Table I.1: Selected Economic and Financial Indicators (2001/2002 - 2008/2009) *

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<tr>
<th></th>
<th>Jun-02</th>
<th>Jun-03</th>
<th>Jun-04</th>
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<tr>
<td>GDP at Market Prices (LE Billions)</td>
<td>378.9</td>
<td>417.5</td>
<td>485.3</td>
<td>538.5</td>
<td>617.7</td>
<td>744.8</td>
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<td>GNP (LE Billions)</td>
<td>393.2</td>
<td>432.1</td>
<td>502.8</td>
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<td>649.4</td>
<td>787.4</td>
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<tr>
<td>Real GDP (% Growth Rate)</td>
<td>3.2</td>
<td>3.2</td>
<td>4.1</td>
<td>4.5</td>
<td>6.8</td>
<td>7.1</td>
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<td>Real Per Capita GDP (% Growth Rate)</td>
<td>1.1</td>
<td>1.2</td>
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<td>4.9</td>
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<tr>
<td>Average Per Capita Income (LE)</td>
<td>5,742.1</td>
<td>6,202.4</td>
<td>7,069.4</td>
<td>7,693.2</td>
<td>8,657.6</td>
<td>10,211.1</td>
<td>12,030.0</td>
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<tr>
<td>Share of Private Sector in GDP (%)</td>
<td>65.7</td>
<td>63.2</td>
<td>62.2</td>
<td>61.7</td>
<td>60.3</td>
<td>62.4</td>
<td>61.6</td>
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<tr>
<td>Overall Fiscal Balance (% GDP)</td>
<td>(10.2)</td>
<td>(10.4)</td>
<td>(9.5)</td>
<td>(9.6)</td>
<td>(8.2)</td>
<td>(7.3)</td>
<td>(6.8)</td>
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<td>Net FDI in Egypt (%GDP)</td>
<td>0.5</td>
<td>0.9</td>
<td>0.5</td>
<td>4.4</td>
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<td>8.5</td>
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<td>Public Domestic Debt (% GDP)</td>
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<tr>
<td>Net Domestic Budget Sector Debt</td>
<td>64.8</td>
<td>67.5</td>
<td>67.4</td>
<td>72.5</td>
<td>72.0</td>
<td>64.2</td>
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<td>Net Domestic General Government Debt</td>
<td>44.6</td>
<td>46.1</td>
<td>46.8</td>
<td>51.5</td>
<td>53.8</td>
<td>49.6</td>
<td>42.7</td>
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<td>Net Domestic Public Debt</td>
<td>45.6</td>
<td>46.3</td>
<td>46.8</td>
<td>52.3</td>
<td>53.9</td>
<td>48.8</td>
<td>43.2</td>
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<td>Inflation Rates</td>
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<tr>
<td>CPI (% Growth Rate yoy) 2</td>
<td>2.4</td>
<td>3.2</td>
<td>10.3</td>
<td>11.4</td>
<td>4.2</td>
<td>11.0</td>
<td>11.7</td>
<td>16.2</td>
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<tr>
<td>WPI (% Growth Rate yoy) 3</td>
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<td>11.6</td>
<td>17.3</td>
<td>9.9</td>
<td>4.1</td>
<td>11.8</td>
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<td>PPI (% Growth Rate y04) 4</td>
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<td>--</td>
<td>4.1</td>
<td>11.8</td>
<td>17.7</td>
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<td>Exchange Rates</td>
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<td>Official Exchange Rate (LE / US$)</td>
<td>4.4</td>
<td>5.2</td>
<td>6.2</td>
<td>6.0</td>
<td>5.7</td>
<td>5.7</td>
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<tr>
<td>Parallel Exchange Rate (LE / US$)</td>
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<td>6.2</td>
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<tr>
<td>Interest Rate on T-Bills (91 days)</td>
<td>7.2</td>
<td>8.3</td>
<td>8.4</td>
<td>10.1</td>
<td>8.8</td>
<td>8.7</td>
<td>7.0</td>
<td>11.3</td>
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<tr>
<td>Broad Money (% Growth Rate y0y)</td>
<td>15.4</td>
<td>16.9</td>
<td>13.2</td>
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<td>13.5</td>
<td>18.3</td>
<td>15.7</td>
<td>84.5</td>
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<tr>
<td>External Debt</td>
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<td></td>
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<tr>
<td>External Debt (% GDP)</td>
<td>34.0</td>
<td>42.5</td>
<td>38.1</td>
<td>31.1</td>
<td>27.6</td>
<td>22.8</td>
<td>20.1</td>
<td>17.0</td>
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<tr>
<td>External Debt (% Exports of G&amp;S)</td>
<td>171.2</td>
<td>157.6</td>
<td>127.5</td>
<td>100.3</td>
<td>82.4</td>
<td>70.4</td>
<td>59.9</td>
<td>64.4</td>
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<td>Debt Service (% Current Receipts)</td>
<td>9.7</td>
<td>10.1</td>
<td>9.2</td>
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<td>7.3</td>
<td>5.9</td>
<td>3.9</td>
<td>5.3</td>
</tr>
<tr>
<td>Debt Service (% Exports of G&amp;S)</td>
<td>12.2</td>
<td>12.1</td>
<td>10.8</td>
<td>9.4</td>
<td>8.5</td>
<td>6.9</td>
<td>4.6</td>
<td>6.2</td>
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<tr>
<td>NIR in Months of Imports (US$ Millions)</td>
<td>11.6</td>
<td>12.0</td>
<td>9.7</td>
<td>9.6</td>
<td>9.0</td>
<td>8.9</td>
<td>7.9</td>
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<tr>
<td>Population (% Growth Rate)</td>
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<td>2.0</td>
<td>2.0</td>
<td>1.9</td>
<td>2.2</td>
<td>1.9</td>
<td>NA</td>
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<tr>
<td>Domestic Savings (LE Billions)</td>
<td>51.7</td>
<td>59.7</td>
<td>75.6</td>
<td>84.6</td>
<td>105.7</td>
<td>121.2</td>
<td>150.4</td>
<td>129.1</td>
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<tr>
<td>National Savings (LE Billions)</td>
<td>66.0</td>
<td>74.3</td>
<td>93.1</td>
<td>109.4</td>
<td>137.4</td>
<td>163.8</td>
<td>204.1</td>
<td>172.2</td>
</tr>
</tbody>
</table>


* Recent detailed data can be found in the Appendices. Historical data are available at www.mof.gov.eg

** Preliminary

Note: June 2002 refers to the Fiscal Year July 2001 through June 2002.

1. The Revised Budget 2008/09 the Overall Fiscal Deficit (%GDP) was -8.0 percent and the Overall Fiscal Deficit (%GDP) 2009/2010 is 8.4 percent.

2. In August 2009, the CPI reached 9 percent. Starting January 2005, Annual and Quarterly CPI (urban areas) data is based on weights derived from 2004/2005 income and expenditure survey, and using January 2007 as a base month. Prior to this date, the basket and weights were derived from 1999/2000 income and expenditure survey, and using January 1999 as a base year.

3. Starting September 2005, WPI data is based on the average weights derived from indices of Industrial and agricultural sectors for the 2 years period extending from 1999/2000 to 2000/2001. Prior to this date, the basket and weights were derived from indices of Industrial and agricultural sectors for the period extending from 1986/1987 to 1987/1988.

4. In August 2009, the PPI reached -8.4 percent. The new series of Producer Price Index (PPI) was issued by CAPMAS starting September 2007, using 2004/2005 prices of goods and services as a base period, and deriving sub-group weights from average values of agricultural, industrial and services production for the years 2002/2003 and 2003/2004. It is worth mentioning that Producer Price Index series before September 2007 are not available so far.

5. Value in monthly basis. In July 2009, the monthly Broad Money growth rate was 7.9 percent.

6. In August 2009, the NIR in Months of Imports 7.8 US$ millions, it is estimated on the basis of merchandise imports during the first half of 2007/08.

Note: At the end of August 2009, Net International Reserves (NIR) reached US$ 32.9 millions.
The world economy has witnessed the worst financial crisis since the 1930s.

During the past century, the world economy has witnessed a number of financial and banking crises. More recently, the past decade saw the growth of macroeconomic imbalances that gave flawed macro-incentives in the housing market and the financial system. A financial innovation boom that benefited from these incentives created mortgaged backed securities and other complex financial instruments that offered high rewards and were believed to be spreading risk, not concentrating it. As the demand for cheaply financed housing increased, these instruments were extended to the sub-prime housing market, and a growing asset price bubble emerged.

Telltales for the current crisis started as early as August 2008 when it became obvious that the increasing high asset prices would not be sustainable in the face of the defaults that were spreading rapidly in the housing/mortgage sub-prime market. In September 2008, the housing/sub-prime mortgage problem brought down the world mortgage market and the banks and organizations that had invested in these papers. The global financial system was affected as banks saw significant write-downs that led to a worldwide credit freeze (to a lesser extent in emerging economies). Immediate liquidations of big American banks and organizations that had invested in these sub-prime securities further compounded the crisis.

The resulting global financial turmoil that unfolded rapidly in the following months is considered to be the worst since the Great Depression of the 1930s. It has highlighted the lack of regulatory oversight and the need for change in many of today’s adopted financial rules and regulations.

The crisis has severely hit all world economies, but in different ways and degrees:

- From finance and housing to the real economy in advanced countries

The financial crisis has substantial implications to the world financial system. The crisis immediately spread to the real economy in all advanced economies. The United States and Europe were affected directly by the credit crunch which almost immediately froze all consumption and investment financing. As bank lending in these countries came to a near-standstill, investment spending tumbled, industrial output weakened, workers were laid off, households started to save, and demand for goods from emerging markets waned. As a result economic growth rates started to slow down almost immediately, and turned negative in some countries in 2009.

- From developed markets to emerging ones

No country was exempt from the crisis. Most emerging countries however felt the impact of the crisis a few weeks later, and their economies eventually slowed down through their investment and trade links with the advanced markets. As their cash dried up, foreign investors became nervous, and less foreign direct investment flowed from rich nations to emerging nations, putting infrastructure and real estate projects at risk in these countries. External demand diminished and exports of emerging markets declined.

Furthermore, it became more difficult for indebted countries to borrow as credit became rare. The risk of default was increased even among advanced countries. However, the prices of oil and other raw material spiraled down, pulling down inflation rates, helping real incomes of the poor who lost jobs or suffered lower incomes as the crisis intensified and its impact passed through to the emerging countries. Average real wages are expected to increase by 0.6 percent during 2009 compared to a negative one percent in 2008.

Global growth rate, therefore, is expected to be zero or negative in some big economies.

World growth is projected to fall to only 1.3 percent in 2009 according to the April 2009 edition update of the IMF’s World Economic Outlook (WEO), its lowest rate since World War II. Despite wide-ranging policy actions, financial strains remain acute, negatively impacting the real economy in many countries. The economic recovery will be possible when confidence is restored, credit markets start flowing again, restoring the functionality of the global financial sector.

In the meantime, monetary and fiscal policies are becoming more supportive of aggregate demand. China, for example, has already moved to increase subsidies to exporters and has reduced interest rates to enhance investment. The US fiscal stimulus plan was designed to give tax rebates and promote investments pending in selected areas. However the long-term fiscal sustainability of Government spending is now a major issue, especially in highly indebted countries. International cooperation will be critical in designing and implementing stimulus policies. Arbitrary measures should be avoided as no one country can gain any advantage by itself but through the concerted efforts of the international community.
The financial crisis has also shown the imperative need for reforming the international financial architecture. The IMF anticipated the housing problem depression and its consequences on world growth many months before the occurrence of the crisis, but its policy warnings were not focused or specific. For many reasons, it was not able to prescribe the appropriate measures to deal with the expansionary and competing monetary policies of the US and China, nor supervise the development of the complex financial instruments that took advantage of excessively cheap credit in the global system, spreading very risky and later toxic mortgage papers that became significant components of the investment portfolios of big companies and financial institutions all over the world. As these papers lost value, these companies suffered such substantial losses that they were either dissolved or bailed out.

**Box (I.1.1): Measures Taken by the US Government to Lessen Impact of the Financial Crisis**

On Sep 16, 2008: Federal Reserve Board, with full support of the Treasury Department, authorizes the Federal Reserve Bank of New York to lend up to $85 billion to the American International Group (AIG).

On Oct 3, 2008: Emergency Economic Stabilization Act of 2008 (TARP) signed, enabling Treasury to purchase troubled assets from financial institutions, with authority to manage purchased troubled assets and to sell or enter into securities, loans, repurchase transactions, or other financial transactions with respect to them, $700 billion was allocated for this plan.

On Oct 14, 2008: It was agreed to use 250 bn of TARP funds to take capital stakes through Capital Purchase Program via senior preferred, non-voting shares (Tier I) in qualifying financial institution (QFI). Nine major US banks (Citigroup, Bank of America, Goldman Sachs, Wells Fargo, JP Morgan, Morgan Stanley, Merrill Lynch, State Street, Bank of New York Mellon) have signed up to date. On Oct 27, 2008: In addition to 9 of the top banks receiving $125 billion from TARP. (first tranche of $250 billion infusion announced on October 14), 16 other banks have accepted $33 billion in the second phase of the infusion.

On Nov 25, 2008: The Federal Reserve Board announced the creation of the Term Asset-Backed Securities Loan Facility (TALF), a facility that will help market participants meet the credit needs of households and small businesses by supporting the issuance of asset-backed securities (ABS) collateralized by student loans, auto loans, credit card loans, and loans guaranteed by the Small Business Administration (SBA). Under the TALF, the Federal Reserve Bank of New York (FRBNY) will lend up to $200 billion on a non-recourse basis to holders of certain AAA-rated ABS backed by newly and recently originated consumer and small business loans. The FRBNY will lend an amount equal to the market value of the ABS less a haircut and will be secured at all times by the ABS. The U.S. Treasury Department—under the TARP will provide $20 billion of credit protection to the FRBNY in connection with the TALF. The Federal Reserve also announced that it will initiate a program to purchase the direct obligations of housing-related Government sponsored enterprises (GSEs)—Fannie Mae, Freddie Mac, and the Federal Home Loan Banks—and mortgage-backed securities (MBS) backed by Fannie Mae, Freddie Mac, and Ginnie Mae. Purchases of up to $100 billion in GSE direct obligations under the program will be conducted with the Federal Reserve’s primary dealers through a series of competitive auctions and will begin next week. Purchases of up to $500 billion in MBS will be conducted by asset managers selected via a competitive process with a goal of beginning these purchases before year-end.

On Feb 10, 2009: A new Financial Stability Plan will replace the current program and there are three main measures that were introduced. The first initiative is the Financial Stability Trust. Going forward, all Treasury’s investments in institutions which need capital will be placed in this new trust and institutions will have to adhere to the following requirements. (i) All banking institutions have to go through a carefully designed comprehensive stress test and provide capital to banks who need it. (ii) Introduce
new measures to improve disclosure. (iii) For those institutions that need additional capital, they will be given access to a new funding mechanism that uses funds from the treasury as a bridge to private capital. The second initiative is the creation of a Public-Private Investment Fund which targets distressed assets of financial institutions. The private sector will be called on providing a market mechanism for valuing the assets. This program which will initially rely on public funding will start off with $500 billion with the possibility of expanding it up to 1 trillion. The third initiative is Consumer and Business Lending Program. The lending program will be built on the Federal Reserve's Term Asset Backed Securities Loan Facility (TALF) that was announced last November. The expansion could increase the size of the TALF to as much as $1 trillion and could broaden the eligible collateral to encompass other types of newly issued AAA-rated asset-backed securities, such as commercial mortgage-backed securities, private-label residential mortgage-backed securities, and other asset-backed securities. An expansion of the TALF would be supported by the provision by the Treasury of additional funds from the Troubled Asset Relief Program. The date that the TALF will commence operations will be announced later this month.

On Feb 18, 2008: The Government announced the Homeowner Affordability and Stability Plan. The main measures of the plan are:

i. Refinancing for up to 4 to 5 million responsible homeowners to make their mortgages more affordable.

ii. A $75 billion Homeowner Stability Initiative to reach up to 3 to 4 million at-risk homeowners. A key thrust of this plan is to provide loan modifications so as to bring monthly payments to sustainable levels.

iii. Supporting low mortgage rates by strengthening confidence in Fannie Mae and Freddie Mac.

The $200 billion in funding commitments are being made under the Housing and Economic Recovery Act and will not use any money from the Financial Stability Plan or Emergency Economic Stabilization Act/TARP.

On March 4, 2009, AIG has agreed to issue shares of convertible preferred stock where the Treasury will have a 77.9 percent stake in AIG. The Treasury will also inject other $30 billion into AIG from the TARP Fund by creating a new equity capital facility, in exchange for non-cumulative preferred stock. The $60 billion Revolving Credit Facility for AIG will be reduced from $60 billion to no less than $25 billion. In exchange for New York Fed's preferred stock interests, the Treasury will take a $26 billion stake in American International Assurance (AIA) – AIG's large Asian operations – and American Life Insurance Company (ALICO), a global life insurance business. The New York Fed is authorized to make new loans to an aggregate amount of approximately $8.5 billion to special purpose vehicles (SPVs) established by domestic life insurance subsidiaries of AIG.

The US adopts the biggest bail-out plan in history, and Japan seeks to get out of its worst crisis.

The US House and Senate passed the American Recovery and Reinvestment Act. It was signed by President Obama on February 2009 in order to provide a US$787 billions as stimulus package. The aim of this package is to create more than 3.5 millions job opportunities over the next two years. Of the total amount, 22 percent will be spent in 2009 and the rest in 2010.

On the other hand, Japan, the second biggest world economy, faces critical economic conditions. The rise of the yen against the dollar and the euro was a major factor in the deterioration of Japan's external competitiveness, a long cornerstone of its economic performance.

As for the repercussions of the crisis on the Egyptian economy, it is important to differentiate between two categorical impacts

In general, Egypt has been protected from financial shocks but exposed to real shocks in the economy. Egypt’s financial system is less integrated into the world's financial system than many other countries. Capital flows while increasing, they have been relatively limited. The amount of portfolio investments has also been fairly small, and the Egyptian banks are not very strongly integrated into the international system. Egypt, in that sense, has been fairly protected. However, it is not protected from the impact on the real economy from external shocks that may come from a drop in tourism revenues, volatility in oil prices, or shifts in foreign direct investment (FDI). Thus although on financial sector side Egypt was not highly exposed, its real economy is likely to be vulnerable through the external sector channel.
• First impact will be on the sectors that are directly affected by external shocks, such as workers’ remittances, Suez Canal, tourism, and exports receipts...

Some 70 percent of Egypt’s foreign exchange earnings come from services, mainly the Suez Canal and tourism. Available data for the first quarter of 2008/2009 (July-September 2008, i.e., before the financial crisis occurred) reveal an increase in tourism revenues and Suez Canal receipts. More recent data (June 2009) show that tourism was slightly affected by the present crisis. Tourism witnessed a decrease of 3.1 percent in fiscal year 2008/2009 compared to previous equivalent period. Government expects that tourism industry to fully recover from the global financial crisis by the third quarter of 2010. Tourism revenues could average US$11 billions in 2009/2010, higher than the US$10.8 billions and US$10.5 billions generated in 2007/2008 and 2008/2009 respectively.

Suez Canal receipts went down by 8.4 percent. Revenues have restored its rising trend as the global economy started to recover, especially trading with Asia, which served to boost non-oil traffic and tonnage. It is expected that revenues could reach US$4.8 billions in 2009/2010, compared to US$5.2 billions in 2007/2008 and US$4.7 billions in 2008/2009, assuming the Canal Authority will keep its transit rates unchanged in April 2010.

Remittances from Egyptian workers abroad have gone down by 8.8 percent as expected because of the slowdown in the Gulf.

• Second impact is through the external market - real economy linkages...

Moreover, Egypt’s export sector was hit by the global economic recession. The global financial crisis had an impact on the large-sized enterprises in key export markets. Two of Egypt’s largest manufacturing sectors are ready-made garments, which make up large exports to the US and the EU, and the food industry, which has markets in the EU and the Arab region. Reductions could be expected in exports in these markets in both volume and value.

In the real economy, the effects of the global crisis have not been captured yet, because of lag in the availability of data. However, a slowdown in the real economy is to be expected through the linkage channels to exports and foreign direct investment. Because less foreign direct investment is flowing to Egypt, private investments in infrastructure and real estate projects are reported to have declined. Investment is also expected to decline in export related industries as external demand diminishes and exports fall, jeopardizing real incomes and domestic consumption and investment, the two pillars of strong economic performance since 2004.

Effects of the Global Financial Crisis on the Egyptian Banking Sector:

The impact of the financial crisis has been contained for several reasons:

First, Egypt’s banking system has been able to withstand the recent financial turmoil, reflecting limited direct exposure to structured credit products and low levels of financial integration. Secondly, the Central Bank of Egypt (CBE) adopted a reform plan for the banking sector during the period (2004 – 2008) which encouraged mergers among small entities to create strong banking institutions. The reform plan also included bank financial and administrative restructuring and clearing portfolios from bad debts. Banking system reforms, including a strengthening of bank supervision, restructuring and consolidation, and a cleanup of non-performing loans (NPLs), have contributed to its resilience. On the other hand, the CBE stipulates that mortgage finance activities should not be more than 5 percent of bank’s loan portfolios 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 10 percent of its deposits at offshore banks in order to avoid bankruptcy dangers. Moreover, the CBE sets some risk management regulations concerning the basics of credit risk management and assignment of reserves for real estate loans, consuming loans and contingencies.

Also, liquidity is quite excellent, as the credit ratio is about 52 percent of liquidity available at the Egyptian banking system. Finally, the financial position of Egyptian banks is strong, estimated at LE 74 billions in 2008 against LE 37 billions in 2004. Information through end-September 2008 shows net foreign assets positions of banks and the deposit base have been stable, and the flow of credit to the private sector has continued to grow at the 14 percent annual rate of the previous three years. Nevertheless, to encourage continued confidence in the banking system, the central bank announced in October 2008 that all bank deposits were fully guaranteed.

However, at the outbreak of the crisis, there were some repercussions on the Egyptian banking system for some reasons:

• The increase in demand of foreign investors to liquidate their assets in the Egyptian Stock Market and transfer them abroad.
• The decrease in shares value of the Egyptian banks registered in the Egyptian Stock market or other world stock markets.
• The decrease in shares value of the Egyptian companies registered in the Egyptian Stock market in which the Egyptian banks have substantial shares.
• The decrease of bank investments in securities which were bought for trading.
• Some branches of Arab and foreign banks in Egypt face some problems due to the losses incurred by their headquarters, such as Piraeus Bank - Egypt and Bank Audi-Sal, Audi Saradar Group.

• The credit portfolios were seriously affected because of the advances given to customers against securities which witnessed great losses in their prices.

Then the CBE decreases the interest rate:

It is well known that Egypt previously adopted a restrictive monetary policy in order to keep its inflation rate at its minimum. However, in the second week of February 2009, the CBE decreased the interest rate for the first time since April 2006. The interest rate on deposits, therefore, decreased by a whole one percentage to 10.5 percent as well as the lending rate with the same percentage to 12.5 percent. This decision is expected to encourage the Egyptian economy for many reasons:

• As the GOE is preparing to decrease the inflation rate by June 2009, then the real interest rate in Egypt will be positive for the first time since a long period, encouraging savers to deposit their money in banks.

• The global financial crisis has a grave impact on the world economy, which witnessed a severe recession for the first time since decades. The Egyptian economy, consequently, will be affected, especially the sectors related to exports. The local investors then lose great opportunities in international markets. The GOE sought to compensate this trend, so the CBE took this decision which would encourage producers to invest inward.

• This decrease will not lead to dollarization, i.e. convert deposits in the Egyptian pound into the US dollars. This expectation is considered to be right as the interest rate on all currencies, including the US dollar, witnessed continual decreases during the last period.

Box (I.1.2): GOE Sets a Five Pillared-Plan to Face the Global Financial Crisis

The GOE has set a plan with five pillars to face the global financial turmoil and its repercussions on tourism, exports, FDI, Suez Canal receipts and workers remittances. The GOE expects reductions in returns from these sources during the current crisis. In dealing with the crisis, the GOE concentrates on developing the domestic economy to overcome the negative effects. In the coming period, the GOE will depend more on the local market, will increase Government spending on investments in infrastructure and services, and will utilize the national savings in financing SMEs.

The first pillar: To make up for the expected slowdown in the real economy, the Minister of Finance has prepared a fiscal stimulus package for 2008/2009. The Ministry of Finance announced a recovery package whereby it will pump LE 15 billion in infrastructure projects. The projects are expected to employ more labor and materials, thus enhancing demand and making up for the shortfall in private investment. LE 15 billion will be pumped into infrastructure projects as a preemptive measure, offering new work opportunities and boosting domestic demand.

The second pillar concerned with facing the crisis repercussions on unemployment. This includes setting a social program to encourage companies to keep their labor. This also includes adopting a program to attract about LE 66 billion in agricultural and industrial investments to establish 474 foodstuff factory and 785 logistic centers. The projects will be extended on 1.3 million acre and are expected to provide 750 thousand new job opportunities.

The third pillar is the best utilization of national savings. This includes the best utilization of liquidity available at public banks and other local finance sources. Given that the lending ratio is still only 54 percent of deposit ratio at these sources, which provides a flexible space to increase a more efficient utilization.

Developing domestic trade is the core of the fourth pillar. The GOE is reviewing 12 legislations concerning domestic trade regulations, domestic trade infrastructure improvement, and building an integrated and modern information base for domestic trade.

The last pillar is concerned with attracting Arab oil surplus money to pump investments in Egypt. This aims to execute projects that are worth $10 billion.
The decrease in interest rates might flourish the Egyptian Stock Market after its losses since last October. The interest decrease will make savers search for more profitable opportunities for their money. The Stock Exchange will be a secure resort for this purpose.

The decrease in interest rate has its fruitful effects on decreasing the burden of Government indebtedness to the banking system. It also will offer a suitable opportunity for the GOE if it needs to borrow from the banking system to finalize its LE15 billions stimulus plan to be spent on infrastructure projects.

The continued growth gained during the period 2004/2005 – 2007/2008 had its positive effect on growth and employment. A growth rate of 4.7 percent should still absorb the growth in the labor force. The strength of the domestic economy of the past years will give the Egyptian economy the resilience it needs to weather the consequences of the financial crisis on the real economy. The fiscal stimulus package proposed by the Ministry of Finance and passed recently by Parliament should help pre-empt the expected slowdown and support employment generation. Accelerating public infrastructure spending would strengthen the infrastructure base and help raise potential output.

Supported by the economic successes in fiscal years 2007/2008, and 2006/2007, the economy reinstated its resilience in the financial crisis and grew by 4.7 along the fiscal year 2008/2009 (Figure 1.1.a).

Despite the slowdown of the economic growth rate it is still considered one of the strongest growth rates, given that the IMF’s 2009 WEO update has lowered the growth projections of all world economies to between negative and zero. Egypt is expected to gain the third strongest growth rate in MENA region; after Qatar with its huge oil exports, and Iraq which is implementing a major reconstruction process.

External demand has played a crucial role in bolstering the economy.

It contributed 2.07 percent, 4.18 percent and 3.93 percent for the years 2002/2003, 2003/2004, 2004/2005 respectively. The external demand impulse, sustained since 2002/2003, had a spill-over effect on domestic demand over these years. The GOE realizing the negative impact of the recent developments in the global economy on the external demand, It is set to counter effect this impact by the increased spending on the public side (Figure I.2.). A reduction in real imports due to decrease in real GDP has led to a balance in contribution of Net Exports and Domestic Demand to growth.
Growth since 2004/2005 has been driven by revived domestic demand.

It is expected that this trend will remain to persist and the domestic demand driven by the newly approved public spending and public investment, and will help smooth the external shock effect (Figure I.3).

The Government implemented a number of important fiscal measures that helped strengthen domestic demand. September 2004 saw significant tariff reductions that were followed by a second round of cuts in December 2004. Other measures include ongoing customs reforms and a new tax code that was passed in June 2005. The new law reduced personal and corporate taxes by 50 percent. These cuts that took effect in July 2005 not only served to raise disposable income since 2005/2006, but also reinstated market confidence in the economy, which helped boost investment demand. As a result, domestic economy saw a healthy expansion, as private consumption and investments increased significantly. In fiscal year 2008/2009, Domestic Demand contributed 2 percent to growth of real GDP.

The Egyptian economy’s growth rate peaked to 7.1 percent in 2007/2008. Trade and tax reforms, led to an average rate of growth of 6.7 percent over the past four fiscal years (2004/2005 – 2007/2008). However, growth is expected to slowdown in the face of the global recessionary pressures brought about by the world financial crisis. Data available for the period April-June 2008/2009 show a GDP growth rate 4.5 percent, still a high rate compared with the world rates during the same period (Figure I.1.b).

Domestic demand was largely driven by consumption demand; however during the fiscal years 2006/2007 and 2007/2008 the contribution of investment demand significantly strengthened and picked up with the contribution of consumption. Data of fiscal year 2008/2009 reveal a downward trend in investment due to the impact of the financial crisis on capital inflows and foreign direct investment.

The growth in consumption demand is expected to trigger a secondary effect. In fiscal year 2007/2008, investment contribution to growth in domestic demand picked up with contribution of consumption demand to domestic demand growth. In absolute terms, investment undertaken during the fiscal year 2008/2009 has amounted to LE163 billions, representing 19.5 percent of GDP.

The revealed downturn trend in investment is caused by the impact of the financial crisis on capital inflows and foreign direct investment will be partly compensated by the expansionary fiscal stimulus package for 2008/2009 that the Ministry of Finance has put together and was approved by Parliament.

Foreign Direct Investment (FDI) has grown exponentially over the past few years. According to the World Bank’s Doing Business Report 2009, Egypt is among the first ten countries, for the third time, in implementing reforms concerning Government regulations that lured foreign direct business activities. This year also, Egypt still leads reformers in the MENA region. In 2008, Egypt came on top of the list of world reformers, making it much easier to attract foreign business. However, because of the global recessionary environment, the Egyptian economy received a moderate FDI inflow amounting to US$8.1 billions in June 2009 compared to US$13.2 billions in June 2008.

The macro-economy was more favorable to private sector led growth since 2004/2005. As a result, private sector growth continued to dominate the uptake in consumption demand. Data for 2008/2009 reveal the increased share of public spending that was effected as a fiscal stimulus.
Although private sector growth was negatively affected by the economic slowdown during the early years of the millennium, the acceleration of consumption demand since 2002/2003 which has carried into 2007/2008 is owed mainly to a stronger private sector. Thus in real terms, total consumption is largely driven by private consumption demand (Figure 1.4; Appendix B-Table 1.3.b).

_**In order to keep encouraging the private sector, the Government is implementing many measures aiming to support SMEs in order to keep production and consumption at their highest levels ...**_

According to Egypt’s census in 2006, Egypt has 2.4 millions SMEs, with less than 10 workers, which employ 5.2 millions workers and another 39 thousand SMEs, with between 10-50 workers. SMEs account for more than 80 percent of employment in Egypt’s non-agricultural private sector, including both formal and informal. SMEs, therefore, are crucial to Egypt’s prospects for growth and development, and the welfare of not just the very poor but also the average citizen.

The global financial crisis is likely to transform the SMEs sector to be a refuge for those who will be unemployed from the larger formal sector enterprises, meaning those who lose jobs as a result of the global recession. The SMEs cater more to local consumers, so they are more protected from the slowdown and can prove more resilient as domestic demand remains strong. In the short-term, it is imperative that SMEs have access to credit and all of the non-financial services that help enhance productivity and market access. It will also be important to promote SME access to ICT in an effort to better inform small entrepreneurs of market challenges and opportunities.

A special tax treatment was offered by the Ministry of Finance to SMEs financed through the Social Development Fund. MOF adopted a strategy to promote and strengthen a favorable environment for SMEs eight years ago. The initiative took the form of a project targeting small and medium and micro enterprise policy development.

...and the GOE is supporting the private sector role in society through numerous initiatives, among which is the MOF’s newly born PPP initiative.

The private sector clearly needs to be pushed towards greater formalization, i.e. to provide greater social security and job stability by becoming more formal. This has already happened with a labor law that was passed in 2004, so there are incentives for them to provide formal employment. The private sector in Egypt is also being promoted as the state could not become again the employer of first and last resort. People have accepted the idea that it is the private sector that is going to provide the main engine of employment growth. However, how to get the private sector to provide good jobs will depend on the regulatory framework.

In 2006, the Government of Egypt adopted a new long-term policy of pursuing partnerships with the private sector to expand and increase the country’s infrastructure investments.

In line with the economic reform agenda and strategy to increase private sector involvement in public social infrastructure services by leveraging private spending against public spending, the GOE has taken the initiative to introduce a Public Private Partnerships (PPP) policy and program through the establishment of the PPP Central Unit within the Ministry of Finance.

As the public face of PPP in Egypt, the PPP Central Unit acts as the PPP center for support and expertise, identifies pilot projects together with responsible Line Ministries, sets national guidelines for implementation, standardizes PPP contracts, provides technical/advisory support to infrastructure Line Ministries and monitors the implementation of PPP projects.

**Brief on PPP’s pilot projects:**

- New Cairo Wastewater Treatment Plant: The New Cairo Wastewater Treatment Plant PPP Project is one of the key PPP pilot projects whereby the Ministry of Housing, Utilities and Urban Development (“MHUUD”) through New Urban Communities Authority (NUCA) with the technical assistance of the PPP Central Unit has invited private sector participation, through a competitive bidding process to enter into PPPs for the design, construction, financing, operation and management of a new Wastewater Treatment Plant with a total capacity of 250,000m³/day to treat wastewater within New Cairo City, Madinaty and El Mostakbal with the objective of implementing a model of PPP transaction in the urban services area which can then be replicated in other projects of the wastewater sector. The Project has been awarded to Orasquila (Orascon Construction Industries, Aqualia and Aqualia Infrastractions), Contract signed June 2009, and the Financial Closure is expected on December 2009.
Two New Public University Hospitals & a Blood Bank in Alexandria: The new University Hospitals PPP Project is one of the key PPP Pilot projects whereby the Ministry of Higher Education, represented by Alexandria University, with the technical assistance of PPP Central Unit has invited the private sector participation through a competitive bidding process to enter into PPPs for the financing, designing, constructing, equipping, furnishing, maintenance, operating and provision of non-clinical facility services for two University Hospitals & a Blood Bank through PPP Contract, to be tendered in two lots whereby each of the qualified Bidders is entitled to submit its bid for one or both lots as follows:

1. Smouha Maternity University Hospital and a Blood Bank; a 200 bed hospital and a blood bank in the same hospital building with a separate entrance which will be located at the Smouha Hospital Complex.

2. Mowassat Specialized University Hospital; a 224 bed with Centers of Excellence (COE) for the provision of highly specialized services in Neurosurgery and Urology/Nephrology (including kidney transplants). The hospital will be located in the same site adjacent to the old Mowassat Hospital.

It is scheduled to hold one to one separate meetings with qualified bidders to respond to their questions & provide the necessary clarifications during January 2010, it is also expected that qualified bidders submit their technical & financial bids in May 2010 after which the winning bidder will be announced during August 2010.

From a sectoral perspective, that most of the GDP growth has been driven by the private sector.

Private sector growth is the key to enhancing the growth momentum. Macroeconomic stability will continue to nurture the private sector as an engine for growth. Recent tax and trade reforms, and continued reforms to reduce red tape and bureaucratic constraints are all serving to increase the contribution of the private sector to the economic recovery.

Between 2003/2004 and 2007/2008, the private sector has contributed around two thirds of the GDP growth rate. (Table I.1.2) Main engines of growth in the five years were from manufacturing, wholesale and retail, agriculture, construction and building and communication, amounting to three quarters of the contribution of the private sector. The remaining momentum came from extractions, restaurants and hotels and real estate activities.

Data available for the fiscal year 2008/2009 confirm a 3.31 percent growth in the private sector activities versus 1.35 percent growth in the public sector activities. The same sectors, manufacturing, wholesale and retail, agriculture, construction and building and communication, led the private sector’s contribution to growth.

The textiles sector in particular remains one of the driving forces of the exportable industry. The QIZ agreement signed December 2004 with the United States gives Egyptian textiles manufacturers tariff free access to the US market. Data for 2006 reveal that QIZ cumulative exports rose by 221 percent above the 2005 level and by 74.4 percent in 2007. (Source: Ministry of Trade and Industry)

Egypt also has a robust pharmaceuticals industry. In addition, food processing has always been a driver of Egypt’s manufacturing sector. More recently, Egypt has changed from a net importer of fertilizer products to a net exporter. The fertilizer industry employs some 34 percent of the labor force.

Special economic zones, another vehicle to provide competitive advantages to manufacturing firms, have served to increase manufacturing in fertilizers, iron and steel, pharmaceuticals, building materials and petrochemicals, which all heavily depend on gas for energy. Currently there are two special zones: North West Suez and East Port Said. Continuing reforms that boost private growth and employment will be the key to sustaining the strong growth momentum.

<table>
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<tr>
<th>Table I.1.2 Annual Private and Public Sectors Contributions to Real GDP Growth for 2007/2008 and 2008/2009</th>
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<tr>
<td>Agriculture, Woodlands &amp; Hunting</td>
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<td>Extractions</td>
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<td>Manufacturing Industries</td>
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<td>Construction &amp; Buildings</td>
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<td>Transportation &amp; Communication</td>
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<td>Suez Canal</td>
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<td>Whole Sale &amp; Retail</td>
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<td>Financial Intermediaries &amp; Supporting Services</td>
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<td>Education, health, social, cultural, entertain-</td>
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<td>&amp; personal services</td>
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<tr>
<td>Sub-Total of Sectors</td>
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<td>Total Real GDP Growth Rate</td>
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Source: Estimated from Appendix B - Table 1.5.e
Following the global trends, the inflation rate began to decrease reaching 9 percent in August 2009.

While the slowdown in the economy is a concern because of its potential impact on poverty rates, falling inflation rates will increase real incomes. In 2008, the Government’s economic policy was mainly focused on reducing inflation which had reached a peak of 23.6 percent in March 2008, because of the worldwide increase in food and oil prices. The latest figures indicate that with the weakening demand and falling international commodity prices inflation has steadily declined since the last quarter of 2008. In December 2008, inflation reached 18.3 percent and further fell to 9 percent in August 2009.

Annual urban headline inflation rose to 10.7 percent in September 2009, from 9 percent in August 2009, mainly due to higher food prices. Food, recreation and culture and miscellaneous items increased by 17.4 percent, 6.3 percent and 10.2 percent, respectively, from their level in September 2008. The annual change in these items in August 2009 was 13.4 percent, 5.7 percent and 9.6 percent. On a monthly basis, prices of items in the food and beverages and recreation and culture items increased by 3.7 percent and 0.7 percent, compared to an increase of 3.1 percent in food prices in August 2009, as increased consumption in the summer and Ramadan led to higher food prices.

The increase in inflation in September, confirming a higher resistance of inflation and implying a higher volatility in food prices. Detailed data on the breakdown of food items’ prices showed a higher rise in the prices of grains, dairy products, vegetables, meat and fish and sugar products. Problems between farmers and milk producers since the beginning of the year had been helping fuel food inflation, as did the recent rise in international sugar prices. Changes in the prices of vegetables, fruits and proteins have been more responsive to seasonal changes related to increased demand and one-off factors like the avian flu. International commodity prices have been recovering, rising throughout 2009, applying pressure to local prices of imported items. Fluctuations in the prices of locally-produced fruits and vegetables also fuelled food inflation.

In the meantime, the pound has continued to stabilize...

After the announcement of a free float in January 2003, both the nominal and real effective exchange rates fell significantly, reflecting a real depreciation of the pound, and increased competitiveness (Table 1.1; Figure I.6).

... in response to a number of factors, three key ingredients were:

The establishment of an interbank market...

The launch of a formal and active interbank market for foreign exchange in December 2004 served to create a liquid foreign exchange market and to converge the official and parallel market rates. In addition, confidence in the economy has spurred substantial inflows of private foreign capital that supported the accumulation of reserves and the repayment of external debt. The real effective exchange rate has thus shown signs of appreciation since December 2004 (Figure I.6)

... The elimination of surrender requirements...

The Prime Minister issued Decree No. 2059/2004 rescinding Decree No. 506/2003 that required exporters to surrender 75 percent of their foreign exchange proceeds. This step helped enhance the liquidity of the 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.
**... and the adoption of a credible and transparent monetary policy**

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**... and the adoption of a credible and transparent monetary policy**

A Monetary Policy Committee, established in 2003 is in charge of putting in place a credible and clarified monetary policy whose primary objective is price stability. Towards this end, the Central Bank is committed to maintaining a market determined exchange rate system. In addition, open market operations (OMOs) and a corridor for the overnight interbank rate have been established. The introduction of OMOs is a pre-requisite for the Central Bank to adopt inflation targeting as planned. The CBE is also working on upgrading its technical capabilities. All these factors worked against the positive impact of tariff cuts implemented in September 2004 on inflation.

**Egypt’s external debt position continues to be strong ...**

![Graph showing Egypt's external debt position](image)

Egypt’s total external debt in terms of net present value has declined from US$29.9 billions in 1990/1991 to US$22.8 billions in March 2009. Its maturity structure is favorable, with short term debt constituting 8.07 percent of total external debt (Figure 1.26; Appendix B - Table 4.2). As a percentage of GDP, foreign debt stood at 17 percent in June 2009 compared to 20.1 percent in June 2008. Debt service, as a percent of current account receipts and of exports of goods and services, is 5.3 percent and 6.2 percent respectively in June 2009, up from 3.9 percent and 4.6 percent a year earlier (Table 1.1).

**... and the fiscal deficit is expected to widen for a short period in order to provide for the fiscal stimulus ...**

![Graph showing annual overall fiscal deficit and cash deficit](image)

In 2005, the Ministry of Finance reclassified Government according to the IMF 2001 GFS classification standard (modified to cash principles), in line with international best practices. The re-classification resulted in higher restatements of the budget deficits starting 2001/2002, and illustrates the Government’s commitment to tackle a tough issue.

In compliance with its medium term fiscal consolidation plan designed to reduce the budget deficit by one percent every year discussed above, the cash budget deficit fell from 9.4 percent of GDP in 2004/2005 to 9.2 percent in 2005/2006 and reached 6.8 percent in 2007/2008. This is despite deep reforms such as implemented income tax and tariff rate cuts, as well as possible sources of pressure in the coming years arising from energy price adjustments, pension reforms and bank restructuring. (Figure 1.8; Appendix A - Table 1.1.a & 1.1.b).

However, the fiscal year 2008/2009 has witnessed a widening budget deficit, 6.7 percent of GDP, due to the expansionary corrective fiscal plan adopted by the Government. Temporary increase in fiscal spending has been front loaded. The Ministry of Finance has accelerated spending on public projects that are already planned and approved within the medium term national plan. A decelerated rhythm will follow when the market absorbs the external shock of the global financial crisis. Thus budget deficit will be the same on average for the medium term. This is a temporary measure that will allow an expansion without setting a permanent problem in the structure of the budget.
Meanwhile, public and Government debts remain manageable.

According to IMF projections, under the baseline scenario (GDP growth rate of 5.6 percent), net public debt would decline after five years to 65 percent of GDP. A more ambitious adjustment path (a sustainable rate of growth of more than 6 percent) would lower debt to 56 percent of GDP by June 2011.

With more reliance on non-inflationary financing since 1999/2000, net budget sector and general government debts have slightly increased. Relative to GDP, net budget sector debt was some 53.5 percent in June 2008 compared to 54.1 percent in June 2009. During the same period, net general Government debt was 42.7 percent of GDP compared to 44.7 percent (Figure I.12).

Egypt’s debt dynamics will benefit from expected strong nominal GDP growth; the resumption of privatization; and the stabilization of the exchange rate. Furthermore, better tax compliance under the new simplified tax system could help improve the fiscal position and public indebtedness.

**Development in Debt Management.**

The UNCTAD has been contracted to supply, install and give license to a debt management and financial analysis system “DMFAS” to retain and process all the data of internal and external indebtedness related to Loan roll-over serviced by The Ministry of Finance. The system will provide a database for the debts and it is in the process of being linked with the database of the Central Bank of Egypt, which would contribute to the standardization of concepts and full compatibility to the data of this debt. This system is aimed to lead to an effective management of Public debt. A full database for domestic and foreign debt has been established.

Debt Management Unit “Minister of Finance’s Office” has succeeded extending the debt maturity to two years. In September 2004, debt maturity was 0.8 years. The Unit has used the policy of issuing long-term treasury bills and Government bonds to avoid the negative effects of fluctuating interest rates on the cost of public debt. The Debt Management Unit has also succeeded in reducing domestic and external debt from 120 percent to 80.6 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.

Prior to the financial crisis, the Ministry of Finance was committed to implementing a medium term fiscal consolidation plan designed to reduce the budget deficit by one percent every year. As a first step the Government introduced an energy subsidy reduction package last July 2006. It has also announced deep reforms in the sales and real estate taxes with a view to widening the tax base and enhancing revenues. The Treasury Single Account Law passed on June 2006 by Parliament (See Appendix D) gave the Ministry of Finance better control over its cash management operations and hence improved debt management.

![Annual Domestic Debt as Percent of GDP](image1)

**FIG. I.12** Source: MOF

![Annual Current Account Balance, Trade Deficit and Net Services as Percent of GDP](image2)

**FIG. I.19** Source: CBE
During fiscal year 2008/2009, Egypt’s external sector is witnessing a challenge as current account deficit reaches 2.4 percent of GDP (Figure I.19).

Higher investment demand associated with the September 2004 reduction in tariffs and the recent recovery in economic growth rates was reflected in a rise in imports 37.8 and 25.8 percent increase in 2007/2008 and 2006/2007 respectively. (Figure I.14) The rise in the current account surplus during the past four years has been driven by a significant improvement in the services balance. The fall in the value of the Egyptian pound has made Egypt an attractive tourist destination.

However, as the impact of the financial crisis began to filtrate the economy, imports decreased by 4.6 percent, non petroleum exports decreased by 5 percent, as well as Suez Canal dues that declined by 8.4 percent during fiscal year 2008/2009 while tourism was mildly affected and declined by 3.1 percent in comparison with 2007/2008. A mild current account deficit resulted from this situation. As mentioned earlier, the Government of Egypt has put into function a proper mechanism to deal with the challenge of the global crisis.

Turning to the stock market, throughout the second half of 2006, the whole of 2007 and until May 2008, the stock market maintained its bullish performance, driven by the continued improvement in the external accounts, trade reforms, tariff reductions, tax cuts, and rapid privatization. The stock market received an extra boost after the renewal of the tenure of the reform-oriented Economic Team for another term in October 2005. However, the market entered a period of correction accompanied by the global financial crisis that pulled its index to decrease since May and until the end of March 2009. Then, the market regained its bullish performance since April 2009 to reach its peak on October 2009.

The CBE continues to build its Net International Reserves (NIR), which stand at US$28.6 billions in June 2007 and reached US$33.51 billions in September 2009. The robust NIR position owes to the increase of Egypt’s competitiveness (Figure I.13, Appendix B - Table 2.8.)
Global Economy Outlook for 2009

The stresses in the financial markets of the United States that first emerged in the summer of 2007 transformed themselves into a full-blown global financial crisis in the fall of 2008: credit markets froze; stock markets crashed; and a sequence of insolvencies threatened the entire international financial system. Massive liquidity injections by central banks and a variety of stop gap measures by Governments proved inadequate to contain the crisis at first.

Markets all over the world have been engulfed in a global economic crisis, with stock markets sharply down and volatile, almost all currencies having depreciated substantially against the dollar, and risk premiums on a wide range of debt having increased by 600 or more basis points. Both private-sector and sovereign interest rate spreads for developing countries have spiked even higher.

Commodity markets too have turned a corner. Following several years of increase, prices have plummeted, and although well above their 1990s levels, they have given up most of the increases of the past 24 months.

Growth prospects for both high-income and developing countries have deteriorated substantially, and the possibility of a global recession cannot be ruled out. Based on the outlook for 2009, the Japanese recession is expected to increase over 3.2 percent, accompanied by price increases of 1.4 percent and unemployment soaring to 4.4 percent. GDP is projected to shrink in 2009 to -0.1 percent. As for the USA, GDP is expected to slow down from 1.4 percent in 2008 to -0.5 percent in 2009.

Reductions in the finance available for firms and consumers, coupled with a slowdown in developing countries’ import demand, have set the stage for a recession in the United States, Europe, and Japan beginning in the second half of 2008 and lasting into 2009. International Monetary Fund director has indicated on several occasions that worldwide recession could cause global economy to contract by as much as 3 percent this year.

Overall global GDP growth is projected to decline to 0.9 percent in 2009, with developing economies expanding by 4.5 percent well below the 7.9 percent growth rate recorded in 2007. International trade decelerated sharply, with global export volumes declining for the first time since 1982. As a result, both commodity prices and inflation have eased, with oil prices averaging about US$75 a barrel in 2009 and food prices declined compared with their average for 2008. Prices in all commodity markets have fallen sharply since July 2008 reflecting revised expectations of slower GDP growth. Because commodity prices reflect forward-looking expectations, the sharp slowing of growth that is expected over the next year has caused prices to decline rapidly even though the underlying supply and demand tensions are little changed from just a few months ago when these prices were close all-time highs.

The main source for the slowdown in both developing and high-income countries will be through investment, which for 2009 is expected to decline 3.1 percent in high-income countries. In developing countries, investment growth is projected to slow sharply to 3.4 percent in 2009 from more than 13 percent in 2007. Developing countries, are facing higher borrowing costs, and lower capital flows, (those countries face a credit shortfall of up to US$700 billions) leading to weaker investment and slower growth in the future.

Low-income countries will also be affected by the slowdown mainly through indirect mechanisms, including slower global growth, lower commodity prices, slackening remittance receipts, and partial scale back in aid flows as a result of stimulus packages for the major economic powers that will limit money available for their assistance. The crisis is threatening to unravel Africa’s economic and social success over the last decade and millions of people are prone to be thrown back into poverty.

On the more positive side that is emerging after fiscal and other interventions by Governments, although full recovery will take time, it is expected that an economic revival is a great potential. In the USA, some Government efforts are already paying off, seen in lower mortgage rates, stable money-market funds and more business lending. Another bright spot in the gloomy picture is the Chinese economy. China’s contribution as being very positive in keeping many markets from going down as far as they would otherwise.

Policy Challenges For Egypt

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. 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.
## 2. Status of Recent Economic Legislation

### ENACTED LAWS

1. Financial Leasing Law No. 95/1995, amended by Law No. 16/2001
2. Central Depository Law No. 93/2000
3. Money Laundering Law No. 80/2002
4. Special Economic Zones Law No. 83/2002
5. Civil Association and Establishments Law No. 84/2002
8. Central Bank, the Banking System and Monetary Law No. 88/2003
9. Electronic Signature Law No. 15/2004
10. Small and Medium Enterprises Law No. 141/2004
11. Income Tax Law No. 91/2005
12. Competition Law No. 3/2005
14. Real Estate Tax Law No. 196/2008
15. Presidential Decree No. 231 of the year 2004 concerning the organization of the Ministry of Investment
16. Presidential Decree No. 300 of the year 2004 issuing the Customs Tariffs
17. Explanatory Note on Presidential Decree No. 39/2007 Concerning the Issuance of the Customs Tariff

### DRAFT LAWS

1. Draft Law for Regulation of Public Private Partnership "PPP"
3. Overview of Selected Recent Economic Legislation

3.1 The Real Estate Tax Law No. 196 of 2008.

- Law No.196 of 2008 was issued on June 23rd 2008 to introduce a new real estate tax system, which aims to remedy the obstacles and ambiguities that previous real estate laws could not overcome. By replacing previous real estate tax laws, the new Law stipulates a new set of provisions and procedures which creates a transparent and straightforward real estate tax system. The law is composed of six chapters and two schedules which determines the value of the real estate tax.
- The real estate tax shall be imposed on the owner (natural person or legal entity) of the estate or the person entitled to its exploitation or usufruct right.
- The value of the real estate tax shall be determined at 10 percent of the value of the annual rental value of the estate unit. The annual rental value shall be determined by the “Assessment Committee”, in which the law stipulates its formation and competence. The assessment committee shall determine the annual rental value based on the geographical location and level of construction and utilities connected to the unit. The determination of the rental value shall be reevaluated every five years. At the end of the five year period, new rental values shall be determined, provided that the new assessment of the rental value shall not exceed 30 percent of the previous rental value for residential units and 45 percent for non residential units.
- The rental value assessments shall be published in the official journal after ratification by the Minister of Finance. Real estate taxpayers shall be notified of the rental value assessments by a registered letter at their listed address.
- The real estate tax shall be imposed on all real estate located in Egypt, regardless of its function, located underground or overwater, occupied or unoccupied. However the Law has determined certain estates which shall be exempted from the real estate tax.
- Residential units with an annual rental value evaluated at less than six thousand Egyptian pounds shall be exempted from the real estate tax.
- The law grants the taxpayer the right to appeal the annual rental value and has determined the procedures in which the appeal could be submitted.
- Taxpayers whom commit tax invasion according to the provisions of this law shall face a penalty which is not less than one thousand Egyptian Pounds and does not exceed five thousand Pounds, in addition to compensation to the real estate tax authority equal to the amount of the unpaid tax.

3.2 Electronic Signature Law No. 15 of 2004.

- The Electronic Signature Law No.15 of 2004 was issued on April 21st 2004. The Law was issued with the objective of promoting the industry of information technology and communication and is composed of 29 Articles.
- The Law grants the electronic signature and electronic documents in commercial, civil and administrative transactions, the same status of the signatures stipulated in the evidence provisions of the Civil and Commercial Laws, provided that the electronic signature or document has fulfilled the required conditions stipulated by the Law.
- As a step by the Government to facilitate electronic transactions and information transfer, the “Information Technology Industry Development Agency” was established by virtue of the Law, affiliated with the Ministry of Communications and Information Technology. The Agency is the competent authority for issuing licenses necessary for electronic signature and electronic services, as well as determining the regulatory standards and technical specifications of the electronic signature.
- Any fraud or violation to the provisions of the Law shall be penalized by a fine which is not less than Ten Thousand Egyptian Pounds and does not exceed One Hundred Thousand Pounds.
3.3 Explanatory Note on Presidential Decree No. 39/2007 Concerning the Issuance of the Customs Tariff

Presidential decree No. 300/2004 and its amendments concerning the Customs tariff were issued in 2004. The tariff reductions that came into force then were largely driven by national and international changes the Egyptian economy had experienced at the time. The Egyptian Government’s long term development plan since 2004 has been to create an investor friendly environment that is increasingly led by the private sector and that provides rapid job growth. In this context, a new Customs tariff issued by Presidential Decree No. 39/2007 has made amendments deemed necessary to achieve the Government’s economic objectives in a changing environment.

The main objectives of the amendments were as follows:

- To simplify the structure of tariff rates with a view to reducing distortions in tariff rates and facilitating their implementation by all concerned parties. This objective is achieved through the following reductions:
  a. 12 percent down to 10 percent;
  b. 22 percent down to 20 percent;
  c. 32 percent down to 30 percent;
  d. 40 percent down to 30 percent (with the exception of bands included in Chapter 87).

- To achieve a balance between tariffs imposed on manufactured products, intermediate goods and raw materials, that are used entirely or in part in the production of final goods, while taking into consideration the contradictory goals of supporting the national industry, reducing the burden on the Egyptian people, and supporting the various productive activities.

- To comply with Egypt’s commitments to the International Convention on the Harmonized Commodity Description and Coding System, as stipulated by Presidential Decree No. 33/1999, by adopting the HS 2007 issuance as the basis for the Egyptian Customs tariff. This will help facilitate Egypt’s external trade, put Egypt’s statistics at par with international standards, and ultimately serve negotiations on bilateral and multilateral trade agreements.

- To review Article 3 of the Customs Law concerning the collection of Customs taxes due on goods that are subject to temporary admission – whether for repair purposes or for completion of manufacturing activities – in order to ensure sound implementation of the Law.

- Eliminate many of the tariff lines and keep only those strictly necessary in order for the tariff schedule to be at par with international practice.

- Reduce the current tariff rates on selected imports of basic commodities, medications (especially those used for chronic illnesses) and intermediate and capital goods used for production activities.

- Support production activities while creating a fair and competitive environment that does not represent a burden on the Egyptian consumer.

- Develop a partnership with all stakeholders to ensure transparency – a pillar of the international trading system – in the decision making process. The tariff schedule was discussed widely with all concerned parties such as commodity councils, chambers of commerce, the Federation of Egyptian Industries, a number of private and public sector production units, and industrial and investment compounds. The objective was to harmonize all points of view, and to ensure that all stakeholders are partners in the decision making process so as to engage all parties and factors concerned with production and commercial operations.

- Contribute to the creation of a clean environment by applying to selected environmental products a Customs duty of 2 percent of the value of the product. (In cases where a lower tariff rate below 2 percent has been in force, the lower rate applies.) This tax will be applied on stations supplying vehicles with natural gas, on parts needed to transform vehicles to use natural gas, on equipment used to monitor and control various products of environmental concern, and on equipment for renewable and new sources of energy (wind and solar energy) and their spare parts.

The Customs Law No. 66/1963 stipulates in Articles 6 and 9 that the Customs tariff should be issued by a Presidential Decree that has the power of law, on condition that it be submitted to the legislative authority in its current cycle as soon as it becomes effective. If Parliament is in recess, it is to be submitted to the following legislative cycle.
Appendices

3.4 Law No. 143 of 2006 amending Stamp Tax Law No. 111 of the year 1980

- On July 2006, Law No. 143 of the year 2006 was passed by the People’s Assembly. The Law was issued to amend certain articles of the Stamp Tax Law no. 111 of the year 1980. Such amendments reflected an enhancement in the economic activity and investment promotion, an example of such is the elimination of the stamp tax which was imposed on copies of financial instruments such as checks of all types and values, stocks and commercial bills. Stamp Taxes on certain banking operations such as opening of financial credit, loans and debt returns, letters of credit, opening of banking accounts, extraction of banking statements, portfolio collection were also eliminated. An estimated Tax was imposed on credit facilities balances and loans provided by the bank during the financial year by a value of two of a thousand.

- The Law also eliminated Stamp Taxes imposed on company establishment, certain capital increases, and copies of minutes of board and assembly meetings, such eliminations reflect investment promotion. Other abolished Stamp Taxes include taxes which were imposed on Egyptian nationality issuance decrees, Commercial Navigation documents, invoices and clearance vouchers of a value not less than One Pound, invoices of property taxes. Stamp Taxes which were imposed on all kinds of certificates issued from governmental agencies excluding certain educational certificates were eliminated as well.

- The Law requires a percentage to be paid off insurance installments as a Stamp Tax with rates of 1 percent, 10 percent and eighth in a Thousand, where each percentage rate is determined according to the nature of the insurance. The insurer and the insured bear the due Tax equally, where the insurance company bear the tax imposed on the total insurance installments. However such the Tax is not imposed on reinsurance installments.

- Additionally the Law imposes a Stamp Tax on all brand promoting advertisements, equivalent to 15 percent of the advertisement fee or cost. According to the Law, the Advertising agency is to notify the Tax Authority of all circulated advertisements and its cost, as well as the due Stamp Tax. Entities are to pay the due Tax to the competent Tax Authority; however the advertising agency is to levy the due Tax for advertisements created for natural persons and service it to the Tax Authority.

- Another main feature of the new Law is the dispute settlement for all cases filed or pending at courts of different levels prior to the effective date of this Law are to be settled by servicing a percentage of the tax and other disputed due payments according to the following grades;

  ◊ 30 percent of the tax and other disputed due payments of sums amounting to One Hundred Thousand Pounds.
  ◊ 60 percent of the tax and other disputed due payments of sums exceeding the amount of One Hundred Thousand Pounds.
3.4.1 Ministerial Decree No. 525 of 2006 promulgating the Executive Regulation of Law No. 163 of 2006 concerning Stamp Tax Law.

- The Minister of Finance has issued the Executive Regulations of the Stamp Duty Law, as well as other ministerial decrees in relation to the general directives and executives regulations of the respective Law.

- The Executive Regulations includes several articles that aim to promote and enhance confidence between taxpayers and the Tax Administration. Additionally, the regulations seek to augment the supervisory role undertaken by the Ministry of Finance in order to ensure and maintain a balanced relationship between the aforementioned parties.

- With regards to the tax due on bank transactions, businesses and documents, as well as the akin to such, the Executive Regulations have defined such taxable bank bases and types, as follows:

  According to the amendment, all transactions related to the «Uses» and «Resources» of the General Budget of the State, including the transactions related to non-financial assets (investments), must be recorded on cash basis. With this provision, the Budget recording will be in perfect compliance with the international standards.

  ◊ An estimated tax shall be levied on the consolidated balances of loans, credit facilities, inventories in all their forms, including bank obligations, i.e. shares, speculations, interest accruals or any other form of funding.

  ◊ Consolidated balances shall be determined quarterly (referred to hereinafter as the period) according to the total amounts granted to creditors and which are deposited into their own accounts, with the exclusion of such unused amounts that are within the bounds of authorized credit facilities, loans.

  ◊ The consolidated balance shall be determined at the close of each period (on a quarterly basis) and shall be entered into the opening balance of the following period, accompanied by credit facilities, loans and inventories advanced by banks, after the deduction of paybacks settled during the same period of time.

- In the event where credit accounts appears in credit facilitates, loans at the end of each period, such accounts may not be debited from the total consolidated balances, as well as allocations of loans and accrued interests may not be debited from the total consolidated balances.

- The Executive regulation does not impose an estimated stamp tax on interest accruals or marginal revenues which are not added up to the credit facilities, loans for customers and banks. The estimated stamp tax shall fall due only on such debits from credit accounts of creditors and which are listed in their accounts, except those amounts that are not used from the authorized credit limit of credit cards. The estimated stamp duty may not be levied on debit cards or stored-value cards, including smart cards, and more progressive public finance.
3.5 Law No.139 of 2006 amending some of the articles of Law No. 127 of 1981 concerning Governmental Accounting

- On June 17th Law No. 139 of 2006 was approved by the People’s Assembly. Law No. 139 is issued to amend Articles 5, 6 and the first paragraph of article 30 of Law 127 of 1981 concerning Governmental Accounting.

- **Recording on cash basis:**
  According to the amendment, all transactions related to the «Uses» and «Resources» of the General Budget of the State, including the transactions related to non-financial assets (investments), must be recorded on cash basis. With this provision, the Budget recording will be in perfect compliance with the international standards.

- **Treasury Single Account:**
  Law No.139 will introduce another significant improvement to the State Budget. The Law states that a single account must hold all the accounts of:
  ◊ The Ministry of Finance,
  ◊ The administrative body units,
  ◊ Local administration and public service
  ◊ Economic authorities
  ◊ All other accounts of public and governmental agencies already opened.

- The new accounting system develops a more transparent and effective State Budget. Previously, public money was fragmented into:
  ◊ 48,400 accounts within the Central Bank of Egypt
  ◊ 5,000 accounts in other commercial banks

- By the end of December 2005, the cash in these accounts amounted to LE 82.3 billions which represents around 14 percent of GDP.

- The Treasury Single Account will consolidate sub-accounts for each of the above mentioned entities. With this additional remedial step, the Ministry of Finance is heading towards a lower budget deficit and more progressive public finance.
3.6 Law No. 8 of 2005 amending the Customs Exemptions Law No. 186 of 1986

- The provisions of article 4 of law 186 of 1986 regulating customs exemptions, concerning the collection of customs duty at a fixed rate of 5 percent of the value, shall apply to companies and establishments for all their imported machinery, equipment, devices, means of transportation for materials and vehicles (other than private cars) necessary for establishing projects, including investment projects, hotels, tourist establishments, stated in law 1 of 1973.

- The provisions of article 8 of law 186 of 1986 regulating customs exemptions states that machinery, equipment, devices (other than private cars) shall be temporary released to be rented or used within the country at a tax rate of 20 percent of the value for every year or portion of a year that they remain in Egypt. Article 9 paragraph A generally restricts the usage of items that have been exempted or that have a discounted customs tariff or have a fixed tax rate. According to article 4, it is prohibited to use these items within a specified period for any means other than their main purpose, except after paying the applicable customs duties.

- There was a debate concerning the validity of the fixed rate of 5 percent for machinery, equipment, and devices as specified in article 4. Therefore, the matter was reviewed and discussed by the cabinet committee concerned with settling investment disputes and decided the expansion of the previously mentioned category.

- The application of the 20 percent tax rate as stated in article 8 will be a burden on the projects that import machinery, equipment and devices. This could prevent them from importing such equipment despite the need for them.

- In addition, article 9 paragraph A of the same law states the prohibition of usage of these items until paying taxes and fees and prohibition of transferring them to other projects that have similar privileges. According to the decision of the general assembly of the departments of fatwa and issuing legislations in State Council, these projects became deprived from reusing such machinery, equipment and devices despite the fact that these items could be imported and be exempted or have a discounted rate or have the fixed tax rate of 5 percent.

- For all these reasons, the amendments of the previous articles are required to settle any dispute may arise in the projects stated in article 4 who enjoyed the 5 percent tax rate, and to ease the burden on the institutions and establishments that are willing to benefit from article 8. In addition to permitting the transference of the exempted machinery, equipment and devices or enjoyed a discounted customs tariff rate or have a customs duty of 5 percent to other projects that have the same privileges during the period of seizure without forcing them to pay any customs duties.

- Meanwhile, the law includes re-regulating the period of seizure in exempted commodities or have a discounted tariff rate or have a 5 percent fixed duty rate according to its expiry dates and types and following the principle of graduation in setting the customs duty in cases of transferring such commodities during the seizure period.

- The attached law also states the necessity to revise the requirement for commercial and manufacturing samples for the exempted commodities according to article 2 of the mentioned law to inspect whether these commodities shall be exempted or not.
3.7 Law No. 91 of 2005 Concerning the Income Tax

- Less than two months after the appointment of the new Cabinet, Minister of Finance Youssef Boutros-Ghali presented a new income tax law during the annual conference of the National Democratic Party, held in September 2004. The draft law was circulated and discussed by all stakeholders and then sent to Parliament for approval. The Parliament has passed the new law and the President has signed and issued it in the Official Gazette in June 2005.

- The new income tax law makes the Egyptian tax system more transparent for both national and foreign companies looking to invest in Egypt. It cuts personal and corporate income taxes, and unifies tax exemptions and legislations. It introduces a 50 percent reduction in personal and corporate taxes to a maximum rate of 20 percent. It has also restructured income tax brackets into three categories, with tax rates of 10, 15 and 20 percent. Existing tax exemptions for annual earnings of under LE 5,000 would double. Working spouses would benefit from the new law as each of them would be eligible for an exemption of LE 5,000 on wages. Civil servants would get a personal exemption of LE 4,000 annually.

- Additionally, the law grants a general amnesty for taxpayers in all cases before courts the subject of which is the disagreement between the taxpayer and the Tax Authority on the tax estimation, provided that the disagreed tax amount does not exceed LE 10,000. Moreover, the law provides for a settlement process in tax evasion cases or other offences upon request from the concerned person within one year of the entry into force of the law. These provisions are seen essential in order to encourage Egypt’s informal economy to legalize its status.

- The law also provides for phasing out tax exemptions for newly established companies. Companies listed on the Stock Exchange would also lose the tax exempt status of their paid-in capital.

- In addition to rate reductions, the law provides for streamlining tax administration and merge all income tax legislations into one law. The law is intended to encourage the voluntary submission of tax returns by taxpayers, the timely payment of taxes, and greater compliance of citizens who previously evaded taxes whether because of high rates or cumbersome procedures. A key element of the law is the introduction of self-assessment for taxpayers. This places the burden of proof for tax evasion on Tax Authority which will now limit its inquiry to a sample of some 5 to 10 percent of all taxpayers. The elimination of what had been viewed as discretionary assessments aims at regaining the missing trust between taxpayers and the Tax Authority.

- The Ministry anticipates a significant improvement in the cost effectiveness of the Tax Authority and a reduction in costs to enterprises and individuals associated with the payment of taxes. The new system raises revenue from a limited number of tax rates and will therefore substantially reduce administration and compliance cost. Avoidance of numerous taxes that yield limited revenue will also facilitate tax assessment and avoid the impression of excessive taxation. The new law also introduces high deterrent penalties against tax fraud.

- The proposed rate reductions and administrative changes will, in the medium term, stimulate the economy. Higher profits for businesses will encourage faster economic growth, thus expanding the tax base and ultimately increasing tax revenues. This should partially make up for the shortfall in tax revenues, estimated at between LE 3.2-3.5 billions. GDP growth rates should increase by 2-2.5 percent giving rise to at least LE two billions in additional revenues.

- A broad tax base with limited exemptions enables revenue to be raised with relatively low rates. The erosion of the tax base through exemptions requires higher tax rates to make up for the loss in revenue. Higher rates only serve to increase the likelihood of tax evasion. Hence, expected improved tax compliance under the new reforms should also cover a large part of the loss in tax receipts.

- Proceeds from an ambitious privatization program that includes 172 state-owned companies, a public sector bank and the stake of the Government in joint venture banks will also be used to finance the temporary increase in the budget deficit.

- Over the longer term the Government will be building up the administrative capacity of the state to collect taxes. In addition, a plan was set, immediately after the issuance of the law, to create awareness of taxpayers in order to encourage them to take part in the reform. This plan depends to a large extent on press and media campaigns directed to all classes of society.
3.7.1 Minister of Finance decree No. 991 of 2005 promulgating the Executive Regulation of the Income Tax Law

- Article Eighth of the law issuing the income tax law provide that the Minister of Finance shall issue the Executive Regulation for the tax law.

- Accordingly, the Minister issued decree No.991 of the year 2005 promulgating the Executive Regulations of the Income tax law. The Regulation set forth the guide lines and interpretation of tax law articles, and helps in leading the way to the best application of the concepts laid down in the law, by providing the definitions of the principles stipulated in the law and the procedures needed to apply such principles therein.

- The Executive Regulations consist of 146 articles contained in six books.

- Book One speaks about general provisions which deals with the issues of the calculation of the tax period and the conditions needed to approve a change in the tax period. In addition, the cases when the natural person is considered as having permanent residence in Egypt and the actual headquarters of a legal person as well.

- Book two deals with the Income Tax of natural Persons with regard to the following issues:
  - Tax scope and rate,
  - Salaries and the like
  - Commercial and Industrial activity,
  - Exemptions,
  - Revenues of non commercial professions,
  - Real estate revenues

- Taxes on the profits of the legal persons is the subject of Book Three from the regulations. It deals primarily with determining the scope of the tax and the equation of calculating the average capital stock, the average of loans and advances of determining taxable income.

- Book Four set fourth the withholding of tax at source, and the issues of Deduction, Collection, and Tax advance Payments are the subject of Book Five from the regulations. Book Six sets the obligation of Taxpayers and others which includes notifications, bookkeeping tax return ,tax assessment, tax audit and investigations, collection guarantees and finally appeal procedures.

- All articles set forth in the regulations respond totally to the principles of the income tax law, and aims primarily to support the efficient application of the law.