

EGYPTIAN INITIATIVE FOR PERSONAL RIGHTS



المبادرة المصرية للحقوق الشخصية

**Fiscal Statement of the State's Public Budget for the Fiscal Year 2014/2015**

**Austerity Measures and a Rush to Counteract a Crisis at the Expense of Social Justice.**

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## **Introduction:**

The state's public budget in Egypt suffers from fundamental problems related to transparency in terms of its structure, preparation, and implementation. In terms of its structure, the budget is made up of items which are not linked to measurable objectives, thus rendering it difficult to assess the costs of these items in terms of the outputs of expenditures. The budget further contains many items for which it is impossible to follow the actual spending going to them even when final fiscal statements are issued. In terms of its preparation, the budget is essentially drafted by the executive bodies in the absence of public participation. Indeed, the budget is prepared through negotiations between the various ministries over the allocation of money, rather than by society according to the basic needs it identifies and spending priorities ranked accordingly. The result is a seriously flawed concept of spending priorities which does not correspond to the actual needs of different local communities and which, consequently, will not be effective in solving the problems facing society. This is particularly problematic due to the current total absence of any effective tools to increase society's ability to evaluate this effectiveness after the money allocated by the budget has been spent.

The fiscal statement on the state budget for FY2014/2015 is laden with problems related to transparency, some of which have been inherited from the past and some of which stem from the circumstances in which this budget has been issued. Indeed, the budget was issued in the total absence of a parliament or any other mechanism for public oversight and participation, despite the budget's inclusion of measures which carry the most serious repercussions for the Egyptian economy seen in decades.

The fiscal statement on the state budget for FY2014/2015, along with the measures that accompany it in terms of taxes and ending subsidies, comes as a hasty reaction by the government to tackle the growing budget deficit. According to the fiscal statement, the structural deficit as a percentage of GDP could have grown to 15.8% by the end of FY2013/2014 if it were not for a number of cash and in-kind grants.<sup>2</sup> The availability of these grants kept this percentage to 12% as of the end of FY2013/2014, yet this deficit was reflected in the rise of public debt as a percentage of GDP to 93.6% by the end of FY2013/2014.

The fiscal statement specifies targeting an increase in the real growth rate from 2.2% in FY2013/2014 to 3.2% in FY2014/2015 – despite predictions of increased inflation – in order to increase employment rates and recover from the current recession. In addition, the fiscal statement also specifies targeting a reduction in the budget deficit as a percentage of GDP in FY2014/2015, such that it does not exceed 10%. This is lower than the estimates included in the initial draft of the budget, presented late last May, which targeted a deficit equal to 12% of GDP. Thus, the value of the deficit was reduced from about 288 billion EGP in the initial draft budget to not more than 240 billion EGP in the final budget for FY2014/2015.

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<sup>2</sup> Calculated by deducting the impact of any non-recurring expenditures.

Maintaining the deficit at or below 10% of GDP was the central focus of the fiscal statement in many ways. Despite listing many economic objectives, only the goal of reducing the deficit was reflected in all of the policies and financial estimates. The fiscal statement laid out the decision to take a set of structural measures over three years, beginning in FY2014/2015 and ending in FY2016/2017, with the goal of maintaining the deficit as a percentage of GDP to around 10%. It further made clear that without these structural measures, the deficit as a percentage of GDP would have risen to 14.5% in FY2014/2015.

The dangerous economic repercussions of a widening budget deficit and growing public debt cannot be denied. At the same time, however, two issues cannot be ignored: First, the structural flaws in the public budget limit most spending to three areas: wages; interest paid on debt, which increases as the public deficit itself widens; and subsidies, for which there is no alternative system in place to limit worsening poverty, albeit partially. Further structural flaws in the public budget restrict state revenues to sales taxes and employment taxes, and together these flaws produce a continuous deficit. Yet it is unacceptable that measures to tackle this deficit should constantly come at the expense of the poor. Second, neither the severity of the budget deficit nor “safe limits” for this deficit can be measured as absolute numbers without also thinking about how to deal with the repercussions of reducing the deficit to the exclusion of other objectives. Nor should a reduction of the deficit be sought without considering the components of state expenditures and their effectiveness at bringing about equitable growth, achieving social justice, and fulfilling citizens’ rights to high-quality public services. Alternative ways to stimulate the economy must also be considered, rather than solely imposing severe austerity measures.

According to the fiscal statement, the package of reforms that led to a lessening of the expected deficit in the public budget did take into account the goals of achieving social justice, increasing rates of economic growth and employment, and ensuring cross-generational justice by limiting the rise of public debt. This requires examination and an analysis of the distribution of expenditures and revenue and of the measures included in this package of reforms, seen by both sides from the perspective of economic and social justice. In this case, the analysis focuses on those who primarily bear the consequences of the financial crisis and of the measures taken to address it. It ends by presenting a set of comments and recommendations aiming to spur further discussion about alternative ways to reduce the budget deficit which would be less prejudiced against the poor.

### **First: Projected Revenues and Their Sources:**

The fiscal statement established the target of raising the value of total revenues from around 507 billion EGP in FY2013/2014 to 548.6 billion EGP in FY2014/2015, an increase of about 42 billion EGP.

It should be noted that the target value of revenues in the absence of the structural reforms included in the framework of a three-year program was estimated to be around 476 billion EGP. This means that the structural reform package which begins this year will increase revenues by about 72 billion EGP.

The revenues projected by the fiscal statement also represent an increase of an estimated 31 billion EGP from the initial draft budget for FY2014/2015, which was presented late last May and estimated revenues to be around 517 billion EGP.

This means that the budget was drafted after adding both the impact of the structural reforms and the impact of the new austerity measures, seeking to further increase revenues following the issuance of the initial announcement of the budget.

With the projected decline of foreign assistance, the fiscal statement included a set of measures aimed at increasing revenues. The issuance of this statement was also accompanied by a number of tax amendments and additions. The most important components of the plan to increase revenues are as follows:

- An increase of the annual income tax on individuals and legal entities whose annual income exceeds 1 million EGP, according to Law no. 44/2014.
- The imposition of a new tax on capital gains and dividends, according to Law no. 53/2014.
- A number of amendments to Law no. 91/2005 on income taxes, according to Law no. 53/2014. The most important of these amendments is the imposition of an annual tax on the total net income of resident individuals according to their realized income earned either in Egypt or abroad if Egypt is a center of their commercial, industrial, or professional activities. The tax also applies to the income of individuals who are not residents of Egypt according to their realized income in Egypt. Taxes are also imposed on the net income of liberal professions and other non-commercial professions pursued independently by the taxpayer and in which the fundamental element is labor; on the income received by the holders of intellectual property rights from the sale or use of these rights, whether in Egypt or abroad; and on any revenue from any profession or activity not previously stipulated in Article 6 of Law no. 91/2005, as amended. Also added were new conditions on the application of exemptions of workers' contributions to private and life insurance funds stipulating that the amount exempted shall not exceed 15% of the net revenue or 10,000 EGP, whichever amount is less, and specifying the inadmissibility of repeated exemptions and premiums.
- Measures to counter tax evasion and harsher penalties for tax evasion.
- Application of the law on property taxes.
- A shift from a sales tax to a value-added tax (VAT).
- Issuance of a law on mines and quarries which includes regulation of private sector participation in this field and increases the yearly fee for licenses to search, protect, and

exploit, in addition to the imposition of royalties on annual production, according to the type of material being mined.

In reviewing the expected distribution of revenues from taxes of all forms, we see from the fiscal statement that tax revenue as a percentage of GDP is expected to see a slight increase from estimates of about 14.2% for FY2013/2014 only to about 15.2% in the public budget for FY2014-2015. This is due to the weak rates of economic growth that are expected despite efforts to increase this growth. In terms of value, an increase in tax revenues from 287 billion EGP predicted by the end of FY2013/2014 to 364 billion EGP in the budget for FY2014/2015 is targeted, an increased value of 77 billion EGP.

The table below displays the most significant items for the increase in tax revenue expected for FY2013/2014:

<b>Title</b>	<b>Estimated increase from predictions for FY2013/2014 (billions EGP)</b>
Sales tax	26.5
Taxes on companies (other than economic authorities)	16.6
Customs taxes	3.6
Capital gains taxes	2.7
Taxes on industrial and commercial activities	2.6
Taxes on professional activities other than trade	2.2
Employment taxes	1.8
Stamp tax	1.4
Real estate tax	0.3
Other	0.2

**Source:** Researchers' calculations based on data from the fiscal statement on the state budget for FY2014/2015.

Despite some expected increases in revenues from direct taxes, the budget's structure has not changed, with the General Petroleum Corporation maintaining its share of over 26% of the revenues from direct taxes, the Suez Canal maintaining 7%, and over 9% coming from taxes on treasury bills and bonds. This leads to a fundamental dependence on indirect taxes.

We can note from the above table that the greatest amount of the planned increase in tax revenues from the values predicted for the end of FY2013/2014 depends on sales tax, or VAT if a shift is made to that. Next come corporate taxes, the estimated increase of which raises many doubts,

particularly as this increase was estimated to exceed 37.6 billion EGP in the budget for FY2013/2014, yet it will not have reached more than 31.8 billion EGP by the end of the fiscal year, according to current predictions.

In terms of social justice, sales taxes continue to make up the fundamental basis for eliminating the budget deficit, as was demonstrated above. This was quickly reflected in the issuance of Law no. 58/2014 to adjust the sales tax on certain commodities, namely alcohol and tobacco. As is commonly known, sales tax – as a form of indirect taxation – is paid by consumers of all different income levels (albeit to varying degrees depending on the nature of the commodity and the price of the tax). As such, sales taxes are least able to address social inequalities.

When the temporary income tax was applied to those whose income exceeds 1 million EGP, according to Law no. 44/2014, the law overlooked the segment of people whose incomes equal 1 million EGP or less. As such, the law was only applied to the income value above 1 million. Moreover, the law itself states that the taxpayer may “request to use the revenue of this tax to fund one or more service projects, as defined by a decree issued by the minister of finance in coordination with the ministers responsible for planning in the areas of education, health, housing, infrastructure, and other areas of service.” This provision provides a major loophole which allows for the evasion of all or part of this tax. From another perspective, the freedom of the taxpayer to choose how the revenue from this tax should be spent – rather than the financial authorities who are subject to societal oversight – renders this “tax” more like voluntary philanthropic spending than like a tax, which is understood as making up the income of the sovereign state. At the same time, the tax will not apply to those who enjoy tax exemptions on their commercial or industrial profits until the period of these exemptions ends.<sup>3</sup> All in all, the adjustments to the income tax do not indicate a trend toward establishing a clear structure for the imposition of a progressive tax.

In the absence of a parliament, the amendments to the income tax law as a whole were never subjected to societal debate, despite the fact that taxation is one of the most significant acts of sovereignty undertaken by the state, as well as one of the most important regulators of the relationship between the ruler and the ruled.

In contrast, the capital gains tax, included in Law no. 53/2014, stirred up much debate. This tax had become urgently needed due to both the growing lack of justice and the increasing budget deficit. Several attempts had been made to impose this tax since the January Revolution, two of which were defeated – the first under the first government of Essam Sharaf and the second under the government of Hisham Qandil.

The current government was determined, following social and political demands, to impose this tax despite the huge drop that hit the Egyptian stock market out of protest at the draft law containing this tax. The imposition of this tax, however, cannot be viewed in isolation from the direction taken by the government towards adopting measures aimed at reducing fuel subsidies

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<sup>3</sup> <http://www.mof.gov.eg/Arabic/MOFNews/Press/Pages/news-a-12-6-14.aspx>

and imposing taxes on cigarettes and alcohol, as well as potentially taking further measures during the current fiscal year such as moving to a value-added tax. Taken together, these measures would have an inflationary effect, which would profoundly impact the lower-income segments of the population. The imposition of capital gains taxes thus takes on great importance in order to better distribute the tax burden and justify difficult decisions related to reducing subsidies. The law thus fulfills a societal demand and is not undermined by the predicted low revenues, as they may be attributed to the limited market value of capital shares in the stock market - which is itself limited in comparison to the size of the economy and the state budget. Although the tax does not exceed 10%, the law – which we consider to be positive overall – did not escape the social biases in favor of businessmen, as is clearly seen in context of the following:

- In comparison to all of the segments of society which will be affected by all decisions made by the government, whether with regards to taxes or fuel prices, the stock market community enjoys the advantage of being able to negotiate and debate with the government following the angry reaction of those who deal in the stock exchange. This is because there are bodies and arrangements that represent the interests of the stock market community, which is limited in size in comparison to other classes and segments of society.
- Due to this ability to negotiate, representatives of the stock market made an important gain – the total exemption of dividend stocks from taxation, as such stocks would have been subject to taxation two years after the passage of the law, according to the original draft. This is particularly significant when taking into consideration that taxes and dividends, both monetary and in-kind, make up at least 50% of expected revenues and that dividends are more permanent and continuous as a source of taxation as compared with realized gains, which may vary greatly from year to year.
- The claim does not stand that capital gains taxes represent a balance in the distribution of the burden of austerity measures, as the stock market community has the benefit of being able to negotiate, as referred to above. Furthermore, those who deal in the stock exchange, whether individuals or firms, enjoy the ability to make use of the services of legal and accounting experts in order to reduce the taxes they owe within the framework of the law. For example, speculators will adjust their dealings on the basis of speeding up their sales of stocks which are rendering losses and maintain those stocks which are making profits, such that the effect of the real losses increases as compared to the real gains. Similarly, corporations will increase the distribution of dividends as stock rather than as cash in order to qualify for exemptions stipulated by the law. Such advantages are not available for the rest of the segments of society, which struggle under the weight of increased prices and have no recourse to safety nets.

In conclusion, even if the direction of the government towards decreasing the budget deficit through an economic policy of broadening the base of direct taxes and increasing gains taxes on some companies, as well as some taxes on high-income individuals and efforts to counter tax evasion, may be moving in a positive direction, it remains limited and fails to implement a

progressive tax. Nor does it does include a fundamental change in tax policy, as it continues to defer to the economic interests related to those classes which enjoy a greater ability to influence policymakers.

## **Second: Rationalization of Expenditures and Those Who Bear Them**

The fiscal statement establishes the target of a limited increase in total expenditures from 737 billion EGP expected by the end of FY2013/2014 to about 789 billion EGP in the budget for FY2014/2015, an increase of not more than 52 billion EGP. This represents a growth rate of 7.1%, which is a lower rate of increase in public expenditures as compared to recent years; in FY2012/2013 the growth rate of expenditures was 25% more than the previous year, and in FY2011/2012 this rate was 18% higher than in the previous fiscal year.

It should be noted that, according to the data provided in the fiscal statement, the estimated value of public expenditure, without adding the impact of the structural reforms – which take effect this year and will continue for the three years – would have reached some 827 billion EGP. This means that the reform package referred to in the fiscal statement is expected to reduce expenditures by 38 billion EGP, or 4.6%.

According to the press statement released by the Ministry of Finance in late May 2014 discussing initial indicators about the budget prior to any amendments, public expenditures were estimated at about 807 billion EGP. This means that the latest austerity measures are supposed to saved only about 18 billion EGP from being added to the deficit, a reduction of 2.2% from the initial estimate in the first version of the budget. This represents a savings rate estimated at about 6.3% of the value of the deficit, which was estimated to be about 288 billion EGP in the initial announcement of the budget at the end of May.



### Distribution of Expenditures (billions EGP)

Item	Budget FY2014/ 2015	Estimated FY2013/2014	Difference
Wages and worker compensation	207.2	180.0	26.4
Purchase of Goods and Services	33.1	27.96	5.1
Interest payments	199	178.2	20.8
Subsidies, Grants, and Social Benefits	233.8	233.3	0.5
Other Expenses	49.06	38.4	10.7
Investments	67.2	78.4	-11.2

**Source:** Financial statement for the budget of FY2014/2015

The savings on expenditures came primarily from reviewing spending on subsidies to fix the total value of subsidies, grants, and social benefits at the level predicted for the end of FY2013/2014. This was essentially achieved by reducing subsidies on petroleum products from over 130 billion EGP predicted for the end of FY2013/2014 to around 100 billion EGP in the budget for FY2014/2015. At the same time, spending on social security pensions increased by about 5.7 billion EGP. Spending on electricity subsidies also rose by about 14 billion EGP to exceed 27 billion EGP in the budget for FY2014/2015, an increase which partially reflects the impact of the rise in the price of natural gas and other petroleum resources used to produce electricity, which made it necessary to come up with new arrangements on this matter.

At the same time, investments witnessed a notable reduction in order to make possible increased spending on interest payments, by about 21 billion EGP, and on wages, by about 26.4 billion EGP. In addition, the minimum wage continued to be applied, along with other measures including formalization of the status of contracted workers and a bonus established by Law no. 128/2009 of 10% added to the original salary at the beginning of July 2014.

In an attempt to limit increased spending on the item of wages, the fiscal statement announced the future governmental policy towards ending the inclusion of a special bonus to basic salaries every five years. Similarly, the tax exemption on **special** bonuses was removed, and a stop was put to new appointments to positions not officially covered in the budget. **These trends are not contributing to finding a fundamental remedy for the issue of wage distortion in Egypt. Rather, they are limited to the aim of ceasing future impact particularly due to the increased minimum wage set at the beginning of 2014 and do not follow structural reform of wages.** At the same time, Law no. 63/2014 to set the maximum wage was also issued. Although it covered more of the various governmental bodies, if this law on the maximum wage is not actively

implemented, it will be impossible for society - and particularly for workers in the lower ranks of government - to view this law as anything but a cursory step to enable reduced wage increases for the lowest-ranking employees without any move to confront the problem of the massive salaries earned by those in the highest ranks.

From another perspective, operational spending on goods and services will see an extremely low increase from that predicted for FY2013/2014. This is reflected in the value of allocations for medications, vaccines, grafts, and food for schools, medical patients, and some segments of workers, as the increase in money allocated for all of these items combined did not exceed the amount estimated for last year by more than 251 million EGP. The rate of this increase, which did not exceed 4.8%, does not match annual inflation rates, which are more than double this rate. This means that the actual subsidies for these commodities, which are vital to counter the catastrophic effects of disease and educational dropout rates due to malnourishment on certain segments of the population, have diminished without any societal consultations with the affected populations. These observations seem particularly important in light of the reality that real spending on some of these provisions is less than that estimated for last year's amended budget.

In addition, there has been a significant increase of over 10.7 billion EGP in the spending on item five ("other expenses" which include institutions of a particular nature, such as spending on defense, national security, the judiciary, and the Constitutional Court, in addition to taxes, fees, compensation, and international contributions), compared to an increase of 3.4 billion EGP last year. This comes at a time of heightened demands for increased transparency and an attempt to account for the money allocated to this item in order to limit the ability of the executive bodies to completely control spending on this item.

In terms of the important issue of lifting fuel subsidies, the trend toward lifting fuel subsidies was seen in decrees 1159, 1160, 1161, and 1162 issued by the prime minister immediately after the fiscal statement was released. The impact of these increased prices on the goal of reducing spending on subsidies was not clarified for each product in the fiscal statement, however. Nor were estimates for subsidies on natural gas mentioned.

This paper will analyze the trends seen in the fiscal statement and its relationship to the decrees lifting fuel subsidies from the following three angles:

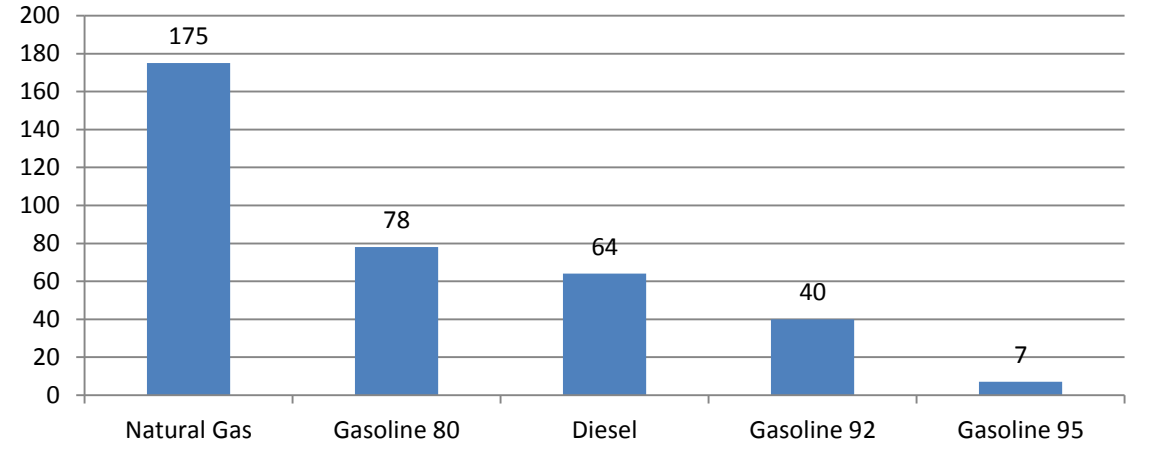
- Equitable distribution of the burden of this price increase.
- Its impact on inflation.
- The impact of the resulting saving for the other budget items which most affect human rights and the rights of the poor, including the rights to health, education, pensions, and the other components of state support, as revealed by the estimates of the fiscal statement.

In terms of equitable distribution of the burden of these increased fuel prices, the price that increased by the highest percentage was that of natural gas for automotive use, with an increase of 175%. This is the gas used by some buses, taxis, and tourist buses. The price that increased by

the second-highest percentage was that of gasoline 80, which is consumed by old cars and some taxis. Next is diesel, which is the fuel which most affects the transportation system, markets, and agriculture; it should be mentioned that the most important sectors which benefit from diesel subsidies are transportation (29.5%) and agriculture / irrigation (16.2%).<sup>4</sup> Diesel is followed by gasoline 92, which is primarily used by newer private cars. Finally, gasoline 95 increased for the second time after its highest price increase occurred in 2012; it is the least used form of fuel, as the previous increases of its price made many of those who used it turn to gasoline 92.

In short, this means that the highest rate at which fuel prices have increased belongs to fuels related to the sectors of public transportation and transportation of goods, despite the fact that these sectors are those which are most capable of shifting the effects of inflation to the final consumer. The greatest price increase was that of the petroleum products which most affect the poor and those most reliant on subsidies to help them avoid the major negative impacts of price increases. This indicates that the aim of financial policymakers in lifting these subsidies was reducing the budget deficit, rather than ensuring better distribution of subsidies in a way that targets social justice (see graph below).

**Average price increase of petroleum products for transportation and similar uses (%)**



**Source:** Calculations by researcher.

In terms of subsidies on fuel for industrial use, the cost of energy for all factories was increased – accounting for 38% of gas subsidies – including for food manufacturers. A maximum price was set for some energy-intensive industries. Perhaps the most prominent price adjustments were to the price of gas, which is sold for around 8 USD per million thermal units to the cement industry,

<sup>4</sup> According to data from the economic and social plan for 2014/2015.

at a 33% increase from its previous price of 6 USD, which had been set most recently according to Decree 110/2013. Gas is sold for 7 USD to the iron, steel, aluminum, copper, ceramic, porcelain, and glass industries and for 5 USD to food industries (increased from a price which had fluctuated between 2<sup>5</sup> and 2.5 USD, representing a doubling of this price) and the textile, pharmaceutical, brick-making, and other industries. The price at which natural gas is sold to the cement and petrochemical industry is 4.5 USD per million thermal units, yet the decree added the following line about determining the price for cement and petrochemicals: "...or according to the price equation referred to in the contracts," which could be used to defend maintaining the prices agreed upon for years.

The price of importing gas for electricity was set at 3 USD per million British thermal units (about 75 piasters per cubic meter of natural gas), increasing the price from its former level at a cost of about 44 piasters per cubic meter by more than 70%.<sup>6</sup> Electricity makes up a larger proportion of subsidies than natural gas by 59%.

At the same time, bakeries providing subsidized bread continue to obtain natural gas at the price of 14.1 piasters per cubic meter, even though the cost of natural gas has risen for households. This requires a strong system to prevent fuel smuggling and to ensure its use to maintain production of sufficient amounts of inexpensive bread.

The price of fuel oil used by food industries also increased from 1000 EGP per ton to 1400 EGP per ton, a one-time increase of 40%. In addition, the price at which fuel oil is sold to cement industries rose from 1500 EGP per ton to 2250 EGP per ton, an increase of 50%. The price at which fuel oil is sold to other industries, increased from 1500 EGP per ton to 1950 EGP per ton, an increase of only 30%; the price of 1950 EGP included brick industry as well.

From an analytical perspective on the social justice dimension of the increased prices of energy going to energy-intensive factories, we can say that these increases have come in response to social justice demands. Indeed, EIPR considers that these increases came very late, following years of an irrational policy of subsidies for energy-intensive industries. EIPR reaffirms its continued opposition to the setting of prices through contracts and price equations for these industries in a way that obstructs the application of any future price increases and restricts policymakers from liberalizing the price of energy going to these factories.

From an analytical perspective on the justice dimension of the increased prices of electricity for household use, according to the new price regime for electricity,<sup>7</sup> analyses indicate<sup>8</sup> that the price increases and restructuring of some segments have led to increases in electricity bills of between

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<sup>5</sup> 50 piasters per cubic meter.

<sup>6</sup> 1 million thermal units equals 28 cubic meters of natural gas, so 3 USD x 7 EGP = 21 EGP per 28 cubic meters, and 21 EGP / 28 cubic meters = 75 piasters.

<sup>7</sup> According to statements by the prime minister in a press conference at the beginning of this month.

<sup>8</sup> See the calculations at the "Shadow Ministry of Housing" website, available at: [http://blog.shadowministryofhousing.org/2014/07/blog-post\\_6.html](http://blog.shadowministryofhousing.org/2014/07/blog-post_6.html).

17 and 56%, which is no minor increase. Similarly, according to research data on expenditures and consumption published by the Central Agency for Public Mobilization and Statistics for FY2004/2005, the average monthly consumption for the segment of society with the lowest income was about 195 kWh, thus falling within the third stratum. The first and second strata are made up of those who are completely isolated or who use electricity only secondhand. They are not the poor strata, as government officials claimed. Lastly, these price increases have their greatest impact on the poor, not the rich, as the prices of electricity will increase for consumers from the poor segments of society (the third stratum) by 56%, whereas they will increase for consumers in the fourth stratum by 39%, in the fifth 25%, in the sixth 18%, and in the seventh around 17%. Here also it is clear that the idea of distributing price increases across the strata which consume electricity was governed by fiscal considerations seeking to reduce the size of the deficit more than by social considerations related to reducing social inequalities and stopping subsidies for the reach.<sup>9</sup>

With regards to the inflationary impact of this major reduction of subsidies on all forms of petroleum products, a study conducted by Abu El-Enein and others<sup>10</sup> in 2009 indicated that every 10% increase in the price of petroleum products increases the rate of inflation by 1.5%, with the assumption of more closely regulated markets than the current reality. This would mean that every 50% increase in prices of petroleum products would lead to an increase in inflation of 7.5%. This study estimated that modest increases in the prices of some energy derivatives in May 2008<sup>11</sup> contributed to an increase in the inflation rate of 6.2%. It also said that the effect of inflation could be accumulative, meaning that its immediate increase may be reflected again in higher increases in the future. This is was raises expectations about forthcoming rises in prices beyond these estimates in the context of the reduction of subsidies by percentages that in some cases exceeded 70%. The probability of future price increases seems even higher in light of the fact that these reductions were applied on all petroleum products at once, including for the food industries, and in conjunction with a major reduction of energy subsidies for the production of electricity, including for households, and the rising prices of gas for household use as well.

According to government statements, inflation will reach 14.5% by the end of FY2014/2015, an increase of 8.3% from its May 2014 levels.<sup>12</sup> As such, any different statements by the government

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<sup>9</sup> Some estimates went further, with some press statements about recent studies by Dr. Heba Al-Leithy, professor in the Faculty of Economics at the University of Cairo and a participant in the research on income, expenditures, consumption, and mapping of the poor with UNDP, indicating that / derive predictions that all prices will see an increase of 30% on average over the coming months due to the measures to reduce fuel subsidies; however, the final study has not yet been published.

<sup>10</sup> Abu elenein, Soheir, El-Leithy, Heba and Kheir eldin, Hanaa, 2009, "The impact of phasing out subsidies of petroleum energy products in Egypt", Working Paper Number 145, April

<sup>11</sup> The most significant feature of which was an increase in the price of gasoline 90 by about 34% - the sale of which was completely canceled by recent decisions after scarcity of this gasoline in the markets for a long period – and in the price of gasoline 92 by about 32% and of diesel for transportation purposes by about 46%, along with increased prices on the import of natural gas for some energy-intensive industries.

<sup>12</sup> According to statements made by the Minister of Planning.

attempting to downplay the inflationary effect of increased prices of petroleum products will be difficult to believe and will be impossible to interpret as anything other than an attempt to avoid admitting that the poor will bear the primary burden of reducing the budget deficit. Such an admission would invoke the state's responsibility toward the poor to lighten the burden of inflation that they face by proposing alternatives to create a social safety net.

The Egyptians who live just above the poverty line will be confronted by the effects of the economic crises in all their forms, particularly by dramatic inflation, even if this inflation is quantitatively small. The economic crises of FY2008/2009 were accompanied by a doubling of the percentage of the population living under the **severe** poverty line from 3.6% in FY2004/2005 to 6.1%, according to the income, spending, and consumption study of FY 2008/2009 issued by the Central Agency for Public Mobilization and Statistics. In short, financial policymakers must realize that the effects of the financial crises in all their forms, and the inflation which results, vary in terms of the size of the impact on groups of different income levels and that the brunt of these crises should not be borne by the poorest segment of society in any case.

In an attempt to reveal the effect of such policies on poverty rates, we find that the poverty line for a family of five was equal to 1620 EGP per month, according to the income, spending and consumption study of FY2012/2013. Adjusting this value to account for additional inflation at a rate of 15%<sup>13</sup> by the end of FY2014/2015, we find that the poverty line exceeds 2000 EGP per month. This means that all of the families whose monthly incomes are equal to or slightly above 2000 EGP have thus fallen below the poverty line. This segment includes a large number of middle-income families, according to the income, spending, and consumption study of FY2012/2013. This estimated increase in the number of families living below the poverty line results solely from price changes, without considering other poverty-producing factors, and appears conservative when compared to the actual rise in the value of the poverty line for such a family from 1280 EGP per month in FY2010/2011 to 1620 EGP in FY2012/2013. Further, this increase occurred in the absence of measures which could lead to major jumps in overall inflation rates. The value of the national poverty line is related to numerous factors, the most important of them being inflation occurring in a set of basic commodities, which could be subjected to rapid prices changes much greater than the average across all commodities.

In addition to acknowledging the importance of safety nets as an immediate, initial step towards lessening negative impacts on the poor, EIPR asserts its view that such safety nets are merely a first step and that they are inseparable from and can in no way replace the establishment of the full right to social security and the implementation of a comprehensive social security system. This concept goes far beyond the insufficient proposals thrown out by international institutions which reduce efforts to confront poverty to targeting the poor through a set of social security programs. In addition, EIPR points to the importance of regulating markets, particularly for industries which lack competition and which have long benefited from cheap energy. As indicated by Khattab's

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<sup>13</sup> After adjusting the value of the poverty line to account for inflation rates in FY2013/2014.

study<sup>14</sup> on the ability of energy-intensive industries to absorb the lifting of subsidies aimed at them, the high profitability rates of these industries allow them to completely absorb the impact of increased prices without transferring this burden to the consumer.

It is unacceptable that the burden of structural flaws in the state budget should be thus placed on consumers – particularly from the poorest segments of society – even as the new budget fails to include any serious steps to better enable the poor to absorb the major effects of the inflation which results from the lifting of subsidies.

EIPR expresses its concern about the status of the poor in light of the fiscal statement's references to the structure of subsidies on basic commodities which do not indicate any changes or expansion of these commodities. On one hand, this represents a reduction which was not present in the budget when it was initially presented last May, as the first statement included an increase of allocations going to subsidies of basic commodities, which was itself a minor increase to bring the amount to 34 billion EGP.<sup>15</sup> On the other hand, this contradicts what was announced by the government regarding an expansion of the choices of subsidized goods available to citizens, which had resulted in greater funding and clearer distribution of this item. Under the new schema, the numbers and estimates do not reveal an attempt to tackle poverty any more effectively, to provide food that better suits the needs of those who benefit from it, or to take advantage of the money saved from the energy subsidies to expand the available subsidized choices in light of rising inflation rates, instead of merely focusing on reducing the budget deficit at the expense of the poor. In the new public budget, food commodities were allocated 31.6 billion EGP, which is 3 billion EGP less than the amount projected for the end of FY2013/2014. From the amount allocated to subsidize food commodities, 2.6 billion EGP was set aside to subsidize the domestically-grown wheat; even when this number is added, however, there is a clear reduction of about 477 million EGP to the amount allocated to food commodities. This is reflected in the minor reduction of the quantity of subsidized rice as well as imported and domestically-grown wheat. The state justified this reduction by referring to the expected positive impact of the application of the new bread regime. EIPR asserts that, despite its shortcomings, in-kind subsidies of basic commodities represented an important form of support for the poor in the face of inflation and served as a tool of food security essential for survival. As such, all savings must be directed to expand and improve the administration of these subsidies.

A mere 811 million EGP were allocated for health insurance and medication subsidies. This represents a major reduction from the amended budget for FY2013/2014, which had allocated 2.67 billion EGP to this area, although of this amount not more than 700 million EGP was actually spent last year.

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<sup>14</sup> Khattab, Abdallah, 2007, "The impact on energy subsidies on energy intensive industries in Egypt", Egyptian Center of Economic Studies", Working Paper Number 124, May.

<sup>15</sup> <http://www.mof.gov.eg/Arabic/MOFNews/Media/Pages/releas-a-26-5-14.aspx>

The amount allocated to subsidies on baby milk and medication in the budget for FY2014/2015 was reduced by more than half from that of the previous year, In 2013/2014 it was 655 million EGP, only 180 million EGP were actually spent according to projected numbers for FY2013/2014. This number was increased back up to a mere 300 million EGP in the budget for FY2014/2015, which does not exceed the actual amount spent on this item in 2013/2014 by more than 120 million EGP.

Amounts allocated for subsidies going to health insurance were reduced from 520 million EGP in the budget for FY2013/2014 to 511 million EGP in the budget for FY2014/2015. Funds allocated to health insurance for female heads of households in particular were also reduced from 120 million EGP projected for FY2013/2014 to 104 million EGP in the proposed budget. Subsidies for health insurance for pre-school-aged children were increased by only 7 million EGP from the projected amount in FY2013/2014. These steps reveal a shocking trend by the state in terms of how it views its responsibility to provide health care to the poor, the marginalized, and those most in need of care. EIPR emphasizes its grave concern over these reductions, which contradict what the state has announced regarding funding to purchase medication for hepatitis C at a cost of 450 million EGP to be paid for by the state's fund for medical treatment and by the health insurance authority, the latter of which is to pay about 225 million EGP of the cost.

The increased amount allocated to passenger transportation subsidies did not exceed the 2013/2014 amount by more than a mere 54 million EGP. In previous years, this amount had seen an annual increase of between 150-200 million EGP.

Housing subsidies face major structural problems related to unclear processes of distribution which take place through numerous different bodies and funds.<sup>16</sup> It is expected that nearly 50% of Egyptians – i.e. the half of the population with lower incomes – will not benefit from the new social housing project due to conditions placed on real estate financing.<sup>17</sup>

In line with what has previously been stated by EIPR in a study about social housing, nearly 613 million EGP in housing subsidies, in addition to 9.5 billion EGP in related investments, have been directed at the top 50% of Egyptians in terms of income, i.e. the middle class, the upper-middle class, and the wealthy. This blatantly conflicts with the government's rhetoric about supporting the poor in attaining their right to adequate housing.<sup>18</sup>

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<sup>16</sup> No explanation of the items related to housing subsidies or of the components of each of the subsidized housing projects is clear from the financial statement, nor did the statement reveal the reason for the continued receipt by a low-income housing project of 150 million EGP, despite the fact that this project has ended in actuality.

<sup>17</sup> Refer to the study entitled, "Analysis of the budget of housing projects for fiscal year 2014/2015," attached in a separate link.

<sup>18</sup> Shawkat, Yahia, "Hata la yetem at-tamyeez dhid al-fuqara' wa tawgih ad-da'm 'ila man la yestahiq... muqtarah al-mubadara al-misreyya bi-ta'dil shurut bernamig al-iskan al-igtema'y," Egyptian Initiative for Personal Rights, April 2014.



In contrast to what we have stated about the poor bearing the primary burden of the impact of policies aiming to reduce the budget deficit, the increase in social security pensions represented a sole move towards compensating the poor. The value of allocations made to such pensions increased by 5.7 billion EGP from the projected amount for 2013/2014 to reach 10.7 billion EGP. This amount is to be distributed among 2.3 million families, which is 825,000 more families than those which benefited in FY2013/2014. Meanwhile, the government repeatedly claimed that the number of families benefiting from these pensions would double in the coming year to reach 3 billion families, and even the fiscal statement itself made this claim in other paragraphs. These claims present a contradiction which requires an explanation.

According to the fiscal statement, it is expected that average pensions received by families will increase from 258 EGP per month to 386 EGP per month.

While EIPR welcomes this increase to social security pensions, we doubt that this increase will be able to offset the effects of inflation described above, which will have negative impacts on these families. Furthermore, we assert that these pensions, the amounts of which are very modest even after the stated increase, will still not be able to raise these families above the poverty line. Indeed, the value of these pensions is much less than the abject poverty line, set at 214 EGP per month for one individual according to the study of income, expenditures, and consumption for FY2012/2013. As recorded in the fiscal statement, the pension amount allocated to a family of four will not exceed 450 EGP per month in FY2013/2014, or about 112 EGP per person per month. Thus, the only mechanism which might have helped to offset the overwhelming rates of inflation is considered to be ineffective and inequitable in terms of the amount allotted per person. It further continues to suffer from numerous problems related to its targets and evaluating its effectiveness.

In other words, the lifting of subsidies aims to reduce the budget deficit without considering the impacts on the poor. This policy contradicts international experience which considers the establishment of an alternative system for conditional and unconditional cash transfers and an expansion of subsidies for basic food commodities for the poor to be necessary conditions which must be met before measures are taken to reduce subsidies. It further contradicts the standard policy of providing safety nets in the form of social security to protect the poor from the impacts of economic crises, as espoused by international institutions in cases where neoliberal models of growth are followed.

A review of the functional breakdown of expenditures in relation to the sectors which fulfill human rights – and the rights of the poor more specifically – to education and health reveals a minor increase in the proportion of spending going to health as compared to the level of spending projected to have been spent on health by the end of FY2013/2014.

The percentage of all expenditures in the budget for FY2014/2015 going to health is about 5.4%, which is at least 1% higher than the percentage – estimated at 4.5% - of expenditures of the amended budget which will have gone to health in FY2013/2014. This increase was brought about

by the application of some limited increases to systems to incentivize doctors, in light of the existence of two programs funded in collaboration with the World Bank with the aim of improving health services in hospitals in eight governorates and assisting the poorest in society by having the government cover the actual costs of the use of such services for them. As specifically stated in the fiscal statement, the two programs aim “to take the place of making fixed payments for health insurance in light of the pressing conditions facing the state budget, which suffers from a chronic financial deficit”. The combined cost of the two programs related to geographic targeting is estimated at not more than 860 million EGP annually. The sustainability of the impacts of these initiatives on the quality of health services in the target regions cannot be guaranteed, as the system of geographic targeting itself suffers from multiple problems related to the fairness of their health coverage. EIPR thus emphasizes the importance of moving forward with a plan for comprehensive health insurance, as this is the solution which best fulfills citizens’ right to health.

Measuring the estimated amount spent on the health sector as a percentage of GDP reveals this percentage to be 1.8%, as compared with the actual percentage of 1.5% from FY2012/2013 and 1.6% from FY2013/2014. This reflects the failure to begin moving towards implementing constitutional obligations of 3% of GNP<sup>19</sup> to take spending on health care seriously, as opposed to the spending priorities which were clearly emphasized in the fiscal statement.

Despite the money that is expected to be saved during this period of austerity, spending on health has not been increased by more than 9 billion EGP from the amount found in the amended budget from last year, representing an increase of about 27% (real increase of 12.5%). This is compared to the increase of 7.4 billion EGP which was added to the amount spent on health in the amended budget of FY2013/2014, an increase of 28% (real of about 19%) from the actual amount spent on the health sector in FY2012/2013. It is worth noting that the rate of the estimated increases over these two years was higher than the rate of the increase in actual spending on health in FY2012/2013, when the rate of increase was about 16% (real of about 5.1%) more as compared to the previous year. The amount allocated from spending on health for investments in the budget for FY2014/2015 is about 5.7 billion EGP.

Although it is praised, this increased growth rate in terms of societal spending on health remains limited. This raises questions regarding future funding for citizens’ right to health services after the money in the budget made available by the lifting of subsidies and the imposition of sales taxes on cigarettes and alcohol has been used up, particularly as the surplus money currently available has not been sufficiently directed to develop the health sector as a fundamental priority or to bring about other adjustments in the spending structure. Furthermore, this increase was not accompanied by a clear move toward fundamentally improving health services and ensuring a just distribution of these services, which would in turn improve the effectiveness of any future increase in spending

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<sup>19</sup> The constitutional obligations state a minimum expenditure on education and higher education of 6% of GNP. When calculating figures of expenditure on health and education as percentage of GNP (published by World Development Indicators-Atlas Method) minimal variations that does not exceed 0.1- 0.2% appear. However- of course- keeping same trend across time, ensuring that constitutional are yet far to be met.

on the sector as well. EIPR emphasizes the importance of directing financial savings to these sectors which most affect the right to life of high quality and which have a particularly large effect on the poor.

The aim of ensuring a just distribution of investment within the health sector faces the problem that private investment in new health-related projects is very geographically concentrated, with 65% of such investments going to Cairo and Alexandria. Specialized treatment hospitals receive 45% of investment while primary health care receives 21%, which further reflects this inequitable channeling of resources. In addition, private investment in the health sector makes up about 45% of potential investments, which reflects a trend toward increasing dependence on the private sector to fund and provide health services.

Total spending on education represented 11.9% of expenditures in the budget for FY2014/2015, representing a minor increase from its level in the amended budget for FY 2013./2014 of 11.3%. The proportion of spending on education as a percentage of GDP was 3.9%, which did not represent a significant increase from FY 2013/2014 when it was around 4%, or FY2012/2013, when this proportion was estimated to be about 3.8%. These percentages fall far short of constitutional obligations to allocate 6% of GNP<sup>20</sup> to public spending on education and 1% to scientific research.

This raises concerns about what is being gained in return for the sacrifices and austerity measures currently being taken, which are supposed to be going towards ensuring the future ability of ordinary citizens to obtain their rights to health, education, and social security.

The table below lays out the general view held by EIPR with regards to the implementation of the most important pillars of Egypt’s economic policy for the coming year, as defined by the fiscal statement. EIPR stands largely in agreement with these premises and principles, yet we do not see that there is conformity between these principles and practical implementation of Egypt’s economic policy, as expressed in the actual allocations to spending items and investments.

<b>Principles and Premises Taken from the Public Budget for FY2014/2015, as per the Financial statement</b>	<b>EIPR’s Comments on the Credibility of these Objectives in Light of a Review of the Structure of Revenue, Expenditures, and Actual Policies</b>
“Bring about a fundamental change in the method of administering the national economy such that it is managed as a single unit and from the perspective of the whole,	The economic objectives centered on the conservative goals of merely reducing the budget deficit without reviewing the structural problems related to revenue and expenditures in order to seek a fundamental

<sup>20</sup> The constitutional obligations state a minimum expenditure on education and higher education of 6% of GNP. When calculating figures of expenditure on health and education as percentage of GNP (published by World Development Indicators-Atlas Method) minimal variations that does not exceed 0.1- 0.2% appear. And of course, keeping same trend across time, ensuring that constitutional are yet far to be met.

<b>Principles and Premises Taken from the Public Budget for FY2014/2015, as per the Financial statement</b>	<b>EIPR’s Comments on the Credibility of these Objectives in Light of a Review of the Structure of Revenue, Expenditures, and Actual Policies</b>
<p>rather than as separate sectors and issues or for the benefit of narrow group interests.”</p>	<p>change that would be more equitable and more able to stimulate the economy.</p>
<p>“Redistribute available resources to the benefit of the poor.”</p> <p>“No economic measure without a corresponding social measure.”</p> <p>“The most important reason for financial reform: Achieving social justice.”</p>	<p>The spending increases aimed at the sectors of education and health are very minor, and no change was seen in the percentage of GDP or expenditures going to these areas that evidences a change in the distribution of resources to benefit the poor.</p> <p>Even as the government took measures to get through the crisis by reducing subsidies, it did not redirect the resulting savings to the benefit of the poor, who will bear the brunt of inflation in the absence of alternative systems of social security. It is thus impossible to say that a policy of coupling economic measures with social measures is a pillar of the state’s administration of economic policy.</p> <p>The geographic concentration of investment in the health sector remains stark, even though this is the most important sector and is related to the right to life.</p> <p>Taxes affecting the upper classes continued to contain loopholes allowing for tax evasion, and the tax structure remained unfair despite attempts to broaden the tax base. In this framework, it is expected that tax revenues will be centered on consumption taxes, which are borne by all segments of the population.</p>
<p>“Encourage the mechanisms of the free economy and respect for all contracts as long as they are not tainted by corruption, along with the development and strengthening of the state institutions and the governing frameworks to regulate work and investment and to modernize them and establish balance between the rights and duties of various segments [of society].”</p>	<p>No measures to establish a system of serious societal oversight are clear from the policies presented in the fiscal statement; rather, these policies tend towards denying society its right to monitor contracts, as has recently occurred.</p> <p>The fiscal statement did not mention the requirements of strengthening institutions in terms of decentralization and activating the role of popular local councils, elected</p>

Principles and Premises Taken from the Public Budget for FY2014/2015, as per the Financial statement	EIPR's Comments on the Credibility of these Objectives in Light of a Review of the Structure of Revenue, Expenditures, and Actual Policies
	bodies, and syndicates and trade unions. In such a case, it is impossible to consider balance between rights and duties one of the premises of the budget.
“The most important reason for financial reform is ‘to increase the growth rate and the employment rate’.”	This is in contradiction with the reduction of government investment, as referred to in the fiscal statement, and particularly with the ongoing state of political and economic instability, which is expected to increase if no serious review is undertaken of issues of social justice and if nothing is done to lessen the burden of inflation for the poor or to prevent this state of instability from spreading to affect investment in the private sector.
<p>“Eliminate all policies of subsidies in order to direct capital to investment in energy-intensive industries.”</p> <p>“Move towards subsidizing renewable, clean energy.”</p>	<p>No new system of tax incentives based on indicative targeting has been established for any economic sectors.</p> <p>It has been stipulated that some industries will be allowed to use coal instead of fuel oil as a source of energy, which could result in the spread of the use of coal as an industrial alternative. This represents an industrial strategy based on conceding the rights of society to a clean environment in order to preserve elevated profits while avoiding the effects of decisions to eliminate subsidies.</p> <p>EIPR affirms the importance of announcing a clear, comprehensive strategy to shift to clean energy and to refrain from expanding the use of coal as an alternative.</p>
“Provide and improve basic public services.”	The fiscal statement does not include any major change to the structure of the spending components in the sectors of education and health, as the amount allocated from expenditures to investing in health did not exceed 13% on average, with a slight decrease from the estimates of the budget for FY2013/2014 before it was amended, when

Principles and Premises Taken from the Public Budget for FY2014/2015, as per the Financial statement	EIPR’s Comments on the Credibility of these Objectives in Light of a Review of the Structure of Revenue, Expenditures, and Actual Policies
	<p>the percentage was estimated to be around 14.8%.</p> <p>The amount allocated to investing in education was equal to 8% of all expenditures on this sector; this investment also saw a reduction from its levels in the budget of the previous year.</p> <p>Despite the lifting of fuel subsidies, the fiscal statement did not stipulate a clear plan to complete improvements to the public transportation system or increase allocations to subsidize this cost. This was particularly clear outside Cairo and Alexandria, where there is total dependence on forms of transportation that cannot have such spending added to their price. Investment aimed at buying the mechanisms, equipment, and methods of transportation decreased from a projected 15.1 billion EGP in FY2013/2014 to 13.2 billion EGP in FY2014/2015. This is cause for concern regarding the development of the transportation system, or reveals the trend towards reliance on the private sector in this area without any system for subsidizing or setting appropriate prices being clarified so as not to increase the financial burden on citizens.</p>
“Follow policies of social protection.”	<p>The understanding of “social protection” is broad and includes the rights to education, health, housing, appropriate work, a minimum wage, and social security with all of its components. Even as it stipulates following policies of social protection, the fiscal statement limits what it provides in terms of compensation to the poor due to inflation to increased social security pensions.</p>

Principles and Premises Taken from the Public Budget for FY2014/2015, as per the Financial statement	EIPR's Comments on the Credibility of these Objectives in Light of a Review of the Structure of Revenue, Expenditures, and Actual Policies
<p>The beginning of the fiscal statement refers to a vision of the impact of the monetary saving from fuel subsidies on education and health which is reflected in the following:</p> <ul style="list-style-type: none"> <li>• The transfer of some 12 billion EGP more than was provided in the public budget for FY2013/2014 for all services related to education, including the services designated in the budget as falling outside the field of education.</li> <li>• The addition of 9.5 billion EGP to health spending, including services designated in the previous budget, as amended, as falling outside the field of education, to raise spending on health to 51.6 billion EGP.<sup>21</sup></li> </ul>	<p>It is impossible to determine that these increases and new additional increases that came when savings were achieved through reducing subsidies on petroleum products. According to the data from previous years referred to in the initial announcement of the budget last May, annual spending increases on health in the amended budget were estimated according to the same broad definition which includes all services outside the sector in FY2013/2014 at 10.5 billion EGP more than the actual number from the previous year.</p> <p>From another perspective, the fiscal statement explained that there was an increase in spending on the sectors of education and health by 11 billion EGP more than the normal increases in previous periods, without explaining what was meant by these normal increases in previous periods.</p> <p>EIPR asserts that monitoring of the various estimates – with their different understandings – of spending on these vital services, which are related to clear constitutional obligations, requires a clear declaration by the Ministry of Finance and other executive bodies about their vision for the components of accountability and the bodies whose budgets are included in expenditures going to the services of education and health from outside the sectors, as well as on the nature of each increase in spending on these sectors and the bodies responsible for them.</p> <p>As should naturally be the case, EIPR asserts that the proportions which are</p>

<sup>21</sup> There is no complete explanation of these increased numbers; an inquiry took place to compare the table referred to in the first financial statement on the components of social spending in the budget for FY2014/2015 with the corresponding table referred to in the financial statement itself on page 45.

<b>Principles and Premises Taken from the Public Budget for FY2014/2015, as per the Financial statement</b>	<b>EIPR's Comments on the Credibility of these Objectives in Light of a Review of the Structure of Revenue, Expenditures, and Actual Policies</b>
	constitutionally established for spending on particular sectors are intended to mean spending on the sector itself.

### **Concluding Comments:**

It is clear from the information presented above that the fundamental pillars of the fiscal statement for the state's general budget, as well as for the austerity measures that followed, are primarily aimed at reducing the budget deficit. It is also clear that social justice was not a determining factor in the drafting of this budget, as its spending items did not reflect a clear trend towards justice and towards reformulating the role of the state in providing the rights to education, health, and social security with all its components.

Tax adjustments attempted to increase revenues without affecting the existing tax structure, which is essentially dependent on indirect taxes as the basis for increasing tax revenues. Other taxes also partially reflected the interests of the segments of the population which hold the most influence over policymakers. For example, the segment of those with incomes of 1 million EGP were not included in the temporary tax, and exemptions were issued which lessened the tax revenue on capital gains. With regards to spending and austerity measures, EIPR affirms its approval for continuing in the direction of lifting energy subsidies for energy-intensive industries. However, many measures in the same laws directly affect the poor and those with low incomes, as described above, without any clear, preannounced move toward creating alternative forms of social protections.

In sum, austerity policies are essentially based on cutting back on spending by lifting subsidies, yet without the creation of an alternative system of social protection or social security. Increased revenues are largely based on new sales taxes or a shift to a value-added tax, a policy which will lead to inflation – the brunt of which will be borne by the poor – and which does not conform to the objectives of justice.

Perhaps these realities make it necessary to discuss some fundamental positions which have long been held by all civil society organizations and which have often been reflected in the studies issued by the Egyptian Initiative for Personal rights. The most important of these positions are as follows:

- First: Establishing the principles of participation and transparency, along with making public the preparation of the state budget and related legislation which affects financial



issues, are not mere political demands. Rather, they are an economic necessity. Without participation and the public sharing of information, the positions and needs of the different segments of society will not be reflected in the numbers of the budget and the background to its estimates. The effectiveness of expenditures is thus limited, leading to a deeper void of social justice. This in turn results in instability when the segments of society with the least influence over the authorities are denied the ability to express their views and to influence economic decisions which affect them. This year's fiscal statement, as well as its accompanying austerity measures, came in the absence of a parliament and without presenting the budget for discussion by society. The statement further included an announcement about moving towards implementing a value-added tax as an alternative to the sales tax, without any societal discussion having occurred around this draft legislation either, thus repeating the problems surrounding the laws related to the austerity measures once again.

The fiscal statement specifically announced a move towards allowing some industries to use coal instead of fuel oil as a source of energy, thus offering this as an option to avoid the effects of rising energy prices. This comes despite the statement's assertion of support for moving towards clean energy, even going so far as to allocate subsidies of 1 billion EGP to support the shift to clean and renewable energy. It should be mentioned that this item was allocated 1.3 billion EGP in last year's amended budget. However, it is projected that the final account will reveal the failure to spend the money allocated to this item, as its value was estimated in the final projections at zero.

The general propensity of the state to expand the use of coal as an alternative form of energy represents a challenge to the societal rejection of its use, and this without any credible discussion about the effectiveness of the presence of environmental guarantees for avoiding major negative repercussions on the health of citizens.

A general sales tax on cigarettes and alcohol was similarly passed without stipulating or clarifying that the revenues from this tax would be directed to the sectors of health or development. This prompts concerns about the financial possibilities which will be available in the future to fund services related to the human rights to health and education. Government authorities repeatedly announce that the system of subsidies on bread and other basic commodities will be amended, without revealing the effect of this in the fiscal statement and without conducting a societal dialogue about these amendments, the extent of their impacts on the poor, and the extent of the capabilities of technological tools to effectively reach all those who really qualify for such aid. Even as EIPR believes in the importance of eliminating the smuggling of subsidized intermediate goods, such as flour, it asserts that a failure to fully include the poor and all those who qualify for subsidies such that measures taken contradict with the principle of guaranteeing the right of each individual to obtain sufficient food, such as by specifying a set maximum amount for a family made up of a particular number of people, or the insufficiency of what an individual is able to obtain from through minimal allocations, will lead to their confronting new

inflationary pressures which multiply the burden of the prices of basic food commodities. This, in turn, will lead to a state of massive popular anger.

The fiscal statement did not specifically mention any clarifications or clear financial allocations regarding purchase one of the most important components of health spending in this year – medication to treat hepatitis C, one package of which costs 300 USD and lasts for one month. No clarification was given regarding whether funding for this medication would be allocated by health insurance or under treatments covered by the state.

The statement further failed to address complementary measures to the lifting of energy subsidies aimed at the transportation sector, such as subsidizing the price of using such transportation or building a good public transportation network that ensures geographic fairness.

A large set of funds – the annual spending on which is difficult for society to monitor – continue to take up a significant portion of spending under the fourth item of the public budget, that of subsidies and social security. This includes such things as the fund to subsidize and stimulate exports, as well as ill-defined allocations to projects related to the right to adequate housing.

- Second: It is important to review the model of growth being followed, as it has been proven to fail. This model was based on sacrificing a set of basic economic rights – including to education, health, social security, and other rights related to suitable work – in order to bring about growth. It was hoped that the impact of this growth would be reflected in greater employment and higher tax revenues, which would in turn achieve financial sustainability. It would then be possible to use tools in the form of grants to address the issue of poverty, instead of putting forth solutions to address the roots of this problem. These tools of the state have failed to limit increases in the number of poor and to provide subsidies under which the state bears the impact of price changes. This model has not only exacerbated the failure to achieve justice, but it has also created structural flaws due to which the budget deficit, economic recession, and inflation have become self-perpetuating problems whose continuation is made possible through increasing public debt. Even though these structural flaws forced the state to confront the budget deficit, the state did so by lifting subsidies without considering the poor and their needs for alternative methods to be pursued. First the poor bear the consequences of this model of growth, which failed to take them into account in the first place, and then they bear the crises produced by this model's flawed system alone. EIPR affirms that the structural flaws in terms of expenditures have been inherited from the past and are not the product of the current crisis. The reasons behind the public deficit include several factors related to the financial management of the state. A prominent example of this structural flaw is the absence of a role for effective direct taxation in

providing state revenue in an equitable manner, which leads the state to rely on increasing debt to fund the deficit instead of on direct taxes, whose increased contribution to revenues did not reflect growth. At the same time, interest on debt was reflected in a further increase in the deficit.

It was hoped that this fiscal statement would set forth a serious change to the model of growth to make it more equitable as well as to the composition of expenditures such that the poor would not bear the brunt of the economic crisis. However, this did not happen. Instead, the fiscal statement aimed at implementing hasty measures to reduce the current budget deficit – at the expense of the system of rights – with the objective of achieving financial sustainability. However, this sustainability will soon disappear, and the measures taken to address this will lead to increased poverty.

It is not logical to continue with the same structure, much less to sacrifice investment spending and the rights of the poor. Indeed, largely eliminating the rights dimension of the issue results in a narrowing of the economic policy objectives of the state to only include increasing growth and maintaining the budget deficit as a percentage of GDP at or below 10%. These goals alone are insufficient and will not lead to seriously addressing the structural problems which produce a lack of justice.

Austerity measures also raise questions about the ability of the economy to meet expectations about increased economic growth. It may be particularly difficult to achieve an increase in growth in light of decreased government investment from its levels in FY2013/2014, which may prevent meeting the targets set by the economic and social development plan for the same year in terms of achieving an increase in investment from 13.1% during FY2013/2014 to 14% during FY2014/2015 and an increase of real private final consumption expenditure by 2.6%.

Perhaps achieving a higher growth rate requires certain measures based on encouraging expanded government investment and stimulating demand in the market until the economy is able to recover from its current state of inflationary recession.

- Third: It is important to review losses, whether due to corrupt contracting, to flaws in channels of distribution, or to the formulation of programs. A number of channels for loss continue to exist in the energy system. For example, losses of the electricity network increased to 14% in FY2013/2014, an increase of 2% from the previous year,<sup>22</sup> according to a report by the Central Agency for Public Mobilization and Statistics. This ranks Egypt 63<sup>rd</sup> among states in terms of losses.<sup>23</sup> More importantly, however, is that the monetary consequences of these losses are estimated to be 10 billion EGP, based on the price of 47.4

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<sup>22</sup> Irtefa' al-faqd fe a-shabaka al-kahraba'eyya 'ila 14% bi-neheyyet yuneyu, Al-Mal, 01.06.2014, <http://www.almalnews.com/Pages/StoryDetails.aspx?ID=155143#.U71KL7Gk8We>.

<sup>23</sup> Statistics on the losses of electricity networks 2011, The World Bank, [http://data.worldbank.org/indicator/EG.ELC.LOSS.ZS?order=wbapi\\_data\\_value\\_2011+wbapi\\_data\\_value+wbapi\\_data\\_value-last&sort=asc](http://data.worldbank.org/indicator/EG.ELC.LOSS.ZS?order=wbapi_data_value_2011+wbapi_data_value+wbapi_data_value-last&sort=asc).

piasters per kWh.<sup>24</sup> At the same time, the new energy prices do not address the issue of losses, which is not related to lifting subsidies or reducing value but rather with the administration of the system for distribution of the subsidized commodities themselves such that citizens can benefit from subsidies, which generally tend to directly support the final product.

A review should also be undertaken of the types of contracts established regarding sales and export of petroleum products, which at times impose unjust price obligations on the state which may benefit foreign and local investors and foreign markets, but which do not benefit the consumer.

In addition, measures must be taken to encourage electronic payments and to mechanize surveillance of monetary exchange in all of its items and stages.

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<sup>24</sup> Based on the amount of electricity produced in FY 2012-2013; 164.6 billion kilowatt-hours. "Al-'Ihsa'": 4.6% zeyada fe al-kahraba' al-mawloda khilal 2012-2013, Akhbar Misr, 05.06.2014, <http://www.egynews.net/wps/portal/news?params=307146>.