EGYPTIAN INITIATIVE FOR PERSONAL RIGHTS

المبادرة المصرية للحقوق الشخصية

2024/2025: A Budget for Interest on Debt..

Austerity for Us and Profits for Creditors

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Interests share of GDP is larger than wages, subsidies, education and health combined

2024

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The Egyptian Initiative for Personal Rights (EIPR) has been working since 2002 to strengthen and protect basic rights and freedoms in Egypt, through research, advocacy and litigation in the fields of civil liberties, economic and social rights, and criminal justice.

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At the beginning of July 2024, the new budget, which was approved by the parliament after very brief deliberations that are wholly inadequate when measured against the serious financial implications of the new budget, began to take effect. The new fiscal year's budget shows how the expansion of borrowing has siphoned off budgetary resources and diverted them away from much needed service delivery. The discussion of the budget is inseparable from all the issues that currently preoccupy the Egyptian population, whether the high prices of goods and services, or the electricity cuts and load shedding, deteriorating quality of education, and the unavailability of many essential medicines.

In June, one month before the end of the 2023/2024 fiscal year, the government raised the price of subsidized bread, increased the price of medicine, privatized health services in public hospitals, and a month later increased fuel prices, which in turn will lead to higher prices for goods and services[1]. Austerity measures are increasing their ever-tightening grip on citizens' livelihoods a few months following another devaluation of the national currency, a devaluation which is likely to recur given the exchange rate flexibility agreement with the IMF.

In spite of these conditions, Mohamed Maait the Minister of Finance at that time, had no qualms about announcing in a press release[2] after the House of Representatives approved the budget that the priority in this budget was for

1 Ehab Farouk, "Does Egypt's fuel price increase affect inflation?", Asharq Business Bloomberg news platform, July 26, 2024, ln.run/SmU_N

2 "The Minister of Finance after the House of Representatives approved the new budget: Priority is for Health, education, industry and agriculture," press release, Egyptian Ministry of Finance website, June 4, 2024, https://mof.gov.eg/ar/posts/media/665ec28d5fb-8d50008653501/%D9%88%D8%B2%D9%8A%D8%B1%20%D8%A7%D9%84%D9%85%D8%A7%D9%84%D9%8A%D8%A9..%20%D8%A8%D8%B9%D8%AF%20%D9%85%D9%88%D8%A7%D9%81%D9%82%D8%A9%20%D9%85%D8%AC%D9%84%D8%B3%20%D8%A7%D9%84%D9%86%D9%88%D8%A7%D8%A8%20%D8%B9%D9%84%D9%89%20%D8%A7%D9%84%D9%85%D9%88%D8%A7%D8%B2%D9%86%D8%A9%20%D8%A7%D9%84%D8%AC%D8%AF%D9%8A%D8%AF%D8%A9%3A%C2%A0%20%20%D8%A7%D9%84%D8%A3%D9%88%D9%84%D9%88%D9%8A%D8%A9..%20%D9%84%D9%84%D8%B5%D8%AD%D8%A9%20%D9%88%D8%A7%D9%84%D8%AA%D8%B9%D9%84%D9%8A%D9%85%20%D9%88%D8%A7%D9%84%D8%B5%D9%86%D8%A7%D8%B9%D8%A9%20%D9%88%D8%A7%D9%84%D8%B2%D8%B1%D8%A7%D8%B9%D8%A9%20%D9%88%D8%A7%D9%84%D8%AA%D8%B5%D8%AF%D9%8A%D8%B1%20%D9%88%D8%A7%D9%84%D8%AD%D9%85%D8%A7%D9%8A%D8%A9%20%D8%A7%D9%84%D8%A7%D8%AC%D8%AA%D9%85%D8%A7%D8%B9%D9%8A%D8%A9%20%D9%84%D9%84%D9%81%D8%A6%D8%A7%D8%AA%20%D8%A7%D9%84%D8%A3%D9%83%D8%AB%D8%B1%20%D8%A7%D8%AD%D8%AA%D9%8A%D8%A7%D8%AC%D9%8B%D8%A7%20%D9%88%D8%AA%D8%AD%D8%B3%D9%8A%D9%86%20%D9%85%D8%B3%D8%AA%D9%88%D9%8A%20%D9%85%D8%B9%D9%8A%D8%B4%D8%A9%20%D9%85%D8%AA%D9%88%D8%B3%D8%B7%D9%8A%20%D8%A7%D9%84%D8%AF%D8%AE%D9%84

"health, education, industry, agriculture and exports, social protection for the most vulnerable groups, and improving the standard of living for middle-income earners". He went on to say "we are committed to completing the strategy of building the Egyptian people, stimulating private sector growth and dealing with inflationary effects to ease the burdens on citizens." However, the details of the budget do not indicate that it even comes close to achieving the minimum of these goals - in fact, it outright contradicts many of them.

The main feature of the new fiscal year's budget is that debt and its interest payment obligations swallow up a large part of the government's planned expenditure, while that the state relies primarily on bringing in new loans to secure resources to cover the budget deficit. This dynamic means that this is likely to continue and deteriorate for years to come, as it causes the debt service allocations to become increasingly inflated in future budgets.

While public expenditure devoted to servicing internal and external debt has continued to increase over the past ten years, real spending has declined on all items related to citizens' basic rights, such as wages, health, education, and social protection.

Budget data shows that spending allocations on most expenditure items increased by around 20% (year over year), with the exception of debt interest payments, which increased by 63%, and government investments, which declined by 15%. But if we take into account the consumer price index and calculate the real value of expenditures, the analysis is quite different. High inflation rates mean that the real value of money and its purchasing power is declining. Therefore, referring to the average consumer prices available at the time of the paper's release (data from May 2022 to May 2024) to compare public expenditure in 2024/2025 budget with the previous year, shows that spending on all budget items declined in real terms, and the only item that saw growth in real spending was interest payments, which increased by 21%[3].

3 The change in spending in real terms was calculated by considering the real value of the previous year's spending (the nominal value stated in the previous budget multiplied by the average consumer prices from May 2022 to May 2023, then divided by the average consumer prices from May 2023 to May 2024), and comparing it with the nominal value in the new budget to find the real growth or decline rate.

Parliament passed the budget on June 3, after very hasty deliberations that coincided with announcing the government's resignation and assigning its head to form a new government. Many parliament members and government representatives focused their brief discussion on the international and regional crises and their role in Egypt's economic difficulties[4]. A number of opposition MPs rejected the new budget as not fulfilling Egyptians' aspirations for a decent life, while pro-government MPs repeatedly echoed the official rhetoric of executive officials that there are necessities for state building and sacrifices that must be made for the sake of a "better" future.

The report of the House of Representatives' Plan and Budget Committee made a number of worthwhile recommendations and engaged with the details of the budget in several points, but it did not provide a critique of the macroeconomic policies that led to the current situation. Its most important recommendation was to highlight the significance of estimating the necessity of state projects before they are included in the budget plan, and to measure their economic and social impacts and expected returns before they are implemented (a seemingly obvious policy-making step that should be at the core of the mandate of the Plan and Budget Committee, which evaluates planning policies holistically and not just in detail, yet has been largely absent from parliamentary discussions and the broader political debate in recent years). The committee also recommended an obligation to prepare feasibility studies for projects signed off for implementation, whether financed from the treasury or from loans and grants[5].

The government's discourse always seeks to focus on global developments and regional crises as being responsible for the crises of the Egyptian economy, shirking any responsibility for creating these crises, or for continuing to opt for wholly inappropriate tools to respond to them.

4 The Parliament passes the budget asking for "God's protection"with a request for a "jacket" and Maait's smile, Safaa Essam El-Din, Al-Manasseh, June 6, 2024, https://manassa.news/stories/17873?fbclid=IwZXh0bgNhZW0CMTEAAR09oa7u67lmwoa_bAl-pIvX0KX99e7Ev7Z4qjsLhdz_qevhz1hQHdYGa85Q_aem_68HAtS6so_4bo5oTjdXe1Q#-google_vignette

5 The report of the parliament's Planning and Budget Committee on the draft economic and social development plan for fiscal year 2024/2025 and the state budget draft, second legislative term, fourth session.

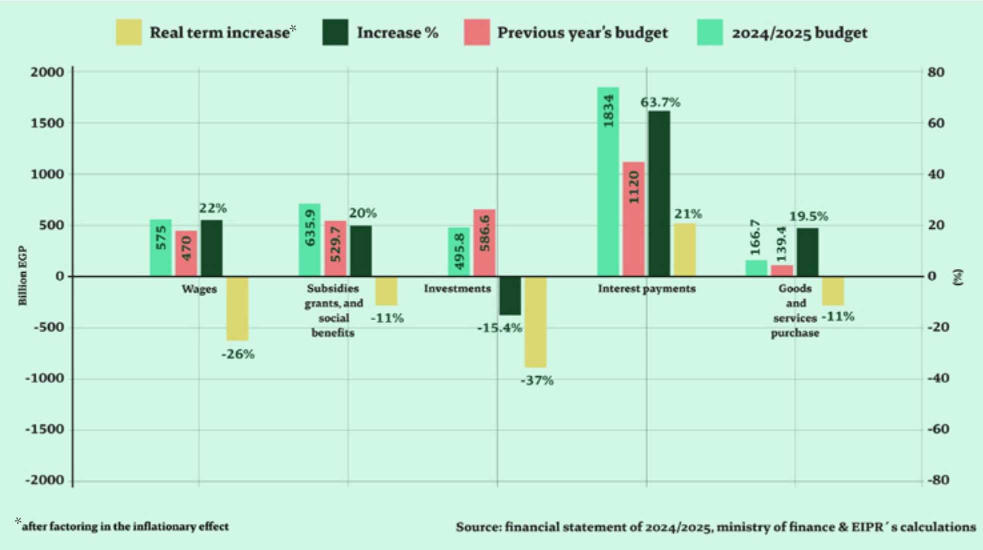
It is important to recall that the state has taken a series of policies and measures over the past ten years that put the Egyptian economy under tremendous pressure and increased its vulnerability to external crises, especially the large expansion of domestic and foreign borrowing in various forms, mostly for purposes that are neither productive nor of a vital and urgent nature. Nor are they directed towards human development, all of which has created increasing pressure on state finances and on hard currency resources, and opened the door to successive devaluations of the local currency and, consequently,successive waves of inflation.

The devaluation policy that the Egyptian government has followed since 2016 –in agreement with the International Monetary Fund (IMF)-- nwas one of the main reasons for the increase in the interest payments bill and debt installments bill due to the inherent dollar component in those payments. This policy was also one of the most important factors behind raising the interest rate to high levels to control the inflation that was, in turn, driven by the devaluation; thus the economy entered into a vicious circle from which it has not succeeded to escape until now.

Waves of inflation began in 2016, when the government implemented its first program with the IMF, and continued with the impact of the Covid-19 crisis and the Russian war in Ukraine. Then came the new loan agreement at the end of 2022, which emphasized the importance of exchange rate flexibility as a condition for obtaining the loan. The government allowed the devaluation of the local currency more than once within two years (March 2022 to March 2024), which came with all the anticipated consequences including rising inflation, higher interest rates, more fiscal deficit and borrowing to cover this deficit - all of which are likely to be repeated under the continuing implementation of IMF conditions.

As for transparency, the former Minister of Finance asserted after the approval of the budget that Egypt has progressed on all transparency indicators related to the budget[6], yet the most important document in clarifying the state's plan and economic direction is still far from being clear and creates a lot of confusion. This is evident to a great extent in what was introduced in the budget for the first time this fiscal year, the so-called "Combined General Government Budget", which includes data from the budgets of public economic bodies added to the data of the general state budget, a step that was taken at the request of the International Monetary Fund; so that all financial data of the state appear in the general budget. This is supposed to be a positive step that realizes the principle of budget unity, but in fact it was completely formalistic, as this new data was included in six tables, in which the figures differ from those used in all the budget sections. No explanation was introduced for the method of calculating this data and how it is reflected in the rest of the sections, making it difficult to understand the value of including this addition, except to fulfill a condition of the IMF in a rather cosmetic manner.

figure1: Expenditure and changes in real spending



6 Finance ministry press release, 5/6/2024, https://www.facebook.com/story.php?story_fbid=949068140596940&id=100064812882317&mibextid=WC7FNe&rdid=CsrRQghJXghOvJFv

Debt is tightening the noose:

The expansion of borrowing and disregarding the warnings of experts over the past years is not just a technical issue, as it directly harms the interests of the public and people's ability to utilize their resources. The allocations that will be directed in the new year to pay installments and interest on local and foreign debts alone account for nearly two-thirds of the total planned expenditure in the budget[7] at 62%, an increase of 6% from the previous year. Thus, the space available for spending on everything that affects the lives of citizens and helps develop the economy decreases year after year, as only 38% of the total allocations are left to fund wages, subsidies, purchase of goods, public investments, and other items.

The systematic and significant expansion of foreign debt in recent years has played a major role in the protracted crisis of the Egyptian economy. Loans have increased steadily over the past ten years, and began accumulating at a high rate after the signing of the loan agreement with the IMF in November 2016, jumping from 16.6% to 33.6% of GDP in one year, and the cost of servicing them in hard currency has obviously risen accordingly. If we track the value of Egypt's foreign debt over the past ten years, we find that it increased from $46 billion in June 2014 to $168 billion in December 2023, and its percentage of GDP during that period increased from 15% to about 43%. After the signing of the Ras Al Hikma deal in February, under which the UAE waived its dollar deposits in the Central Bank of Egypt, as we will explain later, foreign debt began to decline, reaching USD 160.6 bn in March.

The cost of repaying foreign debt installments increased by 110% in the new budget compared to the previous budget, with the decline in the pound's exchange rate against the dollar playing a major role in this increase.

The Egyptian government borrows to bridge the deficit between its revenues and expenditures, to pay domestic and foreign debt installments, and

7 In the Egyptian budget document, these are called "uses".

to finance projects that do not contribute to revenue generation[8] or reduce future expenditures in any way. These increasing loans over the years have not contributed to raising investment rates[9], whether total investment (which includes the private sector) or government investment alone.

The increase in foreign debt is causing a critical fiscal situation because it creates pressure to provide dollar liquidity to meet debt service obligations, including installments and interest, in a country where many of the hard currency resources are fragile in the face of external conditions, and due to increasing reliance on inherently unstable sources of hard currency, such as hot money. This is in addition to the increase in the amounts required to be repaid in less than one year to almost one third of the external debt[10].

Therefore, the failure to invest in developing sustainable and reliable dollar resources ultimately leads to crisis situations that usually end with a new devaluation, which in turn raises the cost of various spending items, and this vicious cycle continues to feed itself.

The devaluation of the local currency increases the value of foreign debt denominated in pounds, which automatically increases the value of public debt. The Minister of Finance has stated that every one pound increase in the price of the dollar against the local currency increases the burden on the budget by 110 billion pounds[11].

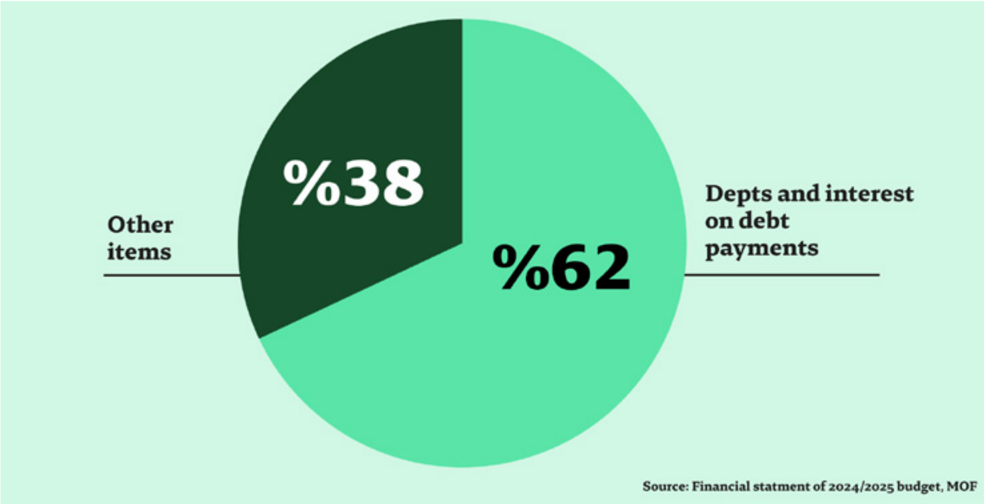
8 Ibrahim Awad, "In-kind or cash subsidies for food commodities," Al-Shorouk, June 6, 2024, https://www.shorouknews.com/mobile/columns/view.aspx?cdate=08062024&id=8f899da8-2b20-428c-9019-3109b805d1bd

9 Amr Adly, "When is borrowingare advances not 'damage'?", Al-Manassa website, https://manassa.news/stories/17376

10 External position of the Egyptian economy report, July/December 2023, vol 84, Central Bank of Egypt.

11 "Minister of Finance: Every pound change in the currency exchange rate by one pound corresponds to an increase of EGP 110 billion in debt," Al-Shorouk, February 15, 2024, https://shorturl.at/KaHkc

Figure 2: The percentage of debt and interest payments from total public expenditure



Selling to pay installments:

In response to the crisis of rising public debt and its service, the Minister of Finance confirmed that half of the revenues from the public asset sale program[12] will be used to directly reduce the government's debt and its service burdens. The ministry also announced that the Ras El Hikma transaction led to an increase in non-tax revenues to EGP 778 bn[13], a growth rate of 258%, during the period from July 2023 to the end of May, compared to the same period of the previous fiscal year.

The 2024 government asset sale program aims to raise between USD 1 to 1.5 billion by the end of the year[14].

12 "Minister of Finance. After the House of Representatives approved the new budget: Priority... Health, education, industry and agriculture," press release, Ministry of Finance website, June 4, 2024, https://shorturl.at/hYvxz

13 "State budget performance indicators in 11 months are better than targeted", press releasestatement posted on the Ministry of Finance website, June 11, 2024, https://shorturl.at/NQXgq

14 "Ministry of Planning: IPOs program targets $1 billion to $1.5 billion," Youm7 online, April 21, 2024, https://rb.gy/y9kpga

Egypt concluded a deal with the UAE last February[15], under which the Abu Dhabi Sovereign Fund (ADQ Holding) acquired the rights to develop the Ras El Hikma project on the North Coast for $24 billion to develop the area, in addition to waiving $11 billion of Emirati deposits at the Central Bank of Egypt, which represent part of Egypt's foreign debt, and converting them into local currency to invest in major projects in Egypt.

The dollar inflows made possible by the Ras al-Hikma deal helped alleviate the severe economic crisis that Egypt had suffered in the months leading up to its signing, mostly caused by the lack of dollar resources required to finance rising hard currency obligations to pay foreign debt service and arrears of foreign companies and importers. While the IMF agreement faltered due to Egypt's failure to commit to devaluing the pound, which fueled speculation on the currency and pushed the parallel market exchange rate to LE70 to the dollar.

The Ras al-Hikma deal allowed for a new compliance with the IMF's conditions and officially devaluing the pound, thereby obtaining a new loan from the Fund[16], followed by a package of international financing.

Egypt's pledges to the IMF included the commitment to spend the deal's funds "wisely" while prioritizing the increase of foreign exchange reserves, paying off arrears in hard currency and reducing public debt, as stated in the report of the first and second reviews of the IMF loan.

Thus, the sale of public assets or their exploitation rights has become one of the tools for debt repayment, which warns of real dangers if an urgent economic vision is not adopted to stop this bleeding and control the path of borrowing - especially foreign - with conditions that limit it to urgent development purposes. Such development purposes are supposed to directly reflect on improving the standard of living of the population or on projects capable of generating hard currency to ensure the possibility of repayment, or contribute

15 "UAE to invest $35 billion to develop Egypt's Ras Al Hikma city," Al Shorouk, February 23, 2024, https://www.shorouknews.com/news/view.aspx?cdate=23022024&id=166a2fc2-964b-4e81-808f-6edcfec9dc21

16 "Prime Minister announces signing an agreement with the IMF," Cabinet website, March 7, 2024, https://cabinet.gov.eg/News/Details/75379

an added value that justifies deducting part of the resources for debt service until the project achieves its goals. All of this should happen while placing this file under clear and rigorous parliamentary oversight.

Interest and the "siphoning" of resources:

Interest payments on domestic and foreign debt have risen in the new fiscal year to swallow up nearly half of all government expenditures that excludes debt installments. Interest payments accounted for 10.7% of Egypt's GDP, according to the budget, which is more than the percentages of wages, subsidies, education, and health combined.

In the first quarter of FY2023/2024, interest payments exceeded total government revenues[17], for the first time in ten years, reaching 142.5% of revenues. This ratio improved as revenues increased over the following months, and the interest payments reached 77% of revenues by the tenth month of the fiscal year. In the new budget, according to preliminary figures planned without shocks or changes in exchange rates, interest on domestic and foreign debt represents 70% of the EGP 2.625 trillion expected public revenues.

If we calculate the per capita interest payments on the bloated government debt, it amounts to EGP 17.2 thousand per year, while per capita government spending on health, for example, amounts to EGP 1,887 per year.

17 Mostafa Eid, "For the first time in 10 years,. dDebt interest payments exceed government revenues," Masrawy website, December 6, 2023, https://www.masrawy.com/news/news_economy/details/2023/12/6/2506306/%D9%84%D8%A3%D9%88%D9%84-%D9%85%D8%B1%D8%A9-%D9%81%D9%8A-10-%D8%B3%D9%86%D9%88%D8%A7%D8%AA-%D9%85%D8%AF%D9%81%D9%88%D8%-B9%D8%A7%D8%AA-%D9%81%D9%88%D8%A7%D8%A6%D8%AF-%D8%A7%D9%84%D8%AF%D9%8A%D9%88%D9%86-%D8%AA%D8%AA%D8%AC%D8%A7%D9%88%D8%B2-%D8%A5%D9%8A%D8%B1%D8%A7%D8%AF%D8%A7%D8%AA-%D8%A7%D9%84%D8%AD%D9%83%D9%88%D9%85%D8%A9-%D8%AA%D9%81%D8%A7%D8%B9%D9%84%D9%8A-#:~:text=%D9%88%D8%AA%D8%B2%D9%8A%D8%AF%20%D9%85%D8%AF%D9-%81%D9%88%D8%B9%D8%A7%D8%AA%20%D8%A7%D9%84%D9%81%D9%88%D8%A7%D8%A6%D8%AF%20%D8%B9%D9%86%20%D8%A7%D9%84%D8%AF%D9%8A%D9%86,%D8%AA%D9%85%D8%AB%D9%84%20%D9%86%D8%AD%D9%88%20142.5%25%20%D9%85%D9%86%20%D8%A7%D9%84%D8%A5%D9%8A%D8%B1%D8%A7%D8%AF%D8%A7%D8%AA.

While the depreciation of the exchange rate plays a role in increasing the interest burden of foreign debt, the bank interest rate plays the biggest role in the overall interest hike, leading domestic debt interest to reach EGP 1.6 trillion in the new year's budget.

Raising the interest rate is one of the traditional tools used to combat inflation, and so it has been raised several times over the past two years in tandem with successive devaluations of the pound exchange rate and the increase in inflation. However, given the conditions of the Egyptian economy, the impact of the interest rate on inflation has proven to be limited in comparison to its severe impact on state finances and public debt, which in turn leads to an ultimate increase in inflation.

The state is the largest borrower from the Egyptian banking system through the sale of bonds and treasury bills, which alone accounts for half of the interest payments in the new budget. The size of the state's domestic borrowing has increased continuously since 2011, while private sector borrowing from the banking system as a percentage of GDP has declined from 42% in 2008 to only 27% in 2020[18].

The insistence on this policy, which is also encouraged by the IMF as a means of curbing inflation, leads to the displacement of more resources from social and developmental spending to local and international banks and institutions lending the state, whose profits accumulate through this process.

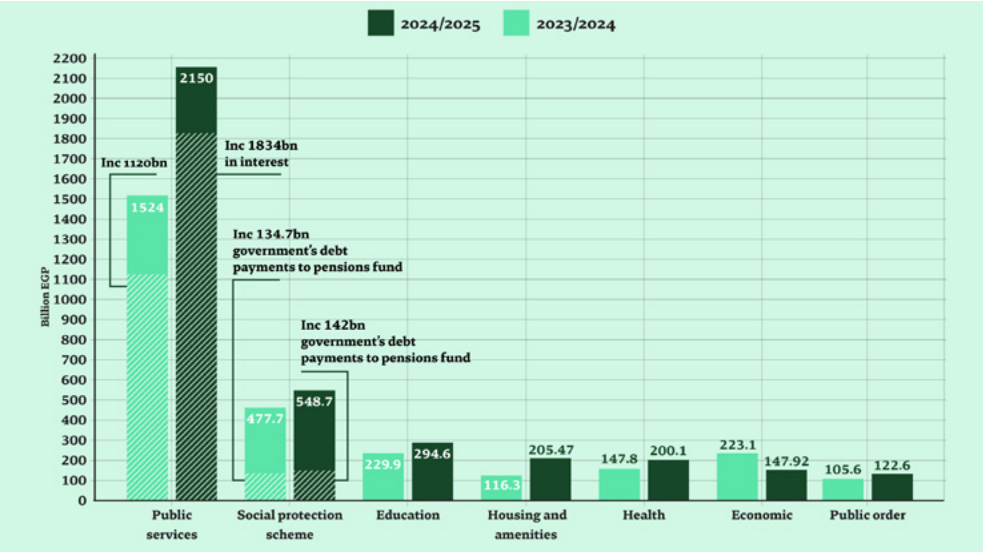
It is alarming to find that the total budget deficit, which represents the difference between public revenues and expenditures after excluding debt installments, is lower than the interest payments on the debt. The deficit amounted to EGP 1.243 trillion in the new budget, and 7.3% of GDP, while interest payments amounted to EGP 1.834 trillion, and 10.7% of GDP, illustrating the role of debt service in increasing the deficit. Thus, resorting to borrowing, which is always justified as a means to close the deficit, increased until its interest alone exceeded the value of the deficit.

18 Amr Adly, "Who bears the cost of the interest rate increase?", Al-Manasseh, January 2023, https://manassa.news/stories/8960

Excluding interest, the budget is running a primary surplus of 3.5%, which is portrayed as an achievement by the government since it is able to run a surplus if the debt disappears. The IMF values the primary surplus, while borrowing and debt service continue to rise year after year, making the surplus practically meaningless. The overall debt-to-GDP ratio in the new budget is between 96.4% and 101.9% (depending on how the relationship between the general government budget and economic entities is calculated).

In a positive move, the cabinet decided in March to set a debt ceiling of EGP 16 tn, equivalent to 96.4% of GDP, with the aim of gradually reducing the debt, based on recommendations from the International Monetary Fund (IMF). However, the ratio is still too high, requiring a different conceptualization of economic policies to reduce it, as well as the need to involve parliament in determining the debt ceiling and prioritizing the spending of borrowed funds, rather than the current situation in which the government alone handles this file without public oversight. The government was originally the cause of the debt crisis and spent the borrowed resources on projects that are neither productive nor income-generating, nor vital to improving the conditions of the population.

Figure 3: Spending Priorities



Source: analytical statment of 2024/2025 budget, MOF

Imbalance in spending priorities

According to the functional classification of the budget,[19] the section of "public services" has the first priority in expenditures, at EGP 2.1 trillion, accounting alone for 55% of expenditures. This item includes the expenses of the House of Representatives, the Senate, the Presidency, the Cabinet, Specialized National Councils, the General offices of governorates, the Central Auditing Agency, the Ministry of Foreign Affairs, and the Ministry of Finance and its various departments, led by the Public Debt Division in the ministry, which is responsible for inflating the expenses of this section of the budget because it includes debt interest payments of EGP 1.8 trillion.

However, the section named public services remains high on the list of spending priorities even after excluding interest, with EGP 316 bn allocation, second only to social protection.

Workers in sectors included herein receive a high share of wages and a significant share of public investments, amounting to 17% in the new budget, close to the share of economic affairs that includes commercial affairs, agriculture, irrigation, livestock production, mining, energy, tourism and telecommunications, which are areas that require a large investment budget, unlike the executive and legislative bodies included in this "public services" section. This percentage of investment allocation is still high, although it has seen a significant drop compared to the previous year, when it accounted alone for 39% of government investments. Last year's spike was likely related to the construction of government and legislative headquarters in the new Administrative Capital and New Alamein City.

Social protection came next to public services in the functional classification

19 The budget is classified according to three types of classifications: economic, functional, and administrative. Expenditures are classified according to the economic purpose into wages, subsidies, purchases, debt interest, and investments. The functional classification categorises expenditures according to the function they serve, and thus is divided into public services, health, education, culture, economic and commercial affairs, housing, public order, and social protection. The administrative classification shows the distribution of expenditures between governorates and administrative bodies.

of the budget, with EGP 548.7 bn, followed by education, housing and utilities, health, economic affairs, and public order and safety.

Despite the Finance Ministry's assertion that revitalizing the economy is one of the goals of the new budget, spending on economic affairs (which includes commercial affairs, agriculture, irrigation, livestock production, mining, energy, tourism, and communications) fell by 34% compared to the previous year, and was the only item to see a decline in allocations by this classification. Public investments directed to economic affairs fell by 45% compared to the previous year.

The state's spending on investment in general saw a decrease in the new budget by about 15%, and its share of GDP fell to 3%, in response to the IMF's demands to limit spending on public investments. This decline was reflected in many areas of spending, but some were unaffected, such as investment allocations for housing and utilities, which saw a significant increase of 82%.

The government continued to ignore the constitutional commitment to the minimum spending on education and health in the new budget. Education allocations increased by 28% in the budget compared to the previous year, but the ratio of this spending to GDP continued to decline to 1.72% instead of 1.94% in the previous year, sustaining its downward trajectory over the past years and moving further and further away from the constitutionally mandated percentages.

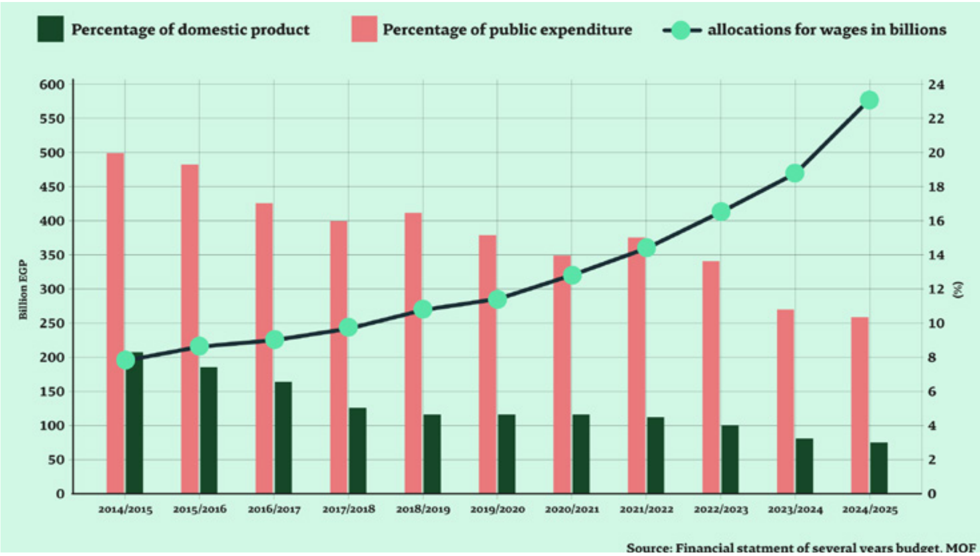
Health spending also saw a 35.4% increase in allocations from the previous year in nominal terms, but its share of GDP fell from 1.24% to 1.17%.

Egypt's 2014 constitution requires the government to increase spending on education and health to 10% of GDP within three years, making it a constitutional entitlement that must be implemented, in which university and pre-university education receive 6% of GDP and health receives 3%. However, what actually happened during this period was the opposite, as the percentages of these allocations were slashed.

President Abdel Fattah al-Sisi[20] admitted last year that the government was not complying with the constitutional minimum spending on education and health, two days after the finance minister at that time stated the opposite in the House of Representatives.

However, the financial statement for the new year's budget again insists on the state's commitment to the constitutional allocations, and provides figures for spending on education and health that differ from those provided in the budget details in the same statement.

Figure 4: Wages as a percentage of expenditure and GDP over 10 years



The share of wages continues to decline:

Wages in government spending have been on a downward trajectory over the past ten years, falling from 8.2% of GDP in 2014/2015 to less than half of that in the current fiscal year, reaching 3.4%.

The number of public sector employees has also declined during this period,

20 "For the first time: President admits government ignored constitutional education and health constitutional quotas," EIPR press release, June 17, 2023, https://rb.gy/sanpvk

dropping by 17% to 4.98 mn in 2022. However, the decline in wage spending was much larger than the drop in the number of employees, reflecting the austerity trend of fiscal policy designed to reduce social spending while expanding debt service.

Workers in the government sector, which includes the administrative apparatus, local administration and service delivery bodies, as well as the public sector companies and the public business sector, represent about 18% of the total labor force in Egypt, according to the latest data from the Central Agency for Public Mobilization and Statistics (CAPMAS).

Although spending on wages nominally increased by 22% compared to the previous budget, reaching EGP 575 bn, the real value calculation, which takes into account the rate of consumer price index increases, shows that real spending on wages decreased by 26% in the new budget.

But government workers do not suffer the same relative decline in the value of wages. The distribution of wages and benefits varies greatly depending on the sector they work in. Workers in the health sector, for example, account for EGP 95 bn of the wage budget, a sector that includes a large number of workers and service providers in Egypt's various governorates, while workers in the "public services" sector (the one mentioned in the section titled "imbalance in spending priorities") receive a comparable share of EGP 91.2 bn. This is allocated to a sector that has a significantly lower number of employees and includes senior state employees working in non-service legislative and executive bodies in the parliament, the Senate, the presidency, the prime minister's office, governorate general offices, and the ministries of finance and foreign affairs.

Workers in the administrative apparatus generally account for 42% of total wages spending,[21] but they count only 34% of government employees. They also have the largest share of additional wages, receiving about 87% of in-

21 Abdel Fattah Al-Gebali, "Reading the 2024/2025 budget-3 "'3', Al-Ahram website, June 5, 2024, https://gate.ahram.org.eg/daily/News/204878/4/944804/%D9%82%D8%B6%D8%A7%D9%8A%D8%A7-%D9%88%D8%A7%D8%B1%D8%A7%D8%A1/%D9%82%D8%B1%D8%A7%D8%A1%D8%A9-%D9%81%D9%89-%D9%85%D9%88%D8%A7-%D8%B2%D9%86%D8%A9--%C2%AB%C2%BB.aspx

centive bonuses, 71% of extraordinary efforts, and 61% of incentives for special-caliber workers. On the other hand, local government employees receive 43% of total wages, despite representing 55% of governmental employees, and receive much lower percentages of bonuses and incentives.

Subsidies, grants, and social benefits

Spending on subsidies, grants, and social benefits in the new budget increased by 20% compared to the previous year, reaching EGP 635.9 bn, but the real value of spending on this item fell by 11% due to the high inflation rates.

The share of subsidy spending in total public expenditures has declined over the past ten years, and its share of GDP has fallen from 8% in FY 2014/2015 to 3.7% in the new budget, within the framework of the financing programs Egypt signed with the IMF in 2016. The IMF always emphasizes the need to reduce spending on subsidies, especially energy subsidies as a source of imbalance in state finances, and because they "do not reach their beneficiaries", while cash subsidies directed to specific groups are better - accordingf to the IMF's vision - than generalized commodity subsidies[22]. The IMF repeatedly claims that reducing these "inefficient" subsidy allocations will generate savings for the budget that can be directed to improving social spending on education and health. Previous experiences, however,demonstrate that reducing subsidies, with all the associated reduction in living standards and increase in inflation rates, did not achieve this objective, and any savings resulting from these austerity measures were directed to debt service[23].

It is important to note that at least half of the subsidies allocations are in fact directed to areas far from social protection. This includes subsidies for industrial and agricultural activities, which actually include subsidizing real

22 IMF Country Report No. 24/98, Arab Republic of Egypt, First and Second Reviews under the Extended Arrangement under the Extended Fund Facility, Staff Report, April 2024.

23 Osama Diab, "The IMF and the End of Energy Subsidies in Egypt," Egyptian Initiative for Personal Rights, September 2023. https://eipr.org/sites/default/files/reports/pdf/sndwq_lnqd_ldwly_wnh_dm_ltq_fy_msr.pdf

estate taxes on buildings used in industrial activities for three years (ending in 2025), reducing cost of loan interest for industrial activities, subsidizing the price of electricity for factories, and subsidizing export promotion–this time alone accounts for EGP 23 billion of the subsidy allocations!

Nearly a quarter of the subsidy budget goes towards paying off the government's debts to social insurance funds. As for the subsidies for petroleum products, which amount to EGP 154.5 billion in the new budget, and account for 24% of the subsidy allocations despite all the programs adopted by the government to reduce them during the past years (and which in turn had a negative impact on living standards and increased prices), the bulk of it is in fact directed to the productive sectors. The family sector only benefits from one-fifth of petroleum product subsidy allocations[24].

In contrast to the six billion allocated by the state to subsidize electricity for industry, the electricity item included under commodity subsidies in the budget, which is where any consumer-oriented subsidies are supposed to appear, rose from zero in the 2023/2024 draft budget - which was amended to LE 2 billion before the end of the year - and then increased to LE 2.5 billion in the new year's budget. This amount is quite insignificant for the state's finances and is not at all proportionate to the government's repeated talking point[25] about how much the state bears to cover the differences in electricity prices provided to the domestic sector on behalf of citizens. This demonstrates a lack of transparency and insufficiency of public information, as figures that support the government's discourse do not appear in the budget document, and some figures in the budget explicitly contradict that discourse.

24 Salma Hussein, "The Four Mistakes Bill: The Egyptian-Fund plan to raise energy prices," Egyptian Initiative for Personal Rights, September 2020, https://eipr.org/en/press/2020/10/egyptian-initiative-personal-rights-launches-its-report-four-flaws-assessing-egyptian

25 "The Load-Shedding Struggle. Who pays the subsidy bills, the government or the citizen?", Akhbar Al-Youm, May 26, 2024, https://m.akhbarelyom.com/news/newdetails/4371767/1/%D8%B5%D8%B1%D8%A7%D8%B9-%D8%AA%D8%AE%D9%81%D9%8A%D9%81-%D8%A7%D9%84%D8%A3%D8%AD%D9%85%D8%A7%D9%84-%D9%85%D9%86-%D9%8A%D8%AF-%D9%81%D8%B9-%D9%81%D9%88%D8%A7%D8%AA%D9%8A%D8%B1-%D8%A7%D9%84%D8%AF%D8%B9%D9%85-

The prices of electricity provisions for consumers have jumped successively during the past years according to the state's plan to reduce subsidies, until the electricity prices became a heavy burden on individuals and families. The last price hike for electricity consumption segments was implemented in January 2024[26]. At the same time, recent power outages have sparked strong discontent among consumers[27], who are now paying a considerably high cost for a service they do not receive on a regular basis. The government has justified the increase in power outages by increasing consumption as a result of extreme heat waves and insufficient gas resources to cover the increased production of power plants, especially since imports from "neighboring countries" have been affected by technical failures, according to official statements[28].

Subsidized bread and food commodities:

The government announced a 300% increase in the price of subsidized bread a month before the start of the new fiscal year, a decision that sparked outrage due to its direct impact on the poor putting many of them at risk of actual hunger, in exchange for achieving financial savings in the budget, as the government justified the decision. This is despite the fact that those savings are

26 "Raising electricity prices in Egypt with new consumption segments 2024," Al-Masry Al-Youm, January 2, 2024, https://www.almasryalyoum.com/news/details/3067191

27 Mohamed El Kholy et al, "No Justice in Electricity Outages", Al-Manasseh website, June 25, 2024, https://manassa.news/stories/18187?fbclid=IwZXh0bgNhZW0CMTEAAR1K-KtMwXn7oVLI_wV4_UW2MI7dCAFHqf8EA_T9qFBaV0zs_TZuLVTERlt8_aem_GpLf4Kk27e2P3bfVPkFCvQ

28 "Gas production in a neighboring country is affected, Prime Minister reveals the reason for yesterday's worsening power cuts," Masrawy, June 25, 2024, https://www.masrawy.com/news/news_egypt/details/2024/6/25/2602470/%D8%AA%D8%A3%D8%AB%D8%B1-%D8%A5%D9%86%D8%AA%D8%A7%D8%AC-%D8%A7%D9%84%D8%BA%D8%A7%D8%B2-%D9%81%D9%8A-%D8%AF%D9%88%D9%84%D8%A9-%D9%85%D9%86-%D8%AF%D9%88%D9%84-%D8%A7%D9%84%D8%AC%D9%88%D8%A7%D8%B1-%D8%B1%D8%A6%D9%8A%D8%B3-%D8%A7%D9%84%D9%88%D8%B2%D8%B1%D8%A7%D8%A1-%D9%8A%D9%83%D8%B4%D9%81-%D8%B3%D8%A8%D8%A8-%D8%AA%D9%81%D8%A7%D9%82%D9%85-%D8%A3%D8%B2%D9%85%D8%A9-%D9%82%D8%B7%D8%B9-%D8%A7%D9%84%D9%83%D9%87%D8%B1%D8%A8%D8%A7%D8%A1-%D8%A3%D9%85%D8%B3

quite minor and have a limited impact on the budget. Bread subsidies account for a small percentage of government expenditure, especially when considering the high number of beneficiaries and the important role bread subsidies play in providing a minimum level of nutrition for the poorest and most in need.

In the 2024/2025 budget, bread subsidies amounted to EGP 90.7 billion, representing 1.6% of total public spending, and no more than 0.5% of Egypt's GDP. Citizens receive subsidized bread through ration cards, benefiting around 69.9 million people, according to the budget statement. The per capita bread subsidy is EGP 1298 per year (equivalent to USD 27 per person per year at the current exchange rate).

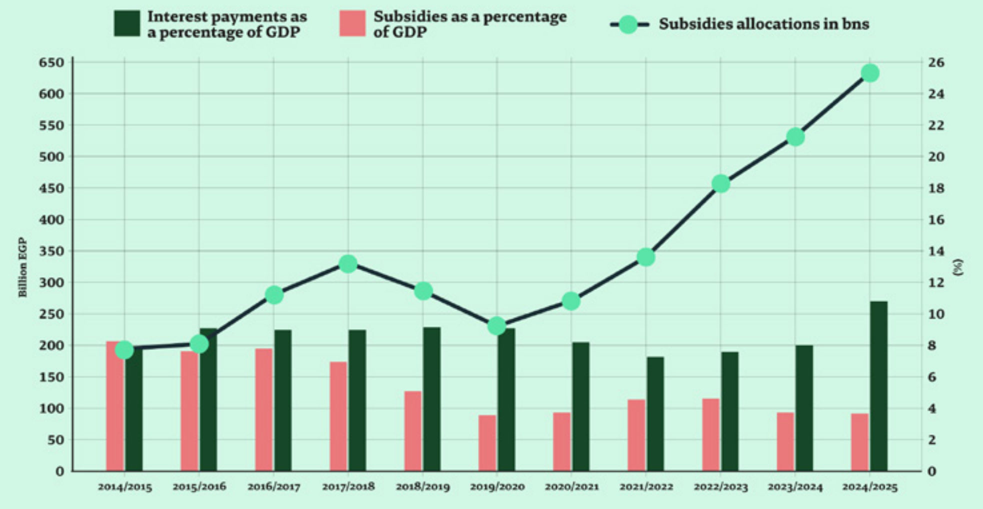
Egyptian citizens deserves this amount of subsidy, given that it is small compared to the per capita share of GDP, which is around 131.5 thousand pounds per year (assuming that output is distributed equally among the population), and in light of the state's important role in directing resources to ensure that the population realizes its economic and social rights.

Egyptians - especially the poor - rely on bread for their daily diet, and wheat has been responsible for providing about 39% of Egyptians' daily calories over the past years. The dependence of the poor on bread has clearly increased since the Covid-19 pandemic in 2020, as a result of their increasing inability to purchase other food commodities such as meat, vegetables and fruits. The consumption of wheat and its products, especially bread, increases with any inflation in the prices of other goods. Thus this recent increase in bread prices, any increase in the price of bread, leads to a reduction in the quantities consumed, which puts many poor Egyptians at risk of real hunger, and of not receiving the calories needed for their daily life to continue.

Although the amount allocated for bread subsidies in the new budget has increased by about EGP 7 billion, the real value of this subsidy after accounting for the impact of rising consumer prices has decreased by 26% compared to the previous year. According to EIPR's calculations,[29] the increase in the sale price of subsidized bread does not save more than EGP 11.5 billion annually, which is a small amount that could have been achieved from making cuts to many other items within the budget without compromising the most basic rights of the poor.

The bread subsidy falls under the ration subsidy item in the budget, which also covers the subsidy of other ration card goods, and which benefits 62.2 million individuals according to the financial statement of the budget. Under this umbrella each individual registered on the card receives goods worth EGP 50 per month, with a maximum of four individuals registered on the card. Families of over four individuals receive EGP 25 worth of commodities per month for every additional person. The total ration subsidy does not exceed 0.8% of GDP.

Figure 5: Subsidies share of GDP compared to Interest Payments



Source: Financial statment of the budget over several years budget, MOF

29 "Austerity is devouring Egyptians' livelihoods. The government removes the last rock protecting the poor," EIPR press release, May 30, 2024, https://www.eipr.org/press/2024/05/%D8%A7%D9%84%D8%AA%D9%82%D8%B4%D9%81-%D9%8A%D9%84%D8%AA%D9%87%D9%85-%D8%B9%D9%8A%D8%B4-%D8%A7%D9%84%D9%85%D8%B5%D8%B1%D9%8A%D9%8A%D9%86-%D8%A7%D9%84%D8%AD%D9%83%D9%88%D9%85%D8%A9-%D8%AA%D8%B2%D9%8A%D8%AD-%D8%A2%D8%AE%D8%B1-%D8%B5%D8%AE%D8%B1%D8%A9-%D8%AA%D8%AD%D9%85%D9%8A-%D8%A7%D9%84%D9%81%D9%82%D8%B1%D8%A7%D8%A1

Cash and commodity subsidies

The reduction of bread subsidies has reignited the debate over cash and commodity subsidies and which one is more economically and socially efficient, especially after recent government statements about a complete shift from commodity to cash subsidies[30].

Different views regarding this debate diverge according to the perception of the role of state in social protection. The basic premise of analysis in this paper is that the state role is to guarantee the basic rights of its citizens by directing the economy towards creating sufficient job opportunities, providing fair wages, and providing the kind of social protection for its population that market forces do not naturally provide, especially in a country where at least one-third of the population falls below the poverty line.

On the other hand, the policies that are actually formulated and executed change with the changing circumstances and are meant to respond to them. If Egyptians have been suffering in the last two years in particular from historically high levels of inflation that are putting increasing pressure on their standard of living in a way that they have not experienced in living memory, and which is difficult to adapt to for the majority of the Egyptian people and ends up pushing increasing numbers of them below the poverty line; these periods actually require the state to increase subsidies in all its forms and invest in improving its efficiency and sharpening targeting tools.. Rather than reduce and eliminate entire forms of subsidies.

Aside from the advantages and disadvantages of cash subsidies in general,

30 "The government's plan to switch to cash subsidies: A thousand pounds per person and increases in bread, fuel and electricity", Masrawy, 28 may 2024, https://www.masrawy.com/news/news_egypt/details/2024/5/28/2589722/%D8%AE%D8%B7%D8%A9-%D8%A7%D9%84%D8%AD%D9%83%D9%88%D9%85%D8%A9-%D9%84%D9%84%D8%AA%D8%AD%D9%88%D9%84-%D9%84%D9%84%D8%AF%D8%B9%D9%85-%D8%A7%D9%84%D9%86%D9%82%D8%AF%D9%8A-%D8%A3%D9%84%D9%81-%D8%AC%D9%86%D9%8A%D9%87-%D9%84%D9%84%D9%81%D8%B1%D8%AF-%D9%88%D8%B1%D9%81%D8%B9-%D8%A7%D9%84%D8%AE%D8%A8%D8%B2-%D9%88%D8%A7%D9%84%D8%A8%D9%86%D8%B2%D9%8A%D9%86-%D9%88%D8%A7%D9%84%D9%83%D9%87%D8%B1%D8%A8%D8%A7%D8%A1

times of high inflation and frequent devaluation are not the best to implement this system in any case, as the real value and purchasing power of the money that beneficiaries will receive will depreciate rapidly. While this speedy depreciation takes place, the amount of the cash subsidy is re-evaluated and adjusted very slowly. and is certainly not commensurate - and that is the case in any direct cash subsidy system - with the inflationary impact of frequent devaluations of the currency exchange rate. Commodity subsidies, on the other hand, guarantee access to a minimum number of goods that provide the required calorie intake for the majority of citizens, preserving the general health of the population as a basic right, as well as their productive capacity.

This was already partially demonstrated with the transformation of the ration subsidy system into a predetermined monetary value for each beneficiary, who will receive goods equivalent to this value only, after previously guaranteeing direct access to a specific number of goods. The goods provided in the subsidy system were those that provide minimum food security such as oil, rice, and sugar. As a result of this change, the amount of goods that beneficiaries receive has decreased and is likely to continue to decrease as prices increase at rates much higher than subsidy increases.

The state provides cash support to the poorest families under the Takaful and Karama programs, in addition to the social security pensions. These cash transfers are included in one line item in the budget, which is allocated EGP 40 billion and covers 5,2 million families, according to the government's financial statement. These allocations account for 6% of the total subsidies budget, while their share of GDP does not exceed 0.2%.

Families receiving the Takaful pension receive EGP 736 per month, in addition to a per-pupil grant ranging from EGP 75-125 for a maximum of three pupils per family.

Karama provides EGP 708 per person, with a maximum of 3 members per family.

The Social Security Pension provides EGP 535 per person, increasing to EGP 745 for a family of four or more.

The amounts provided in cash support programs are subject to erosion as price levels rise and the value of the currency declines, while there is no provision to ensure that those amounts are increased according to or linked to the inflation rate. In fact, they have always remained below the official poverty line even after being increased more than once over the past two years.

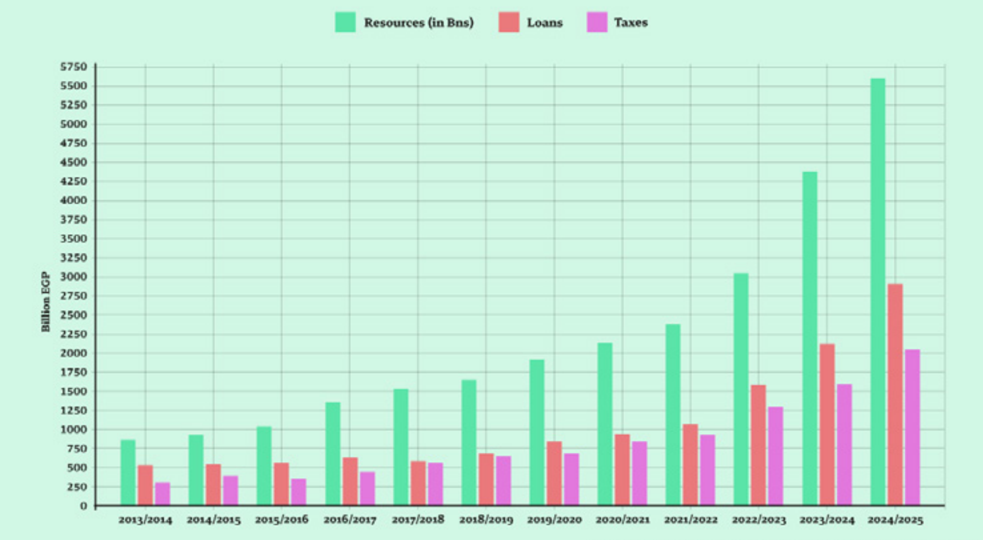
The value of the national poverty line was 857 pounds per month per person in 2019/2020, according to the latest published income and expenditure survey[31], and the average family size in this survey was 4 members, which means that a family needed 3462 pounds per month in order not to fall below the poverty line.

The statistics authority did not release the latest data on incomes and expenditure at the time of publishing this paper, although it is supposed to be published every two years, but attempting to calculate this amount in light of the escalating inflation rates from then until now - according to official inflation data - the poverty threshold for a family becomes 5557 pounds per month at the very least.

Following the devaluation of the pound (from 8.9 to 16 pounds to the dollar) and the increase in the price of government goods and services in 2016, the number of poor people increased by about five million. The number of poor people is expected to increase even more following the recent wave of inflation, especially since the purchasing power of the pound has seen a much greater deterioration over the past two years, having fallen from 16 to about 48 pounds to the dollar. This means millions more will be in dire need of subsidies.

31 Income, Expenditure and Consumption Survey, Central Agency for Public Mobilization and Statistics, 2019/2020

Figure 6: Evolution of total revenues, borrowing and taxes over 10 years



Revenues and taxes

When looking at the other side of the budget, the resources that the state relies on to finance planned expenditures in the new fiscal year, we find that the issue of borrowing takes centre stage in this aspect as well. Projected tax revenues cover only 36% of total expenditure, while the government plans to borrow EGP 2.8 trillion, equivalent to 51% of the required resources in 2024/2025. This means that debt repayment allocations will continue to rise over the coming years, at the expense of all other items required to meet the needs of the population and develop the economy.

If we exclude loans from the calculation, we find that taxes account for 77% of what is called "revenues" in the budget, which is the part that covers expenditure excluding loan repayments. This means that the bulk of the new debt to be borrowed is to pay off old debt installments (56% of new debt is earmarked for paying off old debt), which means we are trapped in a vicious cycle that does not end, but rather continues to grow.

The rest of the borrowing planned for the new year is intended to cover the budget deficit (the difference between expenditures and revenues), which -

not coincidentally - is more than two-thirds the value of debt interest payments, meaning that the deficit to be covered is also debt-driven.

Interest on domestic and foreign debt will take up 91% of projected tax revenue in the new fiscal year. This means that taxpayers are actually financing the profits of the state's lenders - banks, individuals, and corporations - at home and abroad.

Improving state finances and reducing reliance on borrowing requires a fairer and more efficient tax system. Taxes are supposed to be the main source of funding in the state budget, but their collection in Egypt is low given the size of the economy and compared to similar countries in the world, since taxes as a percentage of GDP amount to only 11.8%.

The meagre revenue from taxation can be partly attributed to the state's policy and ideological priorities. As the new budget shows (and previous ones as well), the state does not collect sufficient or commensurate taxes from companies and individuals who make large gains and profits. Those gains necessitate that they pay appropriate tax for their use of resources and in order to achieve a measure of social justice. Nor does the state collect adequate tax from the owners of real estate wealth, which has become the largest store of value in Egypt. The state resorts to expanding the collection of taxes from the hard-earnings of individuals who do not make such profits or accumulate wealth, either directly, as in the salary tax, or indirectly on the goods and services they consume such as the value-added tax, which is collected at equal rates for everyone regardless of disparities in income and wealth.

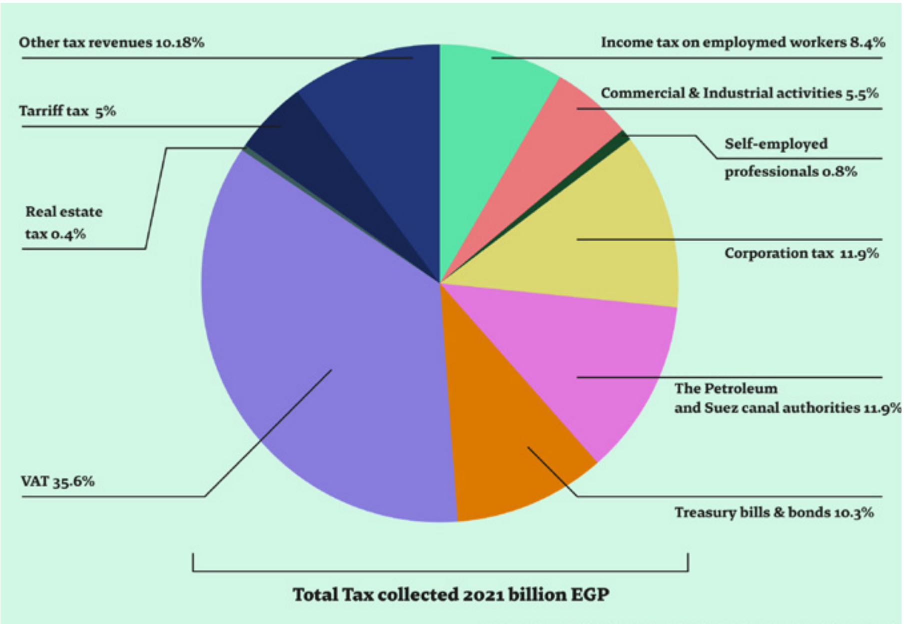
Consumers and wage-earning individuals fund 44% of the total tax collection this year, while profit-making companies contribute only about 12% of this collection, the Suez Canal and the Petroleum Authority (and its foreign partners) contribute 12% of the total taxes, and 10% of the collection comes from taxes on treasury bills and bonds.

Taxes on commercial and industrial activity contribute no more than 5.5% of tax revenue, and the share of the self-employed (doctors, engineers, lawyers, etc.) dwindles to just 0.8%.

Meanwhile, capital gains taxes on stock market transactions remain unenforced a whole ten years after the law was enacted. Its implementation "pause" was extended under the influence of influential stakeholders in this field, despite its fairness as a tax on non-productive profits and its ease of collection compared to other taxes that require inventory and are difficult to obtain data - making it an easy and logical way to maximize tax collection in light of the current economic crisis.

As for real estate taxes, which are considered one form of wealth taxes, the government expects to collect from it only 0.4% of the estimated revenue for the new year, worth only LE 8 billion, at a time when the sale price of a single villa in some areas has reached half a billion pounds[32], as wealthy people increasingly invest their money in real estate whose prices are doubling year after year.

Figure 7: Who finances Taxes in 2024/2025 Budget?



32 The most expensive villas in Egypt, some are up to EGP 775 million, Alarabiya online, 11 December 2023, https://www.alarabiya.net/aswaq/special-stories/2023/12/11/%D8%A3%D8%BA%D9%84%D9%89-%D9%81%D9%8A%D9%84%D8%A7%D8%AA-%D9%81%D9%8A-%D9%85%D8%B5%D8%B1-%D8%A8%D8%B9%D8%B6%D9%87%D8%A7-%D9%8A%D8%B5%D9%84-%D8%B3%D8%B9%D8%B1%D9%87-%D8%A7%D9%84%D9%89-775-%D9%85%D9%84%D9%8A%D9%88%D9%86-%D8%AC%D9%86%D9%8A%D9%87

This pattern in distribution of the sources of tax revenue reflects a waste of resources and possibilities on the one hand, and a major breach of tax justice on the other, as the state expands the collection from the safest parties that have no chance or means to evade collection, and that are not represented by interest groups or any organised force that can lodge objections and resist taxation. Those parties include regular contract-employees and average consumers of goods and services. This leaves plenty of room to increase tax collection from those who make huge profits but require more effort to collect - but at the same time, are more capable than the average citizen of lobbying to protect their material interests and influence tax policy in that direction.

The International Monetary Fund (IMF), in its current partnership with the government on economic policymaking, is also contributing to this pattern and strengthening its hold. In its review of Egypt's loan, the IMF emphasizes that Egypt's tax revenues are low compared to countries in the same income bracket, but also highlights opportunities to increase the VAT, which "would add as much as 1 percent of GDP to tax revenues."

In its latest review, the IMF explains that the government will submit in November an amendment to the VAT law, as part of the program agreed between the two parties, that will increase the efficiency of VAT collection and reduce the number of goods and services that are excluded from it. Because this tax burden is typically passed on from the producer to the end-consumer, it contributes directly to higher levels of consumer price hikes. Thus, the most appropriate decision at a time of high inflation that is difficult to get under control, like the inflationary wave Egypt is currently experiencing, would be to lower the VAT, not raise it. Especially since VAT already provides the state with three times as much revenue as profitable companies!

Eight years ago, the IMF confirmed in the assessments of its 2016 loan program that corporate tax revenues were too low and that increasing them was necessary to improve resources, but when it pressed the government for not adhering to some agreed-upon steps to maximize tax revenues, its political pressure was in fact limited to the imposition of the VAT without addressing other aspects of tax policy. Meanwhile, in the IMF's most recent report on the latest loan, corporate taxation was completely absent!

In fact, the tax system, as revealed by its sources of revenue, is a microcosm of the priorities and political biases of the budget as a whole. Consumers and wage earners bear the brunt of the burden, in contrast to meagre tax burdens on property and wealth owners, stock market speculators, high-income earners, senior professionals, and even finance and trading companies. This in turn multiplies the impact of austerity on social policies. Instead of playing a major role in reducing poverty and social inequality, tax policy ends up contributing to deepening inequality and social vulnerability.