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# Policy Note

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## Toward More Job-Rich Growth: The Case of Egypt

Moheb Said and Chahir Zaki

### About the authors

Moheb Said is an independent researcher

Chahir Zaki is a Professor, Faculty of Economics and Political Science, Cairo University and ERF Research Fellow

### In a nutshell

- This policy brief presents developments at both the macroeconomic and microeconomic levels just before and during the COVID-19 pandemic.
- It also shows how the structural characteristics of the Egyptian economy have exacerbated the negative effects of the pandemic, as well as how some cyclical developments have worsened the situation.
- Deeper and more structural reforms are needed in order to enable the Egyptian economy to create more and better jobs.

### Why Was the Economy Unable to Create Jobs? A Macroeconomic Perspective

The consequences of the pandemic caused the global gross domestic product (GDP) to decrease by 3.6 percent in 2020 compared to 2019. At the macroeconomic level, however, some countries in the Middle East and North Africa (MENA) region, such as Egypt, have been more resilient than others. In fact, Egypt's growth rate reached 3.6 percent in the 2020 fiscal year.<sup>1</sup> Despite the country's macroeconomic resilience, thanks to the different stabilization policies adopted between 2014 and 2016 (Zaki, 2017), most of its structural problems at both the macroeconomic and microeconomic levels have not been addressed, which has affected the ability of the Egyptian economy to generate jobs and foster more sustainable economic growth (Amer et al., 2021).

<sup>1</sup> Egypt's national accounts follow a fiscal year calendar that starts in July of the previous year and ends in June of the current year.

At the macroeconomic level, five main challenges can be identified, three of which are structural while the other two are cyclical. Firstly, we observe that economic growth is chiefly led by capital-intensive sectors such as petroleum, construction, and communication, which witnessed significant growth rates following the pandemic. This was at the expense of the non-oil manufacturing and tourism sectors, which were largely affected by the disruption in supply chains as well as the decrease in exports and investments. This explains why newly created jobs were rather modest, even after the recovery from the pandemic.

The second structural obstacle is the crowding-out effect associated with the increase in domestic credit provided by financial institutions to the government and the decrease of those in the private sector between 2010 and 2020. The increase in domestic credit provided by the financial sector to the government (from 64 percent in 2017 to 67 percent in 2020) was associated with a simultaneous decrease in credit to the private sector (21 percent, down from 24 percent over the same period). Such government credit was mainly used to finance the fiscal deficit and the domestic debt. Yet, it is important to note that the long-term trends show stronger changes, given that the share of public credit increased from 49 to 67 percent between 2010 and 2020. In contrast, private credit decreased from 42 to 21 percent over the same period. Thus, less liquidity has been made available for the private sector, which has affected its contribution to domestic investment and growth, as will be shown later. Third, with the deteriorating investment climate (practices of the informal sector, corruption, tax administration, tax rates, and customs and trade regulations), domestic investment is still far from its contribution potential to growth and thus employment.

At the cyclical level, exports and investment have been volatile due to lower demand from Egypt's main trade partners (mainly European and Arab countries) following the pandemic. Moreover, external debt has been rising substantially with the increase in foreign reserves, thereby adding more pressure on Egypt's foreign currency, which was already affected by the decrease in tourism, exports, and foreign direct investment (FDI). Indeed, the share of external debt in

national income increased from 21.1 percent in 2016 to 37.2 percent in 2020. Moreover, between 2019 and 2020, the share of short-term debt to foreign reserves increased from 20.7 to 30.7 percent, putting further pressure on Egypt's foreign currency (pressured by the decrease in tourism, exports, and FDI). This led the Egyptian government to announce the floatation of its currency in October 2022 and conclude another loan with the International Monetary Fund (IMF) and other international financial institutions amounting to USD nine billion (IMF, 2022).

These macroeconomic developments made the economy relatively less resilient and explain why the quantity and quality of jobs created were rather modest after the pandemic at the microeconomic level.

## What Are the Characteristics of the Egyptian Labor Market?

In order to analyze the labor market developments at the microeconomic level, quarterly data of key labor market indicators are analyzed to observe pre-COVID-19 trends and the impact of the pandemic following the first quarter of 2020, and also to track potential recovery signs. The two main data sources for this section are the Egypt Labor Force Survey (CAPMAS, 2018, 2019, 2020, 2021) and Open Access Microeconomic Data Initiative (OAMDI, 2018, 2019, and 2020). This analysis relies on two sets of indicators. The first set describes the labor market from a quantitative perspective through the change in labor force participation, employment-to-population, and unemployment rates.<sup>2</sup> The second set includes other measures that assess the quality of the labor market, namely informal employment, time-related underemployment, and youth not in employment, education, or training (NEET).

COVID-19 appears to have only exacerbated existing labor market challenges, including relatively low labor

<sup>2</sup> In this chapter, labor force participation and employment-to-population rates are defined for the 15-64 age group, whereas in the CAPMAS Labor Force Survey Bulletin 2021, these rates are defined for the age group 15 and above.

force participation rates and employment-to-population ratios as well as a relatively high unemployment rate, especially among youth and women. The good news is that these labor market indicators were able to largely recover from the repercussions of COVID-19 and have returned to pre-pandemic levels. Yet, lower levels of educational attainment continue to be associated with lower participation rates, except for illiterate males. Moreover, it can be observed that while male unemployment rates fluctuated between 4.3 and 8.6 percent over the period, female unemployment rates varied between 22.5 and 16.4 percent. Despite the disparities in levels, the pandemic had a larger impact on men, where male unemployment rates more than doubled in the second quarter of 2020, reaching 8.6 percent compared to 4.3 percent in the second quarter of 2019. In contrast, female unemployment decreased in the second quarter of 2020 (16.4 percent) and the third quarter of 2020 (15.4 percent) compared to 23.1 percent in the third quarter of 2018. However, there is no evidence that more women actively joined the labor market, as female labor participation rates also decreased during the same period.

From a qualitative perspective, first, Egyptian youth NEETs continue to be one of the major challenges, especially women. More than a quarter of Egyptian youth (26.3 percent) were neither employed nor enrolled in education or training by the fourth quarter of 2020. The youth NEET rate among females reached 45.8 percent in the fourth quarter of 2020, which is more than five times higher than the rate for their male counterparts (8.1 percent). Males almost returned to pre-pandemic levels, while the number of young women NEETs has been steadily rising. The dual decrease in labor force participation and NEET rates among females highlights the discouraging impact of COVID-19 on Egyptian women, especially youth. This finding confirms the existence of important disparities between genders and suggests that the impact of COVID-19 has not been the same across different groups.

Second, the time-related underemployment rate, which is defined as the share of persons in employment working less than 35 hours per week, wanting to change work, and/or wanting additional work, has

increased during the pandemic. Female workers recorded lower time-related underemployment rates than males over the period. The time-related underemployment rates reached 5.1 percent among males and 3.2 percent among females in the fourth quarter of 2020, compared to 1.4 percent and 0.7 percent, respectively, in the fourth quarter of 2018.

Finally, informal employment has been increasing. Throughout 2018–20, a continuing expansion can be seen in the share of informal economy workers, especially among males. By the fourth quarter of 2020, 40 percent of Egyptian workers were informal economy workers, 20 percent worked for the public sector, 16 percent were self-employed, 11 percent were private formal wage workers, and those remaining were employers (6.8 percent) and unpaid family workers (5.8 percent).

## The Way Forward: Creating More and Better Jobs

Although different macro-stabilization programs made the Egyptian economy resilient during the pandemic, they have not helped address the deep-rooted causes of Egypt's structural problems related to employment and inclusive growth. This suggests the need to shift the focus to more structural policies rather than stabilization policies. This includes a special focus on the following policies:

### A consistent industrial policy

Reforms must be directed toward labor-intensive sectors to create more jobs (especially for youth and women) and thus stimulate the economy. Second, in order to increase both domestic and foreign investments, enhancing the business climate – along with facilitating access to finance, competition, land, and energy, especially for small and medium-sized enterprises – should remain at the top of the reform agenda. Some reforms have already started with the structural reforms program that was implemented by the Ministry of Planning and Economic Development

in 2021–24. This program aimed to enhance the efficiency of the labor market, technical and vocational education, and training, in addition to promoting the role of the private sector and removing trade obstacles in order to create a supportive and enabling environment for competition. Yet, a consistent industrial strategy is needed to boost the competitiveness of the manufacturing sector. This strategy must consider the supply-related factors that take into account the country's comparative advantage over demand-related factors (measured by global import growth rates). The priority sectors must be where Egypt has a high comparative advantage and high global demand, as Egyptian supply aligns with global demand. It includes the chemical industries, wood and paper, processed foods, metals, agricultural products, and electrical and electronic products sectors. Given that most of these sectors are labor intensive, they are likely to generate more jobs.

### A fairer competition policy

There is a need to develop a transparent state ownership policy and governance framework in order to enable the private sector to make informed investment decisions and reduce uncertainty. This can take place by making financial and operational information on the activity of state actors available. It is also crucial to separate the commercial and non-commercial activities of state actors and require state-owned enterprises to fully recover the cost of commercial activities (Youssef and Zaki, 2022). In the same vein, limiting exclusions from laws and tax exemptions for state actors will make different sectors more competitive and thus increase the role of the private sector in the economy and in generating jobs. Finally, there is a dire need to separate the roles of state actors as regulators from operators to resolve potential conflicts of interest.

### Creating fiscal space for financing universal and adequate social protection

Creating fiscal space for social protection is a key factor not only in building universal, comprehensive,

and sustainable social protection systems, but also in ensuring adequate social protection benefits for all in accordance with the International Labour Organization's (ILO) social security standards and the UN 2030 Agenda for Sustainable Development (ILO, 2021). Countries need to invest more and better in social protection based on principles of universality, adequacy, sustainability, and solidarity (Bierbaum and Schmitt, 2022). International experience shows that countries can draw on eight different strategies for creating fiscal space (Ortiz et al., 2019). These are: (1) expanding social security coverage and contributory revenues; (2) increasing tax revenues; (3) eliminating illicit financial flows; (4) improving efficiency and reallocating public expenditures from less socially desirable areas; (5) tapping into fiscal and foreign exchange reserves; (6) borrowing or restructuring debt; (7) adopting a more accommodative macroeconomic framework; and (8) increasing aid and transfers. Each country is unique, and the design and implementation of social protection systems need to be carefully examined and decided upon in national social dialogue – and the same applies for financing options, including the potential risks and trade-offs associated with each opportunity (ILO, 2022).<sup>3</sup> It is therefore of utmost importance that social partners contribute to the formulation and implementation of national social protection policies in line with ILO social security standards.<sup>4</sup> Experience shows that informed policy design improves implementation effectiveness and contributes to the ownership of the measures adopted as well as trust amongst tripartite actors and workers in general.

### A more proactive social policy

During the pandemic, the Ministry of Social Solidarity allocated more funds to support 60,000 families through

<sup>3</sup>For more details on creating Egypt's fiscal space, see the new public expenditure review published by the World Bank (2022).

<sup>4</sup> In June 2022, the ILO launched a ratification campaign on Social Security (Minimum Standards) Convention, 1952 (No. 102) and other ILO social security standards and developed a toolkit with the aim of raising awareness and increasing their impact and application in national contexts. The toolkit provides very practical and useful insights as to the ratification procedure, model instruments of ratification as well as interactive information on the relevance and key provisions of these standards. For more information, see <https://www.social-protection.org/gimi/Standards.action>

its Takaful and Karama programs. Second, the Ministry decided to include women over the age of 65 under the umbrella of the social security scheme. Moreover, following the directives of Egypt's President, the Ministry of Manpower announced that an exceptional allowance of EGP 500 for irregular workers would be disbursed for three months. While these measures can help reduce the negative effects of the pandemic on vulnerable categories, social policies remain largely reactive rather than proactive. Therefore, more proactive policies that provide workers with social security and help them get promoted to get out of vulnerability are necessary. In addition, it is important to adopt a more bottom-up approach where social partners and civil society organizations participate in both the design and implementation of different policies.

#### A more sustainable exchange rate policy

The Central Bank of Egypt announced the adoption of a free-floating exchange rate regime in October 2022 as one of the conditions of the recent IMF loan. Thus, this policy must be more sustainable in the medium term to avoid managing an overvaluation of the Egyptian pound to reduce the burden on foreign exchanges and on the real sector, which has to adjust to keep the currency stable. While this is necessary to improve the competitiveness of exports, more reforms are needed to foster and diversify domestic production and remove administrative and unjustified non-tariff measures that affect exports and therefore production and job creation (Youssef and Zaki, 2019).

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#### Contact Information

##### ERF Office

**Address:** 21 Al-Sad Al-Aaly St. Dokki, Giza, Egypt  
 PO Box 12311  
**Tel:** +202 333 18 600 - 603  
**Fax:** +202 333 18 604  
**Email:** erf@erf.org.eg  
**Website:** <http://www.erf.org.eg>

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#### Contact Information

##### ILO Cairo

**Address:** 13 Brazil St. Zamalek, Cairo, Egypt  
 PO Box 11211  
**Email:** [adwa@ilo.org](mailto:adwa@ilo.org)

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