It is over a year now since Egyptians embarked on a new political, social, and economic path after toppling former President Hosni Mubarak during the 25 January 2011 revolution. Such a momentous development, that is expected to transform Egypt to become a transparent, accountable, and socially and economically prosperous country, has not only challenges but also opportunities.

Egyptians continue to resolve several multifaceted challenges faced by their country. Recently, they successfully concluded Presidential elections, and are working towards drawing a new Constitution. A successful settlement on the political front is a fundamental pre-requisite for Egypt to turn around its economy to a sustainable and equitable growth path that would create jobs for its many unemployed youth.

Key Highlights of this Report

- **Economic Growth (GDP)** dropped to 0.4% over the period July-December 2011/2012 (July-June), against 5.5% growth in the first half of 2010/2011, because of the political unrest after the revolution.
- **Unemployment Rate** climbed to 12.4% during the fourth quarter of 2011 (calendar year), compared to 8.9%, in the fourth quarter of 2010.
- **Consumer Price Inflation (CPI)** climbed to about 9% in March 2012, compared to 7% in October 2011, because of the impact of a depreciating domestic currency on imported food commodities.
- **Regarding Monetary Policy**, the Central Bank of Egypt in April 2012, lowered the reserves requirement on deposits in local banks from 14% to 12%, and effective 26 June 2012, has further reduced the requirements to 10%.
- **Domestic Currency Exchange Rate (EGP/US$)** continued to slowly depreciate to EGP 6.04 at the end of March 2012, compared to EGP 5.96 a year earlier.
- **Net International Reserves** that stood at US$ 36 billion (bn) in December 2010 declined to US$ 15.1 bn at the end of March 2012.
- **Balance of Payments** posted a deficit of US$ 5.65 bn by end of the October-December 2011/12 fiscal year, compared to a deficit of US$ 2.36bn at the end of the previous quarter.
- **Budget Deficit** reached 7.2% of GDP, during the period July-March 2011/12, compared to 6.9% of GDP for the period July-March 2010/11.
- **Domestic Public Debt** climbed to 75.4% of GDP by the end of March 2012, compared to the December 2011, level of 72.2% of GDP because of increasing yield on government Treasury-bills.
- **External Debt** decreased by 0.9% to US$ 33.7 bn at the end of December 2011 compared to the September 2011 position.

Overview

This brief was prepared by Charles Muthuthi (Chief Country Economist, EGFO) with inputs by Noha El Demery (Consultant, EGFO) under the supervision of Sibry Tapsoba (Resident Representative, EGFO).
Economic Growth

Egypt’s economy continues to recover from the adverse shocks of the January 2011 revolution, but the speed and trajectory of the recovery is weak and uneven. Historically, from 2006 until 2010 Egypt’s average annual GDP was about 6% (Chart 1). Real GDP growth (at 2006/2007, July-June, market prices) improved to 0.4% by the end of the second quarter of 2011/2012 (October-December) from a growth rate of 0.2% in the previous quarter, and after a weak third quarter of 2010/2011 when the economy contracted by 4.3%. Despite the positive signs, recent data released by the Egypt’s Ministry of Finance reflects a lackluster recovery because of the ongoing political uncertainties.

While private consumption that comprises about 75% of GDP is supportive of the Egypt’s economic growth, other economic indicators on the expenditure side, such as investments, and exports continue to be subdued (Chart 2). Private consumption, expanded by 5.3% during the first half of 2011/12 (July-December), broadly maintaining levels achieved over the period 2006/07 to 2009/10. This provided the principal impetus to GDP growth that at constant prices stood at Egyptian pound (EGP) 460.1 billion (bn) during the period July-December 2012 compared to 458.6 bn during the period July-December 2011.

Less favorable data on consumer spending indicate that Egyptians are increasingly getting concerned about the deteriorating economic situation. Notably, the consumer confidence index —by the Egyptian Cabinet’s Information and Decision Support Centre (IDSC)— dropped by 4.4% to 96 points in April 2012, from the previous month. This demonstrates that private consumption is increasingly getting constrained by perceptions of Egyptian that their incomes are falling.

Investments showed little vigor of rebound after contracting by an annual average of 4.2% during the post revolution period, from April 2011 to December 2011. The contraction of investments continued during the period July-December 2011/12, when gross capital formation declined by 3.5%. Exports of goods and services that contribute about 25% of GDP, contracted by 4.7% during the first half of 2011/12, while government spending, that comprises about 11% of GDP, grew by only 2.9% in the same period.

Value added in all sectors, except agriculture, government, and Suez Canal posted negative growth during the period July-December 2012 (Charts 3 and 4). The agricultural sector remained relatively resilient, growing by about 3% in both July-December 2011/12, and July-December 2010/11 periods, because of the support the sector receives from the government. Suez Canal sector expanded by 7.2% during the period July-December 2012, compared to 11.1% in the previous period, mainly because of the sluggish performance of world trade.
The sectors that shrunk sharply during the period July-December 2010/12 period included tourism (-8.6%; growth in 2010/11 was 13.9%), construction (-1.6%; growth in 2010/11 was 12.6%), and manufacturing (-3.1; growth in 2010/11 was 6.1%), because of the adverse effects of political uncertainties on Egypt’s economic output. The contraction in economic activity is reflected in the slowing down of the private sector activity (which accounts for 63.3% of GDP) by 0.1% during the first half of 2011/12 compared to the same period last year. The public sector, however, remained supportive by moderately expanding by 1.2% during the same period.

Employment and Unemployment

Against the backdrop of deteriorating economic conditions, employment creation stagnated. As a result, the Central Agency for Public Mobilization and Statistics (CAPMAS) reported in February 2012 that unemployment rate had climbed to 8.9% in the third quarter of 2011, and the fourth quarter of 2010, respectively. 300,000 Egyptians joined the workforce during the fourth quarter of 2011. Although official statistics released in September 2011 show that over 3 million Egyptian are unemployed, the International Monetary Fund (IMF)’s estimated in February 2011 that nearly 10 million jobs were needed in Egypt. The private sector contributes about 73% of employment in Egypt, while the public sector employs 27% of the labor force that stands at 26 million, of whom, 22% are women. Policymakers in Egypt have been working towards implementing projects that will promote job-intensive growth, especially among the youth, as about 25% of them are unemployed.

Monetary Sector

The Central Bank of Egypt (CBE) has continued to manage a gradual depreciation of the Egyptian pound since foreign currency inflows slowed down after the revolution (Chart 5). As the exchange rate (EGP per US$) slowly declined to EGP 6.04 at the end of March 2012, compared EGP 5.96 a year ago, Net International Reserves (NIRs), that the CBE has been selling to counter capital outflows dropped to US$ 15.1 bn at the end of March 2012, compared to US$ 36 billion in December 2010. The pace of EGP depreciation picked-up in October 2011, as political uncertainties deepened.

The spike of the domestic currency depreciation in October 2011 exacerbated imported inflation. The year-on-year (y/y) inflation rate (as measured by the urban consumer price index, CPI) bottomed up in October 2011 at 7.1% from 12.1% recorded in April 2011, while core inflation, y/y, had bottomed up two months earlier in August 2011 at 6.98% (Chart 6). By March 2012, the annual inflation rate reached 9%, while annual core inflation rate had risen to 8.68%. Price increases were largely driven by high imported inflation. According to the CBE, the higher price level was mainly due to anticipated rise in international food prices, local supply bottlenecks, and distortions in the distribution channels.
To continue defending the domestic currency from disorderly depreciation, and to ease inflationary pressures, the CBE during its monetary policy committee meeting in November 2011, raised the discount rate to 9.5% from 8.5%. This was the first time for CBE to revise the discount rate —the instrument CBE uses to operationalize its stated monetary policy goal of maintaining price stability— in more than two years. The CBE also raised the overnight deposit and lending rates to 9.25% and 10.25%, from 8.25% and 9.75%, respectively. The 7-day repurchase agreements rate (Repos) that was introduced in March 2011 to manage liquidity in the market on government treasury bills was also adjusted upwards from 9.25% to 9.75%.

As a result, the 3 months T-Bills (TB) rate rose to 14.3% in November 2011 from 11.2% in March 2011, and stabilized at the new level (Chart 7). Other interest rates did not change much. For example, the one-to-three end of month average deposit rates increased only slightly from 6.6% by end of March 2011 to 7.1% in November 2011, and 7.7% in March 2012. Further, the one-year-or-less average corporate loan rate increased from 10.7% at end of March 2011 to 12% by end March 2012.

Against the backdrop of constrained real economic activity, money aggregates’ changes were restrained. The M2 monetary aggregate expanded at a moderate pace of about 2% quarter-on-quarter (q/q) over the four quarters ending March 2012, reaching EGP 1,055 bn, from a base of 988.1 bn in March 2011. Growth in M2 was constrained by the monetary base, that is reserve money (M0) —currency in circulation and the banking sector deposits held at the CBE—, that contracted by 2.3% to EGP 251.3 bn by end-March 2012. However, over the same period, both money (M1) —M0 plus local currency demand deposits—, and Quasi Money —which includes time and savings deposits in both local currency, and foreign currency, and demand deposits in foreign currency—, increased slightly by 2% and 1.4%, reaching EGP 260.7 bn, and EGP 794.3 bn, respectively.

Financial Sector

Conditions in the financial markets remained uncertain over the past year mainly because of weak investor confidence in the speed of recovery of economic activity, after the revolution. In this context, the CBE’s monetary policy remained broadly accommodative. To ease credit conditions in the market and provide additional permanent liquidity into the banking system, the CBE lowered the reserve requirement on local currency deposits to 12% from 14% on 20 March 2012, and on 22 May 2012, further reduced such requirements to 10%, effective 26 June 2012. In March 2012, deposits in the banking system reached EGP 1,005 bn, an increase of 1.6% from end-December 2011. During the same period, credit facilities in the banking system rose by 1.3% to EGP 496 bn. Although this growth was driven by credit to the private sector (84.8% of the total) that expanded by 2%, credit to the public sector (6.9% of total) actually declined by 7.6%. The loan to deposits ratio stood at 49% at the end of the quarter ending March 2012. Nonperforming loans as a percentage of total loans stood at 10.9%
in December 2011, compared to 11.2% in March 2011.

Stock market performance, which had worsened after the revolution, are yet to recover (Chart 8). Overall market capitalization on the Egyptian Exchange (EGX) fell by 12% to EGP 362.5 bn (23% of GDP), by end-March 2012, against EGP 410.1 bn (34% of GDP), at the end of June 2010). The cause was the main benchmark EGX 30 index that sustained a downward performance by falling on average by 33% since January 2011 to close at 5,019 points by end-March 2012. As investors started to price in CBE’s monetary policy accommodation, the EGX 30 benchmark index, started to recover, rising by an average of 4% in March 2012 compared to the February 2012 records.

Public Finances

The latest available data of the budget sector show that fiscal deficit for the period July-March, 2011/12 stood at EGP 113.1 bn (7.2% of GDP), up by 20.3% from EGP 94 bn (6.9% of GDP) recorded during the period July-March 2010/11. Over the same period, while revenues increased by 36.9% to EGP 197.5 bn, total expenditures increased faster by 29.6% reach EGP 310.8 bn.

Despite the economic downturn the rise in budget sector revenues during the period July-March 2011/12 reflects an increase in tax revenues by 21% to EGP 132.3 bn (Chart 9). This was due to an increase in taxes on income and profits from the Egyptian General Petroleum Corporation (EGPC) by 122.9%. Further, non-tax revenues rose by 86.6% to EGP 65.2 bn, mainly because of tax on properties, and an increase in dividends from EGPC by 175.3%. Finally, foreign grants increased to EGP 8.8 bn, against EGP 0.81 bn, a year earlier.

The quickening pace of budget sector expenditures was due to higher cost of government borrowing and recurrent expenditures, as the authorities strived to respond to the demands of the revolution (Chart 10). Over the period July-March 2011/12, salaries for public sector workers increased by 28.9% to EGP 82.9 bn, and interest payments on domestic and external borrowing rose by 28.2% to EGP 78 bn. Over the same period, energy subsidy bill (paid to EGPC) increased by 267.7% to reach EGP 62.5 bn. However, food subsidies bill (paid to the General Authority for Supply Commodities, GASC) declined by 19.7% to EGP 16.4 bn. A quarter of government spending is for consumer price subsidies, and in particular on energy, but also on food prices (Chart 11). Finally, public investment spending declined by 22% to EGP 18.5 bn.

External Sector

Egypt’s foreign reserves —the CBE’s tool for supporting the domestic currency from depreciation—, dropped to US$ 15.1 bn by the end of March 2012, the 15th consecutive monthly fall. Before the revolution, foreign reserves stood at US$ 36 bn in December 2010.

At the end of the October-December 2011/12 period, Egypt’s deficit on current,
and capital (Capital & Financial) accounts stood at US$ 5.6 bn, compared to US$ 2.4 bn, at the end of the previous quarter. Underperformance of the Capital & Financial Account was the main driver for the deterioration of the balance of payments during the October-December 2011/12 period.

In this regard, the Capital & Financial Account had a net outflow of US$ 2.9 bn during the October-December 2011/12 period, compared to a net inflow of US$ 0.5 bn a quarter earlier. In the backdrop of investor uncertainties, net portfolio investment outflows over the October-December 2011/12 period amounted to US$ 1.6 bn, a slight moderation from the US$ 1.7 bn outflows recorded the previous quarter. On the other hand, portfolio investments abroad increased by 47.3% to US$ 0.93 bn over the same period as Egypt opted to selling dollar-denominated T-bills to local banks. Foreign direct investment (FDI) dropped sharply by 295%, registering a net outflow of US$ 0.86 bn compared to a net inflow of US$ 0.44 bn during the period July-September 2011/12. From a geographical perspective, the October-December 2011/12 period data show that European Union (EU) remains the main source of FDI (53.9% of total FDI) followed by countries in the Arab World (28%).

The deficit on the current account improved q/q by 13.6% to US$ 1.87 bn by end of the October-December 2011/12, as current accounts receipts of US$ 16.4 bn fell short of current accounts payments of US$ 18.3 bn. As a result, the ratio of current receipts to current payments improved to 89.7% during the period October-December 2011/12, against 88.2% over the July-September 2011/12 period (Chart 11).

Accumulated surplus in the services account declined by 7.5% to US$ 1.5 bn, over the same period. Receipts from tourism and Suez Canal slowed down by 12.7% to US$ 2.4 bn, and 2.7% to US$ 1.3 bn, respectively. Remittances (net private transfers) also decreased by 3% to US$ 3.9 bn over the same period. The improvement in the current account balance is partly because of an increase in official transfers by US$ 506.8 million, compared to US$ 15.9 million the previous quarter.

Also over the same period, the deficit in the trade account slowed down by 0.6% to US$ 7.7 bn compared to US$ 7.8 bn the previous quarter, driven by a faster increase in merchandise exports by 0.9% to US$ 6.8 bn against an increase in merchandise imports by only 0.1% to US$ 14.6 bn. During the October-December 2011/12 period, Egypt’s total merchandise exports and imports (trade volume) increased by 0.3% to US$ 21.4 bn, compared to the previous quarter. The European Union (EU) is Egypt’s major trading partner for both imports and exports, with 40% of exports, and 37.5% of imports. Egypt’s trade with African Countries (excluding Arab ones) amounts to only 1.7% of exports, and 1.1% of imports, but is expected to increase after a new government is in place (Chart 13).
Fuels, minerals, oils, and products sector remains Egypt’s key exports drivers, accounting for 52.5% of exports, followed by manufactured finished goods (38.2%) (Chart 13). The top three Egypt’s imports are: intermediate goods (28.8%); consumer non-durable goods (23.7%); and investment goods (18.4%). (Chart 14). A major consumer non-durable goods import by Egypt is wheat. According to the Food and Agriculture Organization (FAO), Egypt is the world’s largest importer of wheat. During the 2010/11 fiscal year Egypt imported about 10 million tons of wheat for the food subsidy system, a level that is comparable to the average imports of the previous two fiscal periods.

**Public Debt**

A key macroeconomic related issue that Egypt would need to tackle in the medium-term is the high domestic debt that is crowding out private sector access to credit, and is slowing down progress on achieving the Government’s target for public debt of less than 60% of GDP by fiscal year 2014/15. Foreign debt levels remain relatively manageable (Chart 16).

The growth rate of Egypt’s external debt has been declining over time (Chart 17). By end-December 2011, external debt dropped to 12.9% of GDP, compared to 15% at the end of December 2010, and is declining, standing at US$ 33.7 bn by end-December 2011. Out of this, 76.3% are debts of the government, of which 9% is of short term nature. Debt service during the quarter ended December 2011, declined to US$ 0.3 bn, down by 72.6%, q/q. As a result, external debt service as a percentage of current receipts was 2% at the end of December 2011, against 7.5% at the end of September 2011.

However, domestic public debt has been trending upwards since 2008 during the global financial crisis (Chart 18). By the end of March 2012, domestic public debt rose by 23% to EGP 1183 bn, (75.4 of GDP) compared to EGP 962.3 bn (70.1 % of GDP) at the end of December 2011. Quarter-on-quarter, domestic debt grew by 4.4% compared to end-December 2011 position. Of the total public debt, the government debt comprises 79.9%, public economic authorities’ debt, 5.5%, and debt of the National Investment Bank (NIB), 14.6%. Government treasury bills and bonds stock reached EGP 982 bn by end-March 2012, an increase of 3.2%, q/q.

Recently, domestic debt burden has been rising steadily, with rising government securities’ interest and principal repayments (Charts 18 and 19). Total interest payment as a percentage of the government sector expenditures increased from 21.2% in 2010/11 fiscal year to 26% during the period July-April 2011/12. Interest payments and principal repayments on government debt, respectively, rose from EGP 85.1 bn and EGP 32.2 bn, in 2010/11 to EGP 88.9 bn and EGP 35.5 bn over the period July-April 2011/12. As a result, the total government debt service amounted to EGP 124.4 bn during the period July-April 2011/12, compared to 117.2 bn for fiscal period 2010/11.

As shown in Chart 19, yields on government Treasury bills (T-bills) have been rising over the past year. Currently, yields for the one-year T-bills, are about 15%, and are continuing to rise. This is despite the monetary accommodative measures that CBE has been putting in place, and that have increased the liquidity in the banking system by reducing the reserve requirement ratio as indicated earlier. It would appear that the impact of such measures by CBE is not wholly effective, as evidenced by the rising yields. As such, domestic public debt poses significant interest rate and budgetary risks; therefore a priority for the government is to take measures to re-profile its short-term domestic debt to longer-term foreign currency debt.
Chart 11 Subsidies

Source: Central Bank of Egypt.

Chart 12 Current Account (US$ mn)

Source: Central Bank of Egypt.

Chart 13 Egypt's Trade Partners (US$ mn)
(October-December, 2011/12)

Source: Central Bank of Egypt.


**Chart 14** Exports by Processing Degree (US$ mn)

**Chart 15** Imports by Use (US$ mn)

Source: Central Bank of Egypt.

**Chart 16** Public Debt (% of GDP)

Source: Central Bank of Egypt.
**Chart 17 External Debt Indicators (%)**

Source: Central Bank of Egypt.

**Chart 18 Domestic Debt Indicators (%)**

Source: Central Bank of Egypt, and Ministry of Finance.

**Chart 19 Interest Rates on Government Securities (%)**

Source: Central Bank of Egypt, and Ministry of Finance.
### Egypt Development Indicators

**Land area** 997,739 sq km, of which only 5% is inhabited and cultivated

**Population Major Towns** (July 2007)
- Greater Cairo: 18,440,076
- Alexandria: 4,123,869
- Port Said: 570,603
- Suez: 512,135

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<th>Population (million)</th>
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<td>Population inside the country</td>
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<td>Annual growth rate</td>
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<td>Labor force, 15 years and above, as % of population in Egypt</td>
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<td>Unemployment/ labor force (%)</td>
<td>12.4 (1st quarter 2012)</td>
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<td>Youth unemployment, 25-29 years, as % of total unemployment</td>
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<td>Literacy rate, adult total (% of people ages 15 and above)</td>
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<td>Poverty headcount ratio at $1.25 a day (PPP) (% of population)</td>
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<td>Poverty headcount ratio at national poverty line (% of population)</td>
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<td>Mortality rate, under-5 (per 1,000 live births)</td>
<td>21.8 (2010)</td>
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<td>Improved water source (% of population with access)</td>
<td>99 (2010)</td>
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### Egypt Economic Indicators

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<td>Public finance (as % of GDP)</td>
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<td>Total revenues</td>
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<td>Total expenditures</td>
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<td>As months of commodity imports</td>
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<td>Imports growth (year on year)</td>
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<td>FDI in Egypt (net) (as % of GDP)</td>
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<td>4.3</td>
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Source: Central Bank of Egypt, Ministry of Finance, and World Development Indicators.
About the African Development Bank (AfDB)

The African Development Bank (AfDB) is Africa’s premier development finance institution established in 1964 to mobilize resources for the economic and social development of its 53 regional member countries. The Bank’s membership includes 24 non-regional member countries bringing the total number of member countries to 77.

The Bank has been financing development activities in its regional member countries through its three windows of financing: the African Development Bank (ADB) window, the African Development Fund (ADF) window and the Nigerian Trust Fund (NTF) window. In the first quarter of 2012 alone, the AfDB Group approved 60 loans and grants amounting to USD 5.52 billion.

About Egypt

Egypt is one of the AfDB’s most important regional member countries. In addition to being one of its founding members in 1964, Egypt is one of its top shareholders.

For More Background on AfDB Operations

For more information about the African Development Bank, and its operations in Egypt, visit the Bank’s website at:

Contacts

Mr. Sibry Tapsoba, Resident Representative
Email: s.tapsoba@afdb.org

African Development Bank Group
Egypt Country Office (EGFO)
72B Al Maahad Al Eshteraky St. Heliopolis
Opposite to Maryland Roxy/Heliopolis
Cairo, EGYPT
Tel.: +202 22 563 790 / 1
Fax: +202 22 563 792
Ext: 6730-6759