The Effect of the Rise in the Dollar Rate on the Egyptian Economy

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ABSTRACT

Exchange rate is a measure for the economic performance of the state. It is also a reflection of the case of the political stability of it. It is a measure of the extent of the availability of a good climate for investment in the state, in addition to its important role in influencing the level of the competitiveness of the products of the state. The dollar rate has witnessed successive rises in exchange for the Egyptian pound after firming dollar rate relatively over eight months, as it has risen from 7.14 pounds / dollar to 7.40 pounds / dollar in the official market. These successive rises of dollar exchange rate have led the study to spot light on its reasons and consequences. One of its most important reasons is the desire to eliminate the black market of currency by narrowing the gap between the official rate and the rate of the parallel market and trying to unify the two rates. Some of the most important negative effects of raising dollar exchange rate are the rise in the prices, delaying the implementation of projects, the rise in the rate of inflation, severe losses to tourism companies, lack of medicines and the rise in the prices of building and construction materials, especially those that are imported from abroad, which is followed by an increase in the prices of residential units. Some of the most prominent groups benefiting of the rise in dollar rate in Egypt are the exporters, the Central Bank, foreign investors and the owners of salaries in dollar. Moreover, some of the reasons for raising the dollar rate are the government’s attention to the economic conference in March, the Central Bank’s last decision to reduce the interest rate on bank deposits to 1%, repaying some of the financial obligations, owed by the state, by the Central Bank, the conversion made by the foreign companies working in Egypt to their profits at the end of the last year into US dollar, increasing the strength of dollar in the global markets before the basket of currencies and repaying a part of the dues of the global energy companies by the state.

Key words: Dollar's rate – the rate of inflation – the black market – the economic conference

Introduction

Exchange rate is a measure for the economic performance of the state. It is also a reflection of the case of the political stability of it. It is a measure of the extent of the availability of a good climate for investment in the state, in addition to its important role in influencing the level of the competitiveness of the products of the state. Egypt follows the technique of managed floating in determining the value of its currency against the rest of the other currencies. To manage floating means to allow the exchange rate being determined according to supply and demand and the central bank shall interfere whenever the need arises to modify this price in return for the other currencies. Since the end of 2012, the central bank determines the value of the dollar against the pound according to its selling price in dollar tenders offered by it before banks in order to provide the greenback to meet market needs. Moreover, any reduction in the exchange rate of currency has effects on price movements and the competitiveness of exports, imports, trade balance, the rate of international exchange, the attractiveness of investment climate and tourism market. It has risen from 7.14 pounds / dollar to 7.63 pounds / dollar in the official market and those successive rises of the dollar exchange rate have led the study to spot light on its reasons and consequences, as there are many reasons of the successive rises of the dollar exchange rate. One of its reasons is the desire to eliminate the black market of currency by narrowing the gap between the official rate and the rate of the parallel market (trying to unify the two rates), and thus allowing the official exchange rate to move up. But there is a belief that this may be a permit for those in charge of it to make greater rises in the rates than the official market (moving the rate of the parallel market towards greater rises).

The Problem of the Study:

The problem of the study represents in the continuing decline in the Egyptian pound’s exchange rate against the dollar. This leads to a rise in the prices of all the imported commodities which is equal to the proportion of the depreciation of the pound against the dollar (as their value in the last year has reached to about

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59.8 billion dollars which is equivalent to about 20% of the domestic production). It leads also to a rise in the prices of their corresponding domestic commodities. Therefore, the rate of inflation can exceed, in fact, the estimates of the International Monetary Fund.

The Aim of Study:

The aim of the study is to know the reasons for the rise in the dollar rate and its effect on the Egyptian economy, and to know the groups benefitting of this rise in Egypt.

The Method of Research and Data Sources:

The study has depended on the statistical descriptive method in achieving its objectives. In addition, it has depended on the published and unpublished data of the Central Agency for Public Mobilization and Statistics, the Central Bank, the World Bank and several websites and studies relevant to the subject.

The Results of the Study:

The value of the Egyptian pound has retreated sharply against the dollar in the recent times, as its rate has reached about 7.63 pounds against the dollar, which means that the pound has become equal to 0.13 dollars that is about 13 cents only, which is considered the lowest official rate since 2012 although the effects of this downward movement on the Egyptian economy. More than 60% of the industrial and food needs are imported from abroad in foreign currency. The opinions are various about this retreat, as some people see it as a procedure must be taken and it enhances its point of view that the government is seeking to encourage investment by allowing the currency to reach the rate that the market sees it fair. However, some others see that the devaluation of the Egyptian pound has aggravated over the past four years, as a logical consequence of the economic recession that usually affects the exchange rates in most sectors. They confirm that the time has come for the pound to attract the attention because of the Central Bank’s decision to reduce the value of the local currency.

The Positive and Negative Effects of the Devaluation of the Egyptian Pound:

The Elimination of the Black Market:

Black market is active in Egypt to sell and buy foreign currencies outside the range determined by the Central Bank of Egypt, which is committed by banks, which in turn cannot meet the demand for foreign currencies after the country’s reserve of foreign exchange has retreated to about almost 15.3 billion dollars. The Central Bank tries, through reducing the pound’s rate, to narrow the gap between the official rate and the rate on the black market, which may eliminate the black market according to the statements of the analysts and the Governor of the Central Bank of Egypt.

The Rise in Prices and the Delayed Implementation of the Projects:

At the time when some experts see that the retreat of the pound’s exchange rate will not affect the levels of the domestic prices during the current period because of the retreat in the prices of commodities globally, businessmen and traders complain of a sudden rise in some of production requirements which will affect price levels. Thus, it will affect the rates of implementing the projects, especially infrastructure projects. The Egyptian Federation of Construction and Building Contractors see that the rise in dollar rate in banks and black market causes an increase in the prices of goods and ores used in projects at a rate over 70%, especially the imported ores and materials that projects need. Moreover, most of the materials needed by contracting companies which are working in water stations, networks, sanitation and power plants are imported from abroad (such as generators, valves, water pumps and spare parts). Thus, the rise in the dollar rate negatively affects the rates of implementing and delaying these projects, even if law obliges backing bodies to compensate contacting companies for the rise in the prices of ores.

The Shortage of Foreign Currency Resources under Rising Prices:

There is a fear of doubling prices largely due to the shortage of foreign currency resources, especially after the retreat in tourism revenues, export proceeds, remittances from the Egyptians working abroad and other foreign currency resources, which may make it difficult for importers to buy the raw commodities needed for domestic production and food commodities. (The Governor of the Central Bank stated that the Central Bank will interfere in case of there is a rise in the prices of market, of the procedures of reducing local currency, pointing out that he is following markets accurately during the last period).

Deficit and Debts:

Official data indicate that the Egyptian trade balance is suffering from a huge deficit of 33.7 billion dollars in the fiscal year 2013/2014, compared to a deficit of 30.7 billion dollars in 2012/2013, about 34.1 billion dollars in 2011/2012, 27.1 billion dollars in 2010/2011 and about 25.1 billion dollars in 2009/2010. It is a
continuous deficit without stop for more than four decades. Moreover, the study sees that any attempt to reform the external balances and support the Egyptian balance and ensure its stability must begin with reforming the deficit of trade balance, whether through activating and diversifying exports including what they require of diversifying and developing the production that can be exported, or through rationalizing imports in order to provide foreign currency, especially in times of crisis such as those that the Egyptian economy is going through at the current time.

As for public debt service, it is expected that it would rise by the same proportion of changing the rate of exchange, especially the external dept. Others (officials in the Ministry of Finance) see that liberating dollar’s exchange rate against the Egyptian pound will negatively affect the investment of foreigners in the government debt instruments in the short term although it is the most attractive for investors, as foreigners’ departure from the market of government debt instruments at the current time will expose them to losses (although foreigners share in debt instruments currently is not great). Also, reducing currency rate will reduce the profits of investors by the proportion of retracting the pound’s value. It is worth mentioning that foreigners had come back to buy government debt instruments for the first time in the session of last July 26 after a long stopping in order to benefit from the rise in return prices and the calmness of the political turmoil in the country. Investor will wait for some time in order to follow the developments of the depreciation of the pound against the dollar according to the versions of the Central Bank, which will reduce the intention of foreigners at the current time to buy new instruments, which will expose interest rates to the risk of rising a little over the stable limits currently. However, some others see that the decline in pound’s value has a positive effect in increasing investments by stimulating the desire of Arab investors; especially they are dealing in US dollar in excuting their deals, which increases the value of their capitals. But vice versa for the Egyptian investors, as it will lead to a further decline in the value of pound then a devaluation of the local purchasing and investment power.

As for the rates of saving, the study sees that the decline in the value of currency will have negative effects over the long-term, and it will increase inflation rates. Declining the value of pound is so beneficial for foreign investors, as everything seems to be less expensive, including stocks and bonds, and it will increase investors’ desire to buy bonds because of their lower prices.

Most of analysts expect that the transactions of foreign and Arab markets will be improved because of the decline in the Egyptian pound rate against US dollar. The decline in any local currency means a rise in the purchases of foreigners. So, it is expected, in the coming period, that the main index will rise until the volume of transactions reaches to 10,000 points.

The Negative Effects of Declining the Pound Rate on the Inflation Rate:

The danger of declining pound rate against the dollar is shown from the study, as the coming rises in the prices of commodities and services will raise inflation rates to exceed 12.5%, and it may reach to 13%. In addition, the rises in dollar rates would result in increasing the value of the allocations of commodity imports in the public budget of the state by about 2 to 2.5 billion pounds to reach to 32.5 billion. The savings which were expected to be achieved by the public treasury in the value of supporting the petroleum products as a result of the decline in oil price globally will be reduced by about 5 billion pounds. From the above it is clear that the solution of the governor of the Central Bank to rise dollar rate was not successful, it did not take into account its consequences such as the expected rises in the general rates of prices and the inflation significantly, which increases the burden on ordinary citizens. It also has made Egypt lose the comparative advantage, during the current fiscal year, represented in the expected decline of about 25 billion pounds of the bill of supporting petroleum products for the current year which is estimated at 100 billion pounds, as the rise in the dollar rates will automatically lead to a rise in the general rates of prices and the inflation significantly, which increases the burden on ordinary citizens. It also has made Egypt lose the comparative advantage, during the current fiscal year, represented in the expected decline of about 25 billion pounds of the bill of supporting petroleum products for the current year which is estimated at 100 billion pounds, as the rise in the dollar rates will automatically lead to a rise in the expected savings in subsidy bill, especially the dollar is a candidate to rise.

The Negative Effects of the Rise in the Dollar Rate on the Egyptian Market:

The Egyptian market has witnessed a sudden rise in the official dollar rate. It is known that about 80 percent of the main commodities consumed by the Egyptian market have come through importation and the rise in dollar rate surprisingly is considered as “an economic disaster”. If it is not resolved and the result will be a rise in the prices of commodities or a disappearance for these commodities from the markets. The Head of the Division of importers has assured that the prices of all the imported commodities have increased at a proportion not less than 10 percent and it is a must to provide a lot of dollars by the Central Bank in order not to make investors be as a prey for the black market.

Despite the decline witnessed by the global prices of the main commodities during this period, but that will not work before the rise in dollar rate, as the decline in the global prices has happened since a period, which make a rise in the domestic prices with the occurrence of the dollar jump. Besides the rise in the proportion of costs, manufactures and others, as the commodities whose prices did not change have excess inventory had been imported at the old prices. One of the most prominent commodities whose prices have risen during the last period is oil, as bottle’s price (three-quarters kilogram) has risen from 7.5 to 8 pounds. The rise in the prices of
commodities is expected with the continued crises of rising dollar rate at a proportion not less than 3 percent, as 80 percent of commodities are imported. Thus, supervision on the prices of imported commodities should be tighten, according to global prices in order not to exploit some importers and traders and raise the prices at varying proportions in order to increase the profits.

As for medicines, they are considered one of the most important sectors of interest to citizens and their lack will lead to a major crisis. Pharmaceutical sector is affected differently by raising the dollar rate against the pound, as medicines are priced according to a tariffication, which cannot be changed without a ministerial decree. Therefore, the effect of the dollar was a key factor in the shortage of nearly 400 types of medicine from the Egyptian market. The continuation of dollar crisis will exacerbate the crisis of medicines disappearance because of the reluctance on producing and selling medicines at these prices that cause severe losses for producer in the difference between production inputs on which he relays to import and production outputs which are sold according to the tariffication.

Pharmaceutical sector will not be able to withstand for a long time with the continuing of raising dollar crisis, as it is one of the sectors committed to the tariffication that cannot be changed and the only turn is not importing raw materials and the lack of types in the market. This will lead to the constraint to the alternative medicines that have higher prices, if any, or go to foreign markets in a search of the needed medicines at four times of price. The result of this crisis would be borne by the citizens and the state, and simple patients are the ones, who would suffer. In addition, it will have a negative effect on the pharmaceutical industry in Egypt and the industry in general, and therefore, government shall seek in considering this matter.

The Most Prominent Groups Benefiting of Raising the Dollar Rate in Egypt Include:

1- Exporters:

Exporters are one of the first groups benefiting of raising the dollar rate. Export provides more profits for them, as the purchasing power of the dollar while converting it into Egyptian pounds increases, especially if the state managed to curb any inflationary waves resulting from increasing the dollar. In addition, this rise encourages exporters to increase their business and thus exporting the Egyptian products abroad would be increased.

The Negative Effects on Real Estate Market:

The real estate market in Egypt is facing a new crisis as a result of raising dollar rates and the instability of the Egyptian pound’s exchange rate before it. This matter will cause negative effects on investors and the owners of real estate companies, as well as raising the prices of building and construction materials, especially those that are imported from abroad, which is followed by an increase in the prices of residential units. It is synchronized with a rise in real estate prices by about 10%. In addition, the rise in the dollar rate will affect the prices of raw materials and the workers because when the dollar is raised, workers demand immediately to increase wages. The rise in raw materials is a result that most of them are imported and thus it will have an effect on raising real estate prices.

The Negative Effects on the Tourism Sector:

The deterioration of tourism revenues is the main reason of the disappearance of the surplus of the balance of services trade. This means that the restoration of this surplus is closely associated with restoring the flow of tourists to Egypt. Moreover, Egypt has tremendous potential in the cultural and archaeological tourism, the tourism of resorts, diving and safari and therapeutic tourism. It has a huge and distinct main tourist structure and enjoys an excellent competitiveness towards the cost of tourism in it. The matter is totally relating to the stability of security and the behavioral and environmental controls in tourist areas.

Furthermore, raising dollar rate has affected greatly the tourism sector, as it has enormously raised the prices of Hajj and Umrah, which creates successive crises facing the tourist sector and there are severe losses and because of these losses some owners are exposed to prison for their inability to pay their debts to banks. In addition, the demand for Hajj and Umrah has retreated during this period due to the rise in their prices from 30 to 35%. This crisis has led to lay off a large number of workers within the tourism sector. Also, some companies have closed their doors and their owners became with no work and no support from the government. The study suggests that the government must postpone taxes, social welfare and any other obligations on tourism companies until they cross this critical stage in which they cannot find the salaries of employees. The poor conditions experienced by Egypt during the period has led to decline the numbers of tourists and force all tourism companies to work in religious tourism to compensate their losses and the low revenues, especially with raising the dollar rate.

The Most Prominent Groups Benefiting of Raising the Dollar Rate in Egypt Include:

1- Exporters:
2- Foreign Investors: Investors are some of the beneficiaries of the pound devaluation against the dollar, especially the new investors or those who are seeking to make more investments. This appears more clearly in the stock market, as the share holders who share the same amount in dollar can buy a larger amount of the shares listed in the Egyptian stock market because of the rise in the dollar. It is assumed that this matter will be reflected positively on the Egyptian stock market, and investments will be increased in it.

3- The Central Bank: The dollar rate rises in the black market with the pound devaluation in banks due to the poorness of dollar resources. This may result in raising the prices of the imported commodities; especially those that are financed from the black market in a way may reduce the demand for them in the Egyptian markets and thus reducing their importation at the time when the rise in the dollar is encouraged over the increase in the exports. This crisis results in reducing trade balance deficit and thus reducing the current transactions and increasing the balance of payments surplus (Egypt’s dealings with the external world), which is reflected positively on the foreign exchange reserves in the Central Bank.

4- The Black Market: Exchange companies and the people working in the black market of dollars are one of the most prominent beneficiaries of its rise in banks. Although some people attribute the Central Bank allowance to depreciate the pound in Banks to the fighting speculators in the black market, but the reality shows that one of the most important reasons for the crisis of the black market of the dollar in Egypt is the poorness of dollar resources during the past two years, which makes it difficult to eliminate the black market through this procedure only. But this market will be among the beneficiaries, which has actually happened during the last days.

5- The Owners of Salaries in Dollar: It is expected that the owners of salaries in dollar who work in Egypt will benefit from the rise in the dollar rate, which will be reflected on them through increasing the purchasing power of the money they receive from their business, especially if the state manages to control any rise in the prices of commodities that may be resulted from the rise the in dollar, or in the case of depending on buying the commodities whose production depends on the local raw materials.

The Reasons of the Rise in the dollar:
- The last Central Bank’s decision to reduce the interest rates on bank deposits to 1%, which may lead to make citizens resort to diversification companies.
- The government’s attention to the economic conference in March (2015), which drives the Central Bank to take the procedures of pound floating in order to cancel the black market, so that investors can deal with a unified exchange market and calculate the returns and costs on real rates of currency.
- The desire to eliminate the black market of currency by narrowing the gap between the official rate and the rate of the parallel market and (trying to unify the two rates), and thus allowing the official exchange rate to move up. The study sees that it may be a permit for those in charge of it to make greater rises in the rates than the official market (moving the rate of the parallel market towards greater rises).
- Repaying some of the financial obligations, owed by the state, by the Central Bank (repaying the Qatari deposit in addition to the repayment of the dues on Egypt towards Paris Club in the favor of the creditor countries in the framework of the regular repayment to the dues of these countries every six months).
- The conversion made by the foreign companies working in Egypt to their profits at the end of the last year into US dollar.
- Increasing the strength of the dollar in the global markets before the basket of currencies, this gives more strength to the dollar against the pound.
- Repaying a part of the dues of the global energy companies by the state.
- The government’s desire to encourage foreign investment by allowing the Egyptian pound / dollar rate to approach the real price of it.
- The vision of the Central Bank of Egypt that that is the right time to let the exchange rate at a relative freedom, especially with the reduction of the world prices of petroleum, which may reduce the inflationary pressures that the Central Bank works on restraining them.
- The desire of the state may be to support obtaining the IMF loan, as it requires the liberalization of the exchange rate. Thus, the study believes that Fund’s loan may be one of the reasons for that significant rise in the exchange rate, which has happened in a brief period after stability lasted for nearly eight months. There is still a tendency to rise, though these rises do not live up to liberalization, but they can be called a move for the
price because the state still interfere in determining the price through tenders, and it do not let it be determined by market forces.

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