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Egyptian Initiative for Personal Rights
www.eipr.org
Adalah Center for Rights and Freedoms
www.adalaheg.org
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Egypt's Economic Reforms: An Aggressive Infringement On The Rights To An Adequate Standard Of Living, Health And Education.

Summary

1. On 11 November, 2016, the International Monetary Fund (IMF) agreed to a USD 12 billion loan to Egypt. The loan was agreed on the condition that Egypt would implement an economic reform programme intended to restore macroeconomic stability and promote inclusive growth. Nominally, the reforms were intended to correct external imbalances and restore competitiveness, reduce the budget deficit and public debt, boost growth, and create jobs while protecting vulnerable groups.[1] However, the reforms caused serious volatility to the economy. The currency floatation, high interest rates, and soaring inflation drastically reduced the standard of living of millions almost overnight. The cost of government debt rose to become the government's single largest expenditure, severely impacted access to the right to education, health, and work.

2. This report will explore the human rights implications of the IMF loan. After offering a brief background on the loan, the report will explore the loan's economic consequences on Egypt's economy and budget, and situate Egypt's human rights obligations in a constitutional and international context. The report will then demonstrate how those consequences work against the stated goals of the loan to restrict access to the right to health, education, and the right to work.

Background on the IMF loan

3. Beginning in 2017, Egypt began a series of reforms that caused inflation to spike. These reforms included floating the exchange rate, introducing a new VAT law, and removing all fuel subsidies by the end of 2019. The combined effect of these policies was a historical high inflation rate of 36% in July, 2017. The Egyptian pound fell from EGP 9/USD 1 to EGP 18.5/USD 1.

4. The scale of the consequences far outstripped the IMF's forecasting.[2] The Egyptian pound was expected to settle at EGP 14.5/USD 1 and average inflation in consumer prices was expected to peak at 18%, according to public budget statements for FY 2016/2017. This forecasting error caused millions of Egyptians to slip below the poverty line, denying them basic needs. Despite the self-professed success of the reforms, CAPMAS poverty statistics demonstrate that poverty is rising in Egypt:

[1] IMF. November, 2016. IMF Executive Board Approves US$12 billion Extended Arrangement Under the Extended Fund Facility for Egypt.

[2] Hussein, Salma, and Abdelhamid Mekawy. "An Eye on Debt." Eipr.org. October 2017. Accessed February 7, 2019. https://eipr.org/sites/default/files/reports/pdf/an_eye_on_the_debt_.pdf.

26.3% in 2013, the poverty rate at the end of 2017 rose to 27.8%.[3] It is expected to have increased further since.

5. High interest rates produced by the currency float were mismanaged, creating financial consequences that destroyed the average Egyptians' standard of living. Interest payments on government debt increased after the pound devaluation to more than 49% of public expenditure. In other words, the government had to pay its creditors more interest than it had budgeted for, losing funds it could have spent on education, healthcare, or lowering unemployment. Interest on debt is now the government's biggest expenditure, greater than spending on investments, wages, agricultural subsidies, Upper Egypt development, treatment for the poor, provision of medicines, equipment for hospitals and schools, and other important items of social spending.[4]

6. To catch up with the ever-growing debt, the government decided to increase its tax base and revenues. Instead of continuing the now-frozen Capital Gains Tax on stock market transactions and acquisitions, which was both fair and lucrative, the government implemented a highly regressive tax structure by increasing the Value Added Tax (VAT) rate to 14%.[5] While this was viewed by the government as a means to plug the deficit, no consideration was made as to its negative distributional impact on lower income groups, which spend a greater share of their meager incomes on consumption compared to higher income groups. EIPR research shows that low-income groups spend 6.4% of their annual income on VAT, while higher income groups spend only 3.3%.[6]

7. In another example of the devastating impact of the government's monetary policy, the cost of subsidies for government-imported goods such as wheat and oil products had been calculated on the pre-float exchange rate of EGP 9/USD 1. As a result, the cost of imported goods increased exponentially, causing the subsidy bill to exceed the budget's original allocation. Government debt payments nearly doubled, the public

[3] Central Agency for Public Mobilization and Statistics (CAPMAS) (2018), Egypt in Figures 2017. March 2018. At: http://www.capmas.gov.eg/Pages/Publications.aspx?page_id=5104&YearID=23427

[4] Hussein, Salma, and Abdelhamid Mekawy. "An Eye on Debt." Eipr.org. October 2017. Accessed February 7, 2019. https://eipr.org/sites/default/files/reports/pdf/an_eye_on_the_debt_.pdf.

[5] Reuters. "UPDATE 1-Egypt Extends Capital Gains Tax Freeze, Approves Stamp..." Reuters. March 21, 2017. Accessed February 08, 2019. https://www.reuters.com/article/egypt-economy-tax/update-1-egypt-extends-capital-gains-tax-freeze-approves-stamp-duty-on-stocks-idUSL5N1GY6G0.

[6] Diab, Osama. "Kayfa Tanqil Daribat Al-qeema Al-modafa Al-'ib' Al-dareeby Min Al-aghniaa' 'ila Al-foqara' (How the VAT Shifts the Tax Burden from the Rich to the Poor)." Eipr.org. October 16, 2016. Accessed February 7, 2019. https://eipr.org/sites/default/files/reports/pdf/how_vat_tax_burden_from_the_rich_to_the_poor.pdf.

debt increased by 15% due to the float alone, and the cost of energy subsidies increased from EGP 50 billion to EGP 100 billion in only eight months.[7]

8. To give a concrete example of the impact of this crowding out, Egyptians saw a 160% cumulative increase in their electricity bill from 2012 to 2016.[8] The increase is distributed unevenly on middle and low income households: in 2016 alone, poor Egyptians saw an average increase of 47%, middle-income groups 52%, and the highest three income groups 27%.[9]

9. Instead of promoting inclusive growth by expanding employment opportunities, strengthening social safety nets by increasing spending on food subsidies, and protecting vulnerable groups affected by the austerity measures with cash transfers, the economic reforms caused inflation to skyrocket to historical highs, ballooned public debt, and shifted the economic burden onto the shoulders of Egypt's poorest, adversely impacting the people's standard of living.

Constitutional and international legal context

10. The Egyptian government is beholden to both constitutional and international human rights legal obligations to provide access to health, education, and the right to work. The International Covenant on Economic Social and Cultural Rights, to which Egypt acceded in 1982, recognises the right to work (Art. 6-7), social security (Art. 9), standard of living (Art. 11), health (Art. 12), and education (Art. 13, 19-21). Additionally, while not legal or binding, the Sustainable Development Goals make reference to the right to education (SDG goal 4), health (SDG goal 3), and providing citizens with decent work (SDG goal 8).

11. The 2014 Egyptian Constitution recognises the right to education (Art. 19), healthcare (Art. 18), work (Art. 12-14), and a decent standard of living (Art. 8,17, 27), even going as far as mandating minimum education and healthcare spending as percentages of GDP. Both percentages are mandated to rise to reach international averages. These allocations should have been implemented during FY2017/2018. In fact, spending on both health and education hit historical lows, driving Egypt away from the SDG objectives and from fulfilling its constitutional commitments. The main reason of this failure is the crowding-out effect of the debt payments discussed above.

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[7] Ministry of Finance, 2018. A statement by the minister of finance on the amount of energy subsidies. Available in Arabic. http://www.mof.gov.eg/Arabic/MOFNews/Media/Pages/release16-6-2018.aspx

[8] Diab, Osama. "Kayfa Tanqil Daribat Al-qeema Al-modafa Al-'ib' Al-dareeby Min Al-aghniaa' 'ila Al-foqara' (How the VAT shifts the tax burden from the rich to the poor)." Eipr.org. October 16, 2016. Accessed February 7, 2019. https://eipr.org/sites/default/files/reports/pdf/how_vat_tax_burden_from_the_rich_to_the_poor.pdf.

[9] EIPR & 10 Tooba, 2017. Electricity Facts 2016.

Restricting access to the right to health, education, and work

12. Egypt scores poorly on the World Bank's Human Capital Index (HCI), compared to both the MENA region and to the world's averages.[10] Despite this low performance, public spending on education is shrinking in real terms and is declining as a percentage of GDP. Ministry of Finance (MOF) figures show that in FY2017/2018, education spending was 2.6% of GDP, instead of the minimum constitutional spending of 6% (4 % for K-12 and 2% for higher education). K-12 spending alone declined from 1.6% in FY2017/2018 to 1.4% in FY2018/2019, widening an already large financing gap from EGP 106.9 billion to EGP 136.8 billion and demonstrating that as the economy grows, education spending shrinks in real terms.

13. The same phenomena applies to healthcare spending. The 2018 Universal Healthcare Act was a long-awaited positive step towards realizing the right to health. However, to apply the law, government needs to step up healthcare budget allocations. Spending on health has significantly decreased in real terms. MOF data show in FY2017/2018, healthcare spending was 1.4% of GDP, half the constitutional minimum of 3% and very far from the international average of 5.8%. This situation drives up the out-of-pocket expenses to 70% of total expenditure of health, meaning the government only covers 30% of healthcare spending. This is reflected in the wide gap of expenditure on health between the top income decile and the bottom income decile: the top income decile spends 40 times what the bottom decile spends on primary healthcare, according to CAPMAS data.[11]

14. Unemployment is one of Egypt's largest and most pressing issues. Around 60% of Egyptians are of working age and around 700,000 people join them each year (IMF, 2018).[12] 3.5 million Egyptians are expected to join the labor market in the coming five years. From 2000 to 2010, Egyptians suffered a 10% unemployment rate.[13] Then unemployment peaked at 13.4%. Despite its increased momentum in FY2017/2018, Egypt's economic growth remains unable to integrate Egyptians into the labor market. This was the main development goal Egypt committed to, along with other recommendations from the second UPR cycle in 2014.

15. While FY2017/2018 saw some economic growth, this growth is unable to support meaningful reduction of the unemployment rate because it occurs most in volatile

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[10] Human Capital Index and Components, 2018, The World Bank, Accessed March 19, 2019. https://www.worldbank.org/en/data/interactive/2018/10/18/human-capital-index-and-components-2018

[11] Booklet of the most important income, expenditure and consumption indicators, 2015. Central Agency for Public Mobilization and Statistic. Accessed March 19, 2019.

[12] IMF. Jan, 2018. Arab Republic of Egypt : 2017 Article IV Consultation, Second Review Under the Extended Arrangement Under the Extended Fund Facility, and Request for Modification of Performance Criteria-Press Release; Staff Report; and Statement by the Executive Director for the Arab Republic of Egypt.

[13] Hussein, Salma, and Abdelhamid Mekawy. "Eye on Debt III" Eipr.org. October 2018. Accessed February 8, 2019. https://eipr.org/sites/default/files/reports/pdf/eye_on_debt_iii.pdf

sectors: extraction followed by tourism, construction, and the Suez Canal. These sectors depend on external conditions, are capital intensive, or only provide seasonal employment. Additionally, foreign direct investment (FDI) – around 75% of which goes to extraction or real estate – does little to improve the situation. The distribution of growth helps explain why, despite investment, unemployment rates dropped only slightly, from 12.6% in September 2016 to 11.9% in September 2017.

16. Further impacting access to the right to work, the government began cutting the wage bill in early FY2016/2017 as a response to growing debt. It fell to 6.6% of GDP at the end of FY2016/2017, down from 7.9 percent in FY2015/2016; it is expected to fall to 5.6 percent of GDP by 2018/19. Reduced expenditure on wages avoids harming those who take the lion's share of the budget items and imposes austerity on smaller beneficiaries, in this case, public wage earners. This unfair and unsustainable policy further impoverishes lower income groups while also eroding their purchasing power, impacting not just their right to work, but their right to a decent standard of living. Whether it is tax policy, lifting subsidies on fuel and electricity, or increasing the price of public services, the policies pursued by the Egyptian government makes no distinctions on income or wealth and hit more vulnerable groups hardest.[14]

17. Additionally, one of the main goals of the reforms is boosting female participation in the workforce and increasing their share of employment. However, 1Q2018 CAPMAS data shows that women comprise 20% of the workforce, the same share since the program started in 2016. This is especially concerning because the workforce increased by 129,000 people 1Q2018, 81% of whom were male. It seems that little has been done to encourage specifically female workforce participation and, as a result, this stagnation is likely to continue.

Recommendations

18. Design investment incentives to encourage capital flows to the manufacturing, technology, and agriculture sectors. These sectors are labour-intensive and provide stable and long-term employment. Take other necessary measures to reduce unemployment, especially among young people, by – among other things – increasing public investments in productive sectors, as well as encouraging private sector growth in labour intensive sectors.

19. Review the tax incentives regime and institute fair and progressive taxation with limited and well-targeted exceptions. Stop the rampant tax avoidance on corporate profits, wealth and income in order to include business enterprises and the private sector in the process of comprehensive development. Enact the suspended Capital Gains Tax on stock market profits.

[14] Hussein, Salma, and Abdelhamid Mekawy. "An Eye on Debt." Eipr.org. October 2017. Accessed February 7, 2019. https://eipr.org/sites/default/files/reports/pdf/an_eye_on_the_debt_.pdf

20. Apply a national minimum wage to fulfill the right to an adequate standard of **living**. A minimum wage can also promote inclusive growth and boost aggregate demand. Additionally, better pay may encourage more women to join the labour market.

21. Reschedule public debt and reduce the interest payment bill to allow for the fiscal space needed to meet the constitutional minimum public spending on both education and health.

22. Increase public spending on health and education to meet constitutional commitments and international human rights obligations.