between 16% and 36%

16 - Additional changes to the tariff structure were introduced by Presidential Decrees 39/2007 (simplification of the tariff structure and adoption of HS 2007 classification), 103/2008 (tariff reductions on cement and various food and intermediate products), and 51/2009 (tariff reductions on raw materials, intermediate and capital goods as part of the fiscal stimulus package).

17 - WTO (2005).

18 - World Economic Forum (2009).

Table 7
Summary analysis of the MFN tariff, 2009

	No. of lines[a]	Applied 2009 rates				
		No. of lines used	Simple avg. tariff (%)	Tariff range (%)	Std-dev (%)	CV
Total	5,687	5,676	20.0	0-3,000	148.3	7.4
By WTO definition[c]						
Agriculture	769	758	66.4	0-3,000	386.6	5.8
Live animals and products thereof	97	97	18.4	5-32	13.0	0.7
Dairy products	36	36	11.5	2-32	9.1	0.8
Coffee and tea, cocoa, sugar, etc.	146	146	35.4	2-3,000	247.3	7.0
Cut flowers and plants	34	34	4.0	2-32	7.1	1.8
Fruit and vegetables	158	158	15.9	2-40	12.8	0.8
Grains	16	16	3.3	2-5	1.5	0.5
Oil seeds, fats, oils and their products	99	99	6.4	0-32	5.8	0.9
Beverages and spirits	38	38	1,028.8	12-3,000	1,346.4	1.3
Tobacco	12	1	22.0	22	0.0	0.0
Other agricultural products	133	133	4.1	0-32	4.5	1.1
Non-agriculture (excl. petroleum)	4,911	4,911	12.8	0-3,000	44.5	3.5
Fish and fishery products	116	116	8.5	2-32	9.0	1.1
Mineral products, precious stones and precious metals	346	346	9.7	0-40	9.0	0.9
Metals	639	639	9.8	0-40	8.8	0.9
Chemicals and photographic supplies	920	920	9.5	0-3,000	99.1	10.5
Leather, rubber, footwear and travel goods	182	182	13.9	0-32	11.4	0.8
Wood, pulp, paper and furniture	262	262	13.5	0-40	10.9	0.8
Textiles and clothing	887	887	24.4	0-40	12.1	0.5
Transport equipment	165	165	16.3	0-135	25.9	1.6
Non-electric machinery	591	591	6.2	0-40	8.5	1.4
Electric machinery	314	314	9.2	0-40	12.3	1.3
Non-agricultural articles n.e.s.	489	489	14.0	0-40	12.8	0.9
By ISIC sector						
Agriculture, hunting, forestry and fishing	297	294	5.8	0-40	6.9	1.2
Mining and quarrying	103	103	3.0	0-22	3.2	1.1
Manufacturing	5,286	5,278	21.1	0-3,000	153.7	7.3
By stage of processing						
Raw materials	640	637	4.8	0-40	6.2	1.3
Semi-processed products	1,801	1,801	10.6	0-3,000	70.9	6.7
Fully processed products	3,246	3,238	28.2	0-3,000	188.6	6.7

a Total number of lines is listed. Tariff rates are based on a lower frequency (number of lines) since 11 tariff lines are specific duties and no *ad valorem* equivalent were estimated.

Note: CV = coefficient of variation.

Source: WTO (2005), own calculations.

The network of new trade agreements, coupled with the unilateral tariff reductions of 2005, has significantly liberalized Egypt's trade policy. This has allowed Egyptian exporters better access to significant export markets such as the EU, the EFTA countries and the United States, while at the same time it opened Egypt's economy for cheaper imports of inputs and intermediate goods, thereby increasing the competitiveness of its exporting companies. Trade liberalization has been one of the cornerstones of the 2004 reforms and is likely to be one of the drivers of Egypt's trade expansion and GDP growth in the following years.

3.2. The evolution of trade flows

Before the crisis

As a result of the economic reforms initiated in the mid-1990s and resumed in 2004, foreign trade has played an increasingly important role in Egypt's economy. Fuelled by Egypt's policy of unilateral and regional trade liberalization, foreign trade grew at unprecedented rates - between 2004 and 2008, merchandise exports more than tripled and merchandise imports more than quadrupled (Table 8) At 96% for imports and 62% for exports, growth rates were particularly impressive in 2008, the pre-crisis year. Egypt's openness ratio increased impressively, from 23.2% in 2004 to 48.6% in 2008.

Table 8
Egyptian exports and imports, 2004-08
(US$ million)

	2004	2005	2006	2007	2008
Exports	7,676	10,652	13,720	16,181	26,204
Imports	12,833	19,815	20,614	27,063	52,916
Trade balance	-5,157	-9,163	-6,894	-10,882	-26,712
Openness ratio (%)	23.2	31.1	30.6	31.9	48.6

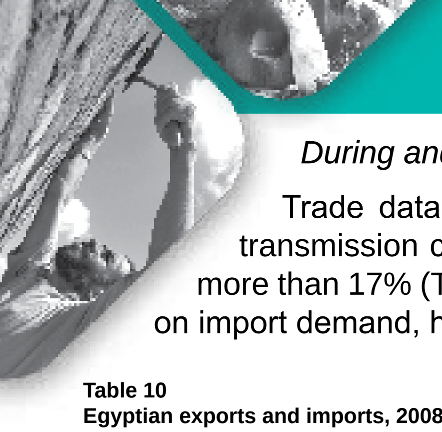
Source: CAPMAS.

While growth rates for exports were indeed impressive, Egypt also managed to diversify its exports, away from the classical goods such as petroleum and cotton, to new growth drivers. Table 9 shows the reaction of individual commodity exports before the crisis. Between 2004 and 2008, all major commodity groups experienced strong growth rates. The exportation of petroleum products nearly tripled, while exports of non-petroleum goods more than quadrupled. The 2008 growth of finished goods exports, from US$ 3 billion to nearly US$11.8 billion is particularly impressive. It was in particular this growth in non-oil exports that contributed to growth and employment. On the other hand, cotton, once among Egypt's best-known export products and the traditional basis for the local textile industry, has lost in absolute and relative importance.

Table 9
Exports by commodity group, 2004-08
(US$ million)

	2004	2005	2006	2007	2008
Total exports	**7,676**	**10,652**	**13,720**	**16,181**	**26,204**
Petroleum exports	**3,094**	**5,226**	**7,403**	**7,946**	**8,992**
Crude oil	403	515	884	1,054	2,200
Other	2,692	4,711	6,519	6,892	6,792
Non-petroleum exports	**4,127**	**4,237**	**4,713**	**5,591**	**17,211**
Raw cotton	482	179	132	153	192
Raw materials	494	525	534	742	2,016
Semi-finished goods	1,061	1,254	1,415	1,688	3,216
Finished goods	2,090	2,278	2,631	3,008	11,788

Source: CAPMAS.



During and after the crisis

Trade data for the first five months of 2009 indicates that trade has been a major transmission channel of the crisis: Exports fell by over 25%, while imports decreased by more than 17% (Table 10). A positive side effect of the downturn was that it also put a damper on import demand, helping to bring down the trade deficit.

Table 10
Egyptian exports and imports, 2008-09
(US$ million)

	2008[a]	2009[a]
Exports	11,831	8,849
Imports	20,928	17,292
Trade balance	**-9,097**	**-8,443**

January-May. *Source:* CAPMAS.

However, not all export destinations and commodities were affected in the same way. The impact of the global crisis on Egypt's economy becomes particularly evident when comparing export figures for individual commodity groups for the first five months of 2009 and 2008. Except for raw materials, all product groups experienced a strong decline in exports. Among non-petroleum products, the decrease was particularly strong for finished goods (-26.6%), which include employment-intensive textile and clothing products (Table 11). Unfortunately, only yearly data on trade by trading partner is publicly available (Table 12), which before the publication of 2009 data precludes an analysis of the impact of the crisis on trade flows by trading partner.

Table 11
Exports by commodity group, 2008-09
(US$ million)

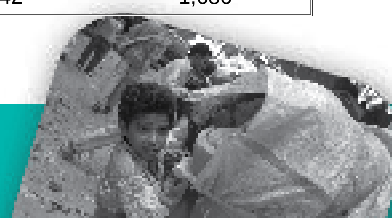
	2008[a]	2009[a]	Change 2009/2008 (%)
Total exports	**11,831**	**8,849**	**-25.2**
Petroleum exports	3,942	2,369	-40.9
Crude oil	927	460	-50.4
Other	3,015	1,909	-36.7
Non-petroleum exports	7,890	6,480	-17.9
Raw cotton	151	16	-89.4
Raw materials	1,010	1,226	21.4
Semi-finished goods	1,442	1,358	-5.8
Finished goods	5,287	3,881	-26.6

January-May. *Source:* CAPMAS.

Table 12
Exports by geographical region, 2004-09
(US$ million)

	2004	2005	2006	2007	2008
Total exports	**7,676**	**10,652**	**13,720**	**16,181**	**26,204**
EU(25)	2,700	3,589	4,603	4,703	9,262
Asia without Arab countries	1,112	1,350	2,185	3,252	4,643
Arab countries	1,395	2,009	2,212	2,479	6,684
North America	639	989	1,225	1,135	1,597
Africa without Arab countries	159	212	144	253	985
Europe other than EU(25)	325	474	465	581	1,066
South America	35	30	51	37	281
Other	1,310	2,000	2,834	3,742	1,686

Source: CAPMAS




4. Employment trends

4.1. The employment policy framework

The Labour Law of 2003 governs the relations between employers and employees in the formal private sector; it represents the main legal instrument with regard to employment and labour market policies in Egypt.[19] In contrast to earlier labour legislation, it accords employers more flexibility, especially in relation to the termination of contracts for reasons of force majeure or negative economic circumstances (such as the current crisis). Employees whose employment contracts are terminated for economic reasons are entitled to a sum equal to one month of the employee's total salary for each of the first five years of service, and one and a half month for each year of service over and above the first five years. The Law also allows for greater flexibility in working hours and permits fixed-duration contracts as well as employment on probation for up to three months. It also introduced the right to strike peacefully, through labour unions, in defence of the employees' professional, economic or social interests. The impact of this Law on job creation has not yet been evaluated.

Although the new Labour Law has facilitated the firing process, it appears that firing costs remain high, at an average 132 weeks of wages.[20] Thus, it has been argued that there is a continuous strong disincentive for businesses to employ full-time workers.[21] In a recent global ranking that measured labour market efficiency, Egypt ranked 134 of 134 countries.[22]

The Government, through the National Council of Wages, sets minimum wages.[23] As at October 2009, the monthly minimum wage was LE 203 in the public sector, while no minimum wage for the private sector is currently in place. In this context, it has been noted that in Egypt minimum wages and social insurance requirements have been frequently ignored by private firms in practice.[24]

With a view to increasing unemployment levels, the government has also put in place various active labour market policy measures, such as public works programmes, support to small and medium-sized enterprises, the establishment of a labour market information system, and incentives for vocational training.[25]

Workers' representatives have called for the establishment of a publicly financed fund to combat unemployment.[26] However, such a fund would face the problem of severe information asymmetries in identifying those who were actually affected by the crisis. As at October 2009, such a fund is not being considered by the Government.

4.2. Egypt's labour market and its evolution during the crisis

Data on Egypt's labour market is available through (1) a comprehensive census carried out every ten years by CAPMAS, and (2) a quarterly labour force sample survey covering some 20,000 households. The most recent census was undertaken in 2006; its results were published by CAPMAS in 2008. Key data on Egypt's labour market are represented in Table 13.

19 - As at December 2009, the Law has not been published on the website of the Ministry of Manpower and Migration. In addition, 46 Decrees have been issued under Law in 2003.
20 - World Bank (2009b).
21 - Egyptian National Competitiveness Council (2009).
22 - Egyptian National Competitiveness Council (2009). In the study, the indicator „labour market efficiency" is composed of ten sub-indicators grouped under the two components of labour market flexibility and use of talent.
23 - The Council, which is composed of representatives of Government, business associations, and unions, was established in October 2003. Its main objective is to determine minimum wages at the national level in light of the cost of living. Minimum wages are reviewed every three years.
24 - El-Megharbel (2007), ILO (2009).
25 - Ministry of Manpower and Migration; International Labour Organization (2009).
26 - Center for Trade Union and Workers Services (2009).

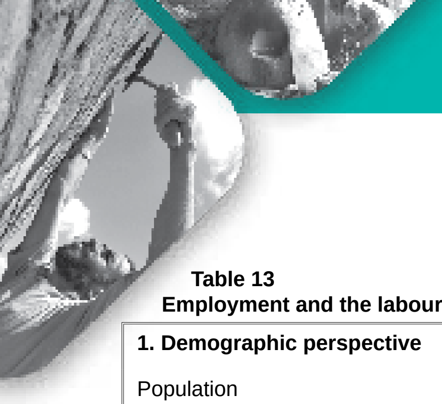


Table 13
Employment and the labour market in Egypt

1. Demographic perspective	
Population	77 million
Annual average population growth (1996-06)	2%
Share of working age population (15–64 years)	64.5% (1995:57%)
2. Labour force	
Labour force	22 million
Annual average growth of labour force (1996-06)	2.7%
Labour force participation rate (2005)	31%
3. Employment and unemployment	
Employment (15-64 years)	19.9 million (of which some 21% informal employment)
Sectoral employment distribution	Agriculture 26.0%; manufacturing 11.8%; construction 9.4%; retail 12.6%; other services 40.2%
Distribution of employment by type of ownership	Private sector 72.5%; 27.2% Government and public sector
Unemployment rate	9.72%
Unemployment rate by gender	7.6% for males; 19.2% for females
Share of young (15-29 years) among unemployed	92%
Vulnerable employment rate in total employment	24.8% (20.4% and 43.5% for women)
Working poverty share in total employment (2 US Dollar a day)	26.3%

a Unless otherwise mentioned, data refer to 2006, the date of the latest census.

Source: CAPMAS (2008), *Census data*.; ILO Key Indicators of the Labour Market

Before the crisis

Even before the outbreak of the crisis, Egypt's labour market was facing a number of challenges that had been rather persistent over time.

1) A rapidly increasing labour force:

Egypt's labour market is characterized by strong annual increases of the labour force, with the challenge to integrate some 700,000 new entrants every year, mainly due to strong population growth. While a growing labour force is not a threat to labour markets *per se*, as it also indicates an increase in potential growth, in the case of Egypt lacking integration of this potential excluded a large number of people from the participation in economic activities.

2) Low participation of women:

Female labour force participation rates in Egypt are amongst the lowest in the world. According to the latest estimates, less than 20% of women at working age participate in the labour market.[27] For young women (aged 15-24) it is around 13%, leaving 87% of young women inactive (not working and not even looking for work). Again, this has to be seen as a continuous waste of potential resources, especially when taking into consideration that young women have never before been educated in that large numbers.

3) Over-employment in the public sector:

According to the 2006 Census almost 27% of workers are employed in the government and in the public sector. Despite the fact that the Egyptian government abolished the guaranteed employment scheme in the 1990s, public sector jobs are still attracting a large proportion of young graduates.

27 - International Labour Organization (2009c)

This could be explained by the lack of entrepreneurship spirit, misconceptions regarding certain occupations, and a general mistrust in private sector practices. It has been also observed that public sector jobs remain of particular attraction as they provide high levels of protection in relation to the termination of contracts, social insurance, and comfortable working conditions.[28]

4) A large informal economy:

A large number of jobs in Egypt are found in the informal economy that continues to create a significant share of new jobs. The large size of the informal sector and its considerable absorptive capacity continue to prevent an over-shooting of unemployment to higher rates. According to the 2006 Census, the share of workers in the informal sector was 21%.

5) Low increases in productivity and wage levels:

Productivity problems in Egypt include most particularly a high labour turnover, lack of skills, and a significant degree of absenteeism.[29] Surprisingly, these are rather characteristics of a "labour deficit" country, where upward pressure on wages is to be expected. Moreover, the link between pay and productivity appears particularly weak in Egypt. In addition, job-matching procedures often hinder that vacancies are filled with the most qualified people. Senior positions are reported to be frequently filled by friends or relatives without regard to merit.[30] All these characteristics have been reflected in rather low increases in productivity over the last decade.

6) High unemployment rates, especially for women and the young:

During the first years of strong economic growth (2001 to 2005), higher economic growth succeeded in absorbing labour market entrants, but failed to translate into decreasing unemployment rates. However, the even stronger growth rates in the following years helped to bring unemployment down, from over 11.2% in 2005 to 8.7% in 2008 (Table 14). Unemployment rates reached their lowest in June 2008 at 8.4%, before the global crisis impacted on Egypt's economy (Table 15).

7) A generally inflexible labour market:

As discussed above, the Labour Law adopted in 2003 has introduced more flexibility. However, it appears that there is a continuous strong disincentive for businesses to employ full-time workers, mainly due to high costs of shedding labour, at an average 132 weeks of wages.[31]

8) Mismatches between supply and demand:

Despite the recent improvement in the quantitative indicators for education in Egypt, (increasing enrolment rates at all levels), the overall quality of education is considered as inadequate, and the link between the education system and the labour market is often missing. Sectors such as manufacturing, tourism and construction lack workers with adequate skills. The stark mismatch between outputs of education and vocational training institutions and labour market demand is causing serious economic bottlenecks. This demand-supply mismatch refers to both the number of jobs available (quantity) as well as the skills required (quality).[32] It is generally observed that the large majority of firms do not provide their employees with any structured training, with the exception of very limited on-the-job training for basic production skills. Only a small number of large local firms and multinational corporations allocate some resources for training and use more diverse training methods than the traditional on the job training.

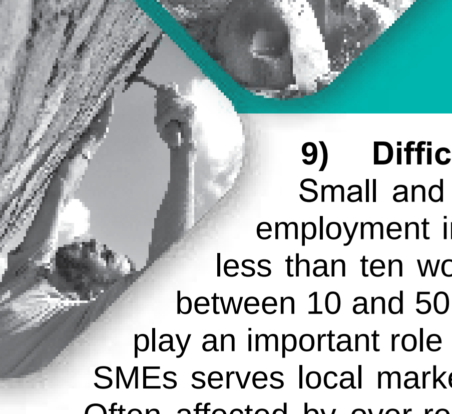
28 - For example El-Megharbel (2007).

29 - American Chamber of Commerce (2009). With regard to the underlying reasons of these factors, the study refers to subsistence thinking and the preference to work as a Government employee.

30 - Egyptian National Competitiveness Council (2009).

31 - World Bank (2009b).

32 - Ministry of Manpower and Migration; International Labour Organization (2009).



9) Difficulties for small and medium-sized enterprises:

Small and medium-size enterprises (SMEs) account for a significant share of total employment in Egypt. According to the 2006 census, Egypt had 2.4 million SMEs with less than ten workers that employed 5.2 million workers, and another 39,000 SMEs with between 10 and 50 workers.[33] There is a consensus that small and medium-sized enterprises play an important role in job creation in general, and for youth in particular. The majority of these SMEs serves local markets. Despite their importance, SMEs encounter major problems in Egypt. Often affected by over-regulation, the burden of compliance with rules and regulations frequently forces them to remain informal. Other constraints facing SMEs include the lack of human and financial resources, and general problems in Egypt's business environment (see also Box 1).

10) Weaknesses in other components of decent work:

Although employers and workers organizations exist, the potential of social dialogue for finding accepted solutions to labour market challenges is not fully used in Egypt. For example, in a recent survey analyzing the impact of the crisis on the textile sector, hardly any of the firms reported consulting workers' representatives or unions in relation to any measures taken in response to the crisis.[34] In addition, various deficiencies in Egypt's social protection system have been observed. The social security system in Egypt provides wide coverage as it includes public and private sector workers, employees working abroad and some vulnerable groups. However, it is criticized for its high contribution rates, which discourage both employees and employers from reporting actual wages and actually paying their contributions. In addition, the maximum wage according to which the social security contributions are calculated is very low. Another significant disadvantage of the system is the lack of financial sustainability.

While these labour market vulnerabilities have been tackled in the past, progress has been slow. This is why the lack of decent work opportunities has stagnated on a high level, making labour markets vulnerable to additional shocks. The lack of decent work opportunities also leads young people to look for work options outside of Egypt. Indicators measuring this brain drain show that high numbers of talented people tend to leave Egypt to pursue opportunities abroad.[35]

Table 14
Annual estimates of labour status, by sex, 2000-08

	2000	2001	2002	2003	2004	2005	2006	2007	2008
Labour force ('000)									
Males	14,702	15,213	15,534	15,839	15,880	16,787	17,767	18,167	19,120
Females	4,199	4,127	4,343	4,521	4,992	5,005	5,110	5,692	5,531
Total	18,9011	19,339	19,877	20,360	20,871	21,792	22,877	23,859	24,651
Employed ('000)									
Males	13,959	14,361	14,551	14,652	14,937	15,593	16,559	17,090	18,042
Females	3,245	3,196	3,306	3,467	3,781	3,749	3,884	4,634	4,466
Total	17,203	17,557	17,856	18,119	18,718	19,342	20,444	21,724	22,507
Unemployed ('000)									
Males	744	852	983	1,187	943	1,194	1,208	1,078	1,078
Females	955	931	1037	1,054	1,211	1,256	1,227	1,058	1,066
Total	1,698	1,783	2,021	2,241	2,154	2,450	2,435	2,135	2,144
Unemployment rate (%)									
Males	5.06	5.60	6.33	7.49	5.94	7.12	6.80	5.90	5.60
Females	22.73	22.57	23.89	23.31	24.26	25.09	24.00	18.60	19.30
Total	8.98	9.22	10.17	11.01	10.32	11.24	10.60	8.90	8.70

Source: CAPMAS

33 - The figures include both formal and informal SMEs.
34 - El-Haddad, Klau (mimeo).
35 - Egyptian National Competitiveness Council (2009).

During the crisis

In line with falling growth rates, unemployment rates increased constantly to peak at 9.43% in June 2009 (Table 15). Since then, unemployment has remained at this level. It is interesting to note that the unemployment rate increased between June 2008 and June 2009 although the total number of employed went up during the same period by over 110,000. Indeed, due to lower growth rates the labour market was not in a position to absorb the majority of new entrants during this period, although at just over 400,000, their number was low in comparison to previous years. This indicates that large numbers of people were discouraged from seeking employment or opted to stay in education. During the same period, the total number of unemployed grew by nearly 300,000, from 2.063 million to 2.369 million.

A gender-specific view on the Egyptian labour market during the crisis reveals that women were hit particularly hard. From June 2008 to June 2009, the female unemployment rate increased from 18.8% to 23.2%, while unemployment among men even decreased, from 5.4% to 5.2%.

Unfortunately, statements about developments regarding the other labour market challenges have to be left to speculation due to the lack of available data.

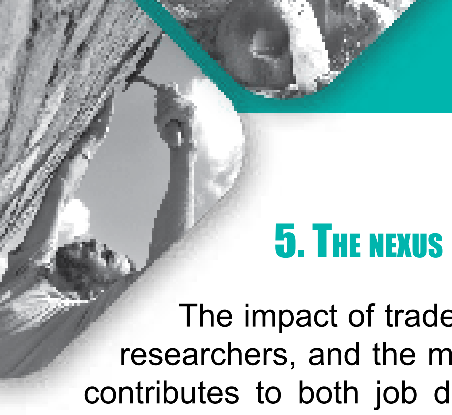
Table 15
Labour force, employment, and unemployment in Egypt, 2007-09

	1.Q	2.Q	3.Q	4.Q	1.Q	2.Q	3.Q	4.Q	1.Q	2.Q	3.Q
	31/3/07	**30/6/07**	**30/9/07**	**31/12/07**	**31/3/08**	**30/6/08**	**30/09/08**	**31/12/08**	**31/03/09**	**30/06/09**	**30/09/09**
Labour force ('000)											
M	17,812	18,075	17,902	18,210	18,639.7	19,173	19,370	19,296	19,123	19,156	19,322
F	5,525	5,350	5,635	6,120	5,549.6	5,461	5,437	5,699	5,908	5,888	5,882
T	23,337	23,424.9	23,537.2	24,330	24,189.3	24,635	24,807	24,995	25,031	25,044	25,204
Working ('000)											
M	16,724	17,002	16,828	17,125	17,589	18,135	18,243	18,209	18,130	18,160	18,305
F	4,506	4,332	4,614	4,981	4,412	4,437	4,444	4,577	4,555	4,524	4,541
T	21,230	21,334	21,442	22,106	22,002	22,572	22,687	22,786	22,685	22,684	22,846
Not working ('000)											
M	1,088	1,073	1,074	1,085	1,050	1,038	1,128	1,087	993	995	1,017
F	1,019	1,019	1,021	1,139	1,137	1,024	993	1,122	1,353	1,364	1,341
T	2,107	2,092	2,095	2,224	2,188	2,063	2,121	2,209	2,346	2,359	2,358
Unemployed rate (%)											
M	6.11	5.93	6.00	6.00	6.63	5.42	5.82	5.63	5.19	5.20	5.30
F	18.45	19.04	18.12	18.60	20.50	18.76	18.27	19.69	22.90	23.16	22.80
T	9.03	8.93	8.90	9.10	9.00	8.40	8.6	8.8	9.37	9.42	9.40

* Preliminary Data.

Note: Figures may not add up to totals because of rounding. Figures do not include those working outside the country.

Source: CAPMAS Quarterly Labour Force Sample Survey.



5. The nexus between trade and employment in Egypt

The impact of trade flows on employment has become a contentious issue for policy-makers, researchers, and the media. One of the key findings of research in this area has been that trade contributes to both job destruction and job creation. The liberalization of trade flows leads to a restructuring of economic activity and employment reshuffling across, but also within sectors.[36] This reshuffling is a continuous process and took place even before the crisis. Given the weaknesses of the labour market in Egypt, this process may hit vulnerable groups particularly hard due to the many constraints that make it difficult to find decent job opportunities. The crisis further added to the difficult situation of vulnerable groups in the labour market. However, the overall impact of the current crisis on employment is likely to vary strongly among economic sectors. Outward-oriented sectors, which are directly exposed to external demand shocks, and sectors that are employment-intensive can be expected to have the highest number of job losses. On the other hand, inward-oriented, highly protected or less employment-intensive sectors are likely to experience less job losses.

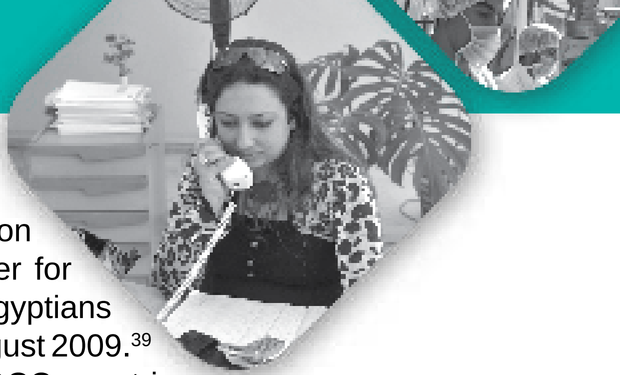
An estimation of the exact number of jobs lost as a result of the crisis would require the following data: (1) exports by sector, (2) employment by sector (ideally with the same sector classification as used for the trade data), (3) employment-to-growth or employment-to-exports elasticities by sector. Unfortunately, the calculation of elasticities and of job losses is precluded by the lack of up to date sectoral employment data. To escape the data dilemma, a very simple, more qualitative and sector-specific approach was chosen, judging the employment impact of the crisis on each sector by either sector-specific studies that had been commissioned[37], information gained through interviews of decision-makers, or on historically known employment elasticities (Table 16).

Table 16
Estimated employment impact of the global crisis, by sector

Sector	Contribution to GDP in 2007/08	Importance in trade, export decline during crisis	Employment elasticity[a]	Estimated crisis impact on employment
Agriculture and food industries	High, some 13% of GDP	Limited, as production is mainly for domestic consumption	High, with high importance of the sector for overall employment	Limited, as the sector has been sustained by domestic demand
Oil and natural gas production (incl. refining)	High, 16.4% of GDP	High, very strong declines in export revenues	Low	Limited, due to low importance for overall employment
Textiles and clothing	Medium, 2.9% of GDP	High, strong declines in export revenues	High	High, with massive lay-offs
Construction	Medium, 4.3% of GDP	Low	High	Limited, as the sector has been sustained by domestic demand and is the main beneficiary of the fiscal stimulus package
Suez Canal	Medium, 3.6%	High, strong declines in export revenues	Low	Limited due to low overall employment
Tourism	Medium, 3.8% of GDP	High, strong declines in export revenues	High	High, with massive lay-offs
Financial services	Medium, 4.1% of GDP	Limited	Medium	Limited due to high inward orientation and low importance for overall employment
Information and communication technology	Medium, some 4% of GDP	Limited	Medium	Limited, due to continued high sectoral growth

a The classification of sectoral employment elasticities is based on El-Ehwany/El-Megharbel (2009).

36 - International Labour Organization, World Trade Organization (2007).
37 - El-Haddad, Klau (2009), Zaytoun (2009).



The employment-impact of the crisis also heavily depends on the number of migrant workers that returns from abroad, in particular from the Gulf states where an estimated 2 million Egyptians are working.[38] According to estimates of the Center for Trade Union and Workers Services, more than 75,000 Egyptians returned from the Gulf countries between October 2008 and August 2009.[39] Thus, economic prospects and labour market policies in the GCC countries have a direct impact on Egypt's labour market situation.

6. Sectoral analysis

6.1. Manufacturing

Manufacturing (including oil refining) accounts for some 19% of GDP and employs an estimated 11.3% of the labour force. In recent years, industrial production in the once-dominant public sector has declined and private-sector production has increased sharply, in response to privatisation and liberalisation initiatives. The vast majority of private manufacturers are small units, and more than 90% of employment is in enterprises of 15 people or fewer. While Egypt produces a wide range of goods, the bulk of manufacturing value added comes from food-processing and textiles.

6.1.1. Textiles and Clothing

Egypt's TC sector is important in terms of contribution to employment, GDP, and foreign exchange generation. The TC industry owes much to the abundant production of high-quality cotton in Egypt, as well as to the large availability of relatively cheap labour. In 2006, the sector contributed 2.9% to GDP. In 2007, there were 6,480 companies in the TC sector which range in size from less than ten workers to more than one thousand.[40] Total employment in the sector is over 400,000.

Despite its ongoing importance for Egypt's economy, the TC sector has experienced a relative decline over the past years. In 1998, the sector still accounted for 15% of all manufacturing jobs and 3.4% of GDP. This contraction was mainly due to the shrinkage of public companies in the sector, which was not offset by comparable growth of private companies.[41] Factors that contributed to the relative decline of Egypt's TC sector include the phase-out of the Multi-fibre Agreement, which gradually subjected textiles and clothing to normal WTO rules (thereby improving market access of some of Egypt's main competitors), and the Government's Economic Reform and Structural Adjustment Program (ERSAP) of 1991, which resulted in a scaling down of publicly owned TC companies.

At less than one US dollar per hour, average labour costs in Egypt's TC sector are relatively low (actually the lowest in the MENA region), and comparable to China's. Nevertheless, Egypt's TC sector suffers from low productivity, which largely erodes the advantage of low labour costs. Despite the renowned quality of Egyptian cotton, this makes it difficult for Egypt's TC sector to compete globally with "labour surplus", low-wage countries in Asia unless productivity improvements are made.

38 - Nassar (2009).
39 - Center for Trade Union and Workers Services (2009).
40 - Industrial Development Authority online information available at: http://www.ida.gov.eg/Egmaly_en.html (4 June 2009).
41- Arab Federation for Textile Industries; Arab Trade & Development Programme (2009), p.3.

Tariffs on textiles and clothing products are relatively high, averaging 24.4%. While this guarantees a high level of protection of the national market, it should be noted that the bulk of production is for exportation. Weaving and spinning machines are imported tariff-free. TC companies are the main users of the QIZ Agreement. In 2007, the last year for which figures on TC exports broken down by export region are available, Egypt exported TC products worth US$652 million, of which US$319 million to European countries and US$129 million to the US. The share of TC products imported from Egypt has increased both in the EU and the US since 2000.

A recent impact assessment Egypt's TC sector came to the result that a dramatic decline in both production (by some 25%) and exports (by some 22%) occurred as a result of the global economic crisis, although TC companies were the main users of the newly introduced export subsidies.[42] This decline translated into a striking 70,000 job losses. The decrease in employment was most pronounced for women and low skilled workers, and among informal companies. Job losses mainly took place in textiles companies (74,000), while clothing even experienced a modest growth in production and employment (plus 3,200).

6.1.2. Local assembly industries

The fiscal stimulus package also included an exchange scheme for cars to promote local assembly industries. Under the scheme, which totalled LE 1.4 billion in the form of tax and duty exemptions and preferential loans, taxi drivers were allowed to exchange their old cars for new ones assembled in Egypt.

6.2. Tourism

Tourism is by far Egypt's most important source of foreign exchange and an important generator of employment. Revenues derived from tourism increased strongly between 2003 and 2008 (Table 17). Total employment in the tourism industry increased from 187,000 in 2003 to 225,000 in 2008.

Table 17
Tourism industry: 2003/04 to 2008/09

	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09
Number of tourists arrivals (‹000)	7,512	8,651	8,693	9,788	10,706	..
Tourist nights (‹000)	73,002	85,730	85,113	96,270	110,968	..
Tourist revenues (US$ million)	5,475	6,430	7,235	8,183	10,827	10,488

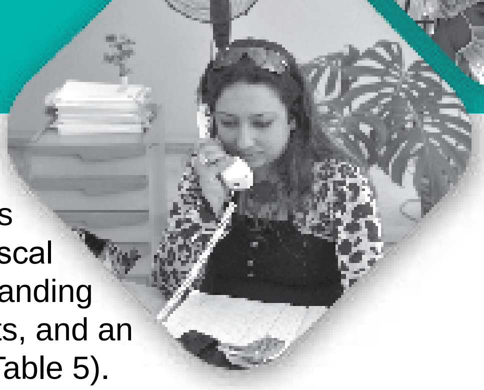
.. Not available.

Source: CAPMAS, Ministry of Finance Quarterly Monitor.

As a result of the global economic crisis, income derived from international tourism fell from over US$ 10.8 billion in 2007/08 to less than US$ 10.5 billion in 2008/09. The decline peaked in the third quarter of 2008/09 when the yearly growth rate amounted to -17.2%.[43] The decline in tourist arrivals has also affected the construction sector and the local sales of the food industries.

A recent impact assessment Egypt's tourism sector, which is characterized by a relatively high skill level of its employees, came to the result that only few companies reacted with dismissals, but rather in ceasing new appointments, wage and bonus reductions and compulsory

42 - El-Haddad, Klau (2009).
43 - Zaytoun (2009).



vacation.[44]

Following the outbreak of the crisis, the tourism sector has been subject to a number of special measures under the fiscal stimulus package. This has included the rescheduling of outstanding debt for tourism projects, the provision of loans for new projects, and an increase of the public marketing budget for tourism (see also Table 5).

6.3. Construction

Egypt construction industry is one of its fastest-growing sectors. The construction sector employs an estimated 7.7% of Egypt's labour force and contributed 4.3% of GDP in 2007/08, after growing strongly by 14.8% in 2007/08 and 15.8% in 2006/07.[45] The 2008/09 growth rate slowed to 11.4%. While the growth of the sector has been spurred in part by the housing demands of an ever-increasing population, it has largely been fuelled by the state's continued investment in large infrastructure projects.

The construction industry has benefited from the government's support of existing large-scale infrastructure projects as well as the support of new projects in the wake of the financial crisis. Of the total LE 15 billion stimulus package issued in March 2009, over half of the budget was directed to stimulate or sustain the construction of infrastructure for public utilities such as water and sewage facilities, roads and bridges, health centres, and schools.[46]

Still, while the construction industry continues to be supported by government spending, this does not a priori translate into increased or sustained levels of employment. In monitoring the response to the global financial crisis, from March to September 2009 the Centre for Trade Union and Workers Services documented lay-offs of 2,667 workers from 29 companies in the construction sector.[47]

6.4. Suez Canal

While the importance of the Suez Canal for employment is limited, fees for using the Canal are a major generator of foreign exchange and an important income category in the state budget. The Suez Canal has performed well in the years before the crisis as high fuel prices have made the longer trip around Africa more expensive for ships travelling between Europe and Asia. However, in the course of the crisis and resulting directly from declining world trade, income dropped from US$ 5,155 million in 2007/08 to US$ 4,721 million in 2008/09.

6.5. Petroleum

Extractive activities, mainly the production of natural gas and oil, accounted for 16.4% of GDP in 2007/08. During the first half of 2008, oil and natural gas prices continued to rise rapidly, leading to huge gains for petroleum producers. By July 2008 the effects of the financial crisis and expectations of much lower global growth caused a collapse in oil prices. As Egypt is a net importer of oil and petroleum products, the current account has improved to the extent that the cost of these imports will decline. Natural gas, on the other hand, is exported according to long-term agreements with fixed prices, implying less vulnerability to price shocks and stability for related fiscal revenues. In terms of contribution to employment, however the sector is of limited importance, at just over 1%. For this

44 - Zaytoun (2009).
45 - African Economic Outlook, Country Report, 2009.
46 - See Table 5
47 - Centre for Trade Union and Workers Services (2009).

reason, the employment impact of the global crisis in the petroleum sector can be expected to be limited.

6.6. Financial services

Just some 0.8% of the labour force is engaged in financial and insurance activities. The impact of the economic crisis on Egypt's financial services sector was less pronounced than on other sectors. First, this is due to the fact that Egypt's banking sector is not highly integrated into the global financial system. Secondly, financial sector regulation is relatively tight in Egypt. For example, the Central Bank of Egypt (CBE) stipulates that mortgage finance activities should not be more than five percent of a bank's loan portfolio and that bank's resource terms should be consistent with lending maturity for mortgage finance. Moreover, the CBE prohibits any bank to save more than ten percent of its deposits at offshore banks in order to avoid bankruptcy dangers.

6.7. Other sectors

Agriculture and food industries

The agriculture sector employs some 27% of the labour force and contributes about 13% to GDP. Though the productivity of the sector is low, farming plays an important role in rural incomes and employment. Most domestically produced agriculture and food products are highly tariff-protected Egypt's agriculture sector is inward-oriented. Some 95% of local production is consumed domestically, despite the increased emphasis on some cash crops for export, such as soft fruits and green beans. Nevertheless, population growth will ensure that Egypt remains a major food importer.

Information and communication technology

The information and communication technology (ICT) sector is one of the fastest growing sectors in Egypt with a share of nearly 4% in GDP.[48] ICT exports, consisting mainly of software and call centre services, were around LE 4.2 billion in 2008. Over the past decade, Egypt has been heavily investing in infrastructure, educational and telecommunications projects to drive interest from companies looking to establish global service delivery centres.[49] Investments in the sector reached LE 14.7 billion in 2007/08, compared to LE 9.6 billion investments in 2006/07.[50] The growing global demand for ICT products and services lead to a fourfold increase in the number of ICT companies in Egypt between 2000 and 2007. As of 2007, an estimated 2,262 ICT companies were registered in Egypt, employing a labour force of some 50,000.[51]

Despite the overall growth of the sector, in the wake of the financial crisis some multinationals operating in Egypt announced cost reductions by adopting a conservative marketing strategy as well as the freezing of non-revenue generating employment. In April 2009, the Ministry of Communications and Information Technology announced a further LE 400 million stimulus for ICT projects, in addition to the portion previously directed from the fiscal stimulus package.[52] The additional expenditure was directed to support infrastructural projects aimed at increasing the local demand on ICT services and the development of e-content, portals, information systems and call centres.

48 - Ministry of Communications and Information Technology: http://www.mcit.gov.eg/ ICT includes: software development, communications, telecommunications, information services, business services, software services, internet and e-commerce activities, IT product and services marketing and export, and peripheral industries.
49 - A.T. Kearney (2009).
50 - AmCham, Egypt Economic Profile, March 2009.
51 - Ministry of Communications and Information Technology: http://www.mcit.gov.eg/
52 - Osama Diab, «IT Sector Stimulus», Business Today, June 2009.

7. Conclusion and recommendations

7.1. Summary of findings

The impact of the global economic and financial crisis on Egypt has been considerable. GDP growth rates declined by over three percentage points, and foreign investment inflows decreased by over 50%, while the unemployment rate grew by more than one percentage point. The economic impact of the crisis varied strongly by sector, with the most negative employment effects in the textiles and clothing sub-sector.

On the other hand, Egypt's economy demonstrated relative resilience to the global economic crisis as compared to other developing and emerging economies. Nevertheless, the prolonged slowdown in global demand and the volatility in some basic commodity prices continue to constitute a threat to economic growth and employment. Having external demand and foreign investment playing an increasingly important role in spurring growth in the past years, the grim outlook for the world economy brings with it considerable challenges to Egypt's economy. Weakening exports of goods and services and decreasing foreign direct investment is likely to hold back economic growth, and reduce record rates achieved between 2004/05 and 2007/08.

7.2. Lessons learned from the crisis, policy recommendations and outlook

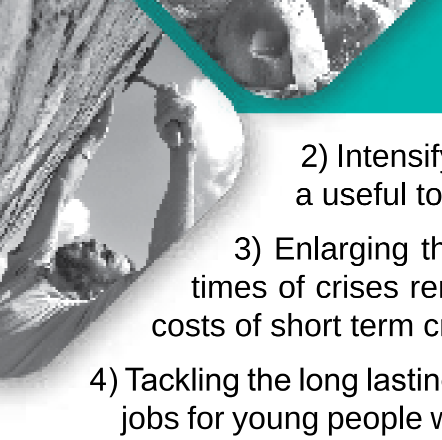
As in other countries trade has not been a cause of the crisis, but one of the channels through which the crisis has been transmitted. Openness is conducive to economic growth and job creation. The government remains committed to carrying ahead its reform program set in motion in 2004. Given its improved economic and institutional fundamentals, the Egyptian economy is expected to maintain its resilience in face of this crisis and also future international economic crises that might occur.

Signs of recovery were evident in Egypt's economy during the second half of 2009. Exports between July and September 2009 were 5.3% above the level of the same period in 2008. Economic activity is expected to continue to soften in 2009/10, with real GDP growth projected to be around 4%.[53] However, the risks of this projection remain tilted to the downside. If the global recession becomes entrenched, or the fallout from the global financial crisis feeds through to the domestic banking sector, the recovery in the Egyptian economy may not be as strong.

Although at end-2009 Egypt appears to have passed the bottom of the crisis, a number of crisis-related policy challenges remain of importance even if the economy is back on its previous growth path.

1) Analysing the employment impact of the trade shocks incurred in the current crisis is difficult because of a lack of adequate data. Thus, improving the quality of economic data in Egypt remains a key challenge. No useful evaluations can be performed when the underlying data are inaccurate, and in turn no accurate policy recommendation can be drawn. A number of suggestions has been made with regard to the institutional design of data collection, e.g. that this should be confined to the particular institution most relevant. The timely publication of consistent data of employment by sector would also allow better judgements of labour market effects of specific policy measures and economic crises in general. Data that is regularly produced should be made publicly available. By the same token, transparency in governance should be increased. Laws and regulations that are in force should be posted on the website of the relevant ministry.

53 - International Monetary Fund (2009).



2) Intensifying social dialogue, particularly in sectors that are prone to crises, has been a useful tool in many other countries, and should be considered in Egypt.[54]

3) Enlarging the scope of social protection schemes to make workers less vulnerable in times of crises remains a key challenge. In the long run, this should also help to reduce the costs of short term crisis responses.

4) Tackling the long lasting issues of the labour market, especially creating sufficient number of decent jobs for young people will foster development and lessen the impact of economic turbulences in the future.

5) In the longer run, undertaking further reforms that continue improving the business and investment climate and support real cost reduction at the enterprise level remains of key importance. Trade liberalization, either unilateral through the reduction of MFN tariff rates or regional through additional free-trade agreements, may give a boost to competitiveness. It has been noted, for example, that promoting free trade in services with the EU would reduce transport costs for exports to the EU by 10% and 15% for imports from the EU.[55] Such trade agreements would also attract additional foreign direct investment.

6) Increasing productivity remains a key challenge for the coming years. Prerequisites to raising productivity include improving the quality of education, adopting a clear and well targeted training strategy, establishing a closer link between pay and productivity, and ameliorating the work environment and ethics. The government's infrastructure programme and continued economic reform should help to boost productivity and increase Egypt's growth potential in the longer term.

54 - International Labour Organisation (2009[d])
55 - World Bank (2009).

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IV. TABLES AND BOXES

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Boxes

(Footnotes)
1 World Bank (2009b).