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ECES
The Egyptian Center for Economic Studies

Our Economy & the World

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Key Global Developments

IMF Warns of Increasing Risks to Global Financial Stability

KUNA:

The International Monetary Fund (IMF) warned against increased risks to the global financial stability in light of higher economic risks and uncertainty, falling commodity prices, as well as concerns about China's economy.

In its latest Global Financial Stability Report, which was distributed in a press conference, the IMF noted that over the last six months, global markets reacted negatively to those factors, but things have "significantly improved" since last February.

The report attributed this improvement to "some better news such as the intensified policy actions taken by the European Central Bank, and the US Federal Reserve's cautiousness toward raising interest rates.

According to the report, China, as one of the most important emerging markets in the world, is still witnessing a complex transition to a slower and more balanced pace of growth and a more market-based financial system. The report also noted that the Chinese authorities have stepped up efforts to strengthen their policy framework, boost growth and stabilize the exchange rate.

IEA Chief Sees Oil Prices Rebound in Second Half of 2017

Reuters:

The International Energy Agency expects oil prices to rebound next year and the market rebalance itself, Fatih Birol, IEA's executive director, said on Wednesday.

"We are not a party to the Doha meeting discussions, but what we can say is that we expect at least in 2017 oil prices to rebound and market to rebalance," he told reporters in Lisbon. He added later, "the rebound should be in the later part of the year."

OECD: Development Aid Exceeds $130 Billion in 2015
KUNA

The Organization for Economic Cooperation and Development (OECD) said on Wednesday that development aid totaled USD 131.6 billion in 2015, representing a rise of 6.9 percent from 2014 in real terms.

The Paris-based organization noted in the annual report on the performance of its Development Assistance Committee (DAC) that aid spent on refugees amounted to 1.7 percent of total aid in 2015.

Official development assistance (ODA) from the 28 countries in the DAC averaged 0.30 percent of gross national income, the same level as in 2014, adding that DAC aid is up 83 percent since 2000 despite the sharp depreciation in many country currencies against the dollar last year.

IMF: Debt Levels Highest since World War II
WASHINGTON, United States (AFP) :

Public debt has soared in advanced economies to the highest levels since World War II as governments struggle against slow growth and deflation, the International Monetary Fund warned.

Levels of government borrowing have picked up since the financial crisis and continue to rise as economic powers like Japan and Europe remain mired in very slow growth and many emerging and poorer economies struggle with the plunge in income from commodities like oil and metals.

The higher borrowing makes it harder for governments to spend any more to support growth, as the Fund has urged.

On average for advanced economies, the IMF said in its new Fiscal Monitor report, "public debt now exceeds the level observed during the Great Depression and is approaching the level immediately after World War II."

For advanced economies, debt has risen to over 107 percent of gross domestic product, with Japan at almost 250 percent.

Emerging market economies are better off at just under 50 percent of GDP, but their needs are rising and many face greater challenges, including sharply higher fiscal deficits, than the advanced economies.

The strain between higher debt and the need to keep spending is contributing to the slow pace of growth.

The IMF lowered its global growth forecast for 2016 on Tuesday to 3.2 percent and warned of the risk that growth could stall worldwide if action was not taken.

Worldsteel: Global Steel Demand Set to Fall in 2016 due to China's Slowdown
Reuters:

Global steel demand will continue to fall this year before a slight pick-up in 2017, the World Steel Association forecast on Wednesday.

Falling demand has plunged the global steel market into crisis, with excess capacity taking a heavy toll on producers, including those in China - leading to plant closures and job losses.

Global steel use is expected to fall 0.8 percent in 2016 to 1.488 billion tons after a 3 percent fall last year, according to Worldsteel.

China's steel demand is seen falling 4 percent this year to 645.4 million tons and a further 3 percent in 2017, after a slide of 5.4 percent in 2015, the group added.

China, which produces about half the world's steel, is under increasing international pressure to tackle a local supply glut that has flooded foreign markets with cheap material.

Rise in Chinese Exports Increases Confidence in the Second-Largest World Economy
Asharq Al-Awsat online:

Chinese exports growth rebounded in March for the first time in nine months, representing a new sign of stability in the second largest world economy and lifting investors' morals in the region.

Exports rose 11.5 percent in March on a yearly basis, registering the first growth since June and the largest percentage increase since February 2015.

The unexpected rise comes after other economic indicators for March implied a slight improvement in the economy in general, despite the fact that other surveys have shown increasing downward pressures on wages and employment.

Imports continued to decline, but at a less pace than expected, as they declined by 7.6 percent in dollar-denominated transactions while most major commodity volumes rose strongly, especially copper and iron ore.

This led to a trade surplus of $29.86 billion in March compared to $30.85 billion in the forecast, according to the General Customs Administration on Wednesday.

World Bank Projects Slow Growth in MENA in 2016
MENA- Washington:

The World Bank projected average GDP growth in the Middle East and North Africa region to be 3 percent in 2016.

The report, published on MENA growth prospects, ruled out the possibility of achieving faster growth as the region is experiencing civil wars, flow of refugees, terrorist attacks, lower oil prices, in addition to the slow recovery of the global economy.

The report stressed that civil wars significantly harmed the economies of Syria, Libya, Iraq and Yemen, and also had an impact on the economies of Jordan and Lebanon.

The World Bank projected that MENA oil importers will witness slower growth rates in spite of lower oil prices, due to security problems as well as slow tourism activity and workers' remittance. Oil-exporting countries, including the GCC, will continue to be affected by lower oil prices.

World Bank Loans at Highest Level since the Financial Crisis
WASHINGTON – AFP:

Developing countries borrowed the most money from the World Bank in 2015 since the 2008-2009 crisis.

"As developing countries continue to face strong economic headwinds, demand for lending from the World Bank has risen to levels never seen outside a financial crisis," the World Bank said in a statement.

During its 2015 fiscal year, lending to emerging-market and low-income economies totalled $42.4-billion, up from $40.8-billion in 2014.

Of that total, lending for emerging, or middle-income countries, was $23.5-billion in 2015, compared with only $14-billion in 2006.
Hit particularly hard by the sharp fall in oil and other commodity prices and China's cooling economy, a number of developing countries are suffering from strained finances and economic difficulties.

Implications for Egypt:

The only way out of this crisis is that instead of denying current challenges, they must be placed in their proper place and dealt with accordingly. Addressing problems has become possible and the vision for the future has become more rooted. The will to reform is what can drive us out of this economic crisis. Hence, the end of the period of economic troubles, which everyone is anxious for, is mainly related to the country's ability to achieve growth capable of utilizing the youth, and hence achieve the optimal model of growth and social justice. It is also related to the political and economic potential of the government, and its ability to take the right decisions to overcome the crisis.

Egypt must pay attention to the fact that the global economic crisis is witnessing new shifts in terms of effects, as the US began to relatively exit recession while developing countries are seeking to enter into new partnerships. Meanwhile, China is making efforts through the Asian Bank to turn into a global economic powerhouse while the pace of economic recession fears are escalating in the EU. This requires that the Egyptian government put together stimulus policies that rely mainly on development and revitalization of domestic industries, import substitution, and export promotion to markets where Egypt enjoys a comparative advantage, especially Arab and African markets. Egypt must also develop medium-term policies for the development of small and medium enterprises to promote economic growth and development away from the effects of the global financial crisis, which is currently experiencing new shifts.

With the financial and economic volatility the world is currently going through along with growing fears of a recession, Egypt should take more robust measures to enhance private growth, especially that downside risks increase in the absence of decisive action. According to the International Monetary Fund, recovery from the global financial crisis between 2007 and 2009 is still “too weak and too fragile,” and risks to its durability are increasing. If policymakers manage to meet challenges and work together, the positive spillovers on world confidence and the global economy will be significant.

Special Analysis

The Global Economy Crawling toward Recovery, Risks Growing
Al-Mal Newspaper Website:

Christine Lagarde, Managing Director of the International Monetary Fund, announced earlier this month that the global economy was recovering, but growth was still fragile and weak and risks were growing. On the other hand, the WTO expects the trade volume to increase by 3.6 percent in 2017—to break the barrier of 3 percent for the first time in six years— and growth in world trade this year to stop at 2.8 percent compared to previous expectations of 3.9 percent announced at the end of 2015.

"The good news is that we have growth, there is a recovery underway, the good news is we have no crisis. But the bad news is that growth is fragile, growth is weak and risks on the horizon are increasing," Lagarde told reporters in Berlin after meeting global finance chiefs and Chancellor Angela Merkel.

In her speech at Goethe University in Frankfurt, Germany, Lagarde noted the need for specific steps, including increasing the minimum wage in the US, improving business training in Europe, and reducing fuel subsidies and increasing social spending in developing economies so that policymakers can face the challenges and work to enhance the positive effects on investor confidence and the global economy.

Although Lagarde believes that recovery from the 2007 and 2009 global financial crisis is still very slow and fragile, with growing risks threatening the continuation of this recovery, emerging market stocks have recovered in 31 countries, led by China and India in March. These stocks increased by about $1.83 trillion, with their total market capitalization rising to more than $14.8 trillion—the largest increase since 2007.

Despite the increased pace of growth in the US economy and in a number of developing markets such as Mexico registering reasonable growth, the IMF warned that growth in Europe and Japan was disappointing. Lagarde stressed the need for countries in the euro area to better train the young labor force and to try to match the needs of the labor market with the appropriate skills to contribute to reducing unemployment among the youth. Meanwhile, slow growth in China affected the oil sector worldwide, as well as countries exporting primary commodities, including Brazil and Russia. Lagarde recommended for the first time a number of specific policies such as speeding economic structural reforms, increasing financial support, and the continuation of expansionary monetary policies.

Lagarde pointed out that a higher minimum wage, expanded tax credits for the working poor and improved family leave benefits - changes championed by President Barack Obama and Democratic Party presidential candidates - could help increase the US labor force, she said. Countries with high and growing debts and elevated borrowing costs should pursue further fiscal consolidation, Lagarde said. But her remarks did not mention negotiations between the IMF, European lenders and Greece for a new bailout program for the heavily indebted country.

The IMF offered a solution to persistently sluggish economic growth that included proposals to deregulate product markets and adopt policies to boost labor market participation. But the analysis in the IMF's annual World Economic Outlook acknowledged arguments from skeptics of such "supply side" reforms that deregulation can cause near-term falls in wages and price deflation and so need to be accompanied by fiscal stimulus.

The IMF said that new research shows that structural changes to labor markets and some more heavily regulated business sectors could help raise potential output over the medium term, while also helping to strengthen consumer confidence in the near term. It recommended deregulation of the railway and professional services sectors, and some network-based sectors such as air, rail and road transportation, electricity and gas distribution, telecoms and postal services, particularly in the euro zone and Japan as well as a number of developing countries.

The IMF noted that supply-side reforms should be accompanied with fiscal stimulus measures to help boost demand in the short term and absorb negative shocks. For example, cutting unemployment benefits and limiting laws protecting labor should be coupled with reduction of labor taxes to help increase net wages and attract individuals to the labor force once again.

Implications for Egypt:

We expect the fragile recovery of the global economy and international trade in addition to continued low oil prices to reflect on Egypt's macroeconomic performance in 2016. It is also expected that the impact of fiscal adjustment policies will lead to spending cuts in a number of budget items announced by the government in the context of policies aimed at achieving some balance between economic growth and fiscal discipline.

Internal developments in countries in the region will also affect growth opportunities in 2016. Therefore, proceeding with the implementation of economic reforms represents a basis for driving growth, especially with regards to reforms aimed at increasing production capacity and enhancing competitiveness.

We also expect continued high rates of inflation, attributed mainly to increased prices due to continued review and evaluation of government support, as well as the increase in demand-driven inflation in 2016. In addition, the exchange rate continues to be under pressure due to lack of foreign currency despite increased exchange rate flexibility. This will help increase pass-through effects.

In light of the above, the Egyptian government has to focus on the implementation of large-scale packages of fiscal reform aimed at rationalizing public spending and boosting revenues. The aim is to consolidate the public budgets and ensure their sustainability, especially in light of the current challenges facing fiscal policy. Tax reforms should be a top priority for fiscal policymakers to boost tax revenues and ensure the equity and efficiency of the tax system through a review of the income and corporate profit tax systems as well as the adoption of value-added taxation. The tax system should also support small and medium enterprises and promising regions. Moreover, attention should be paid to controlling public spending items through rationalization of current expenditure such as limiting wage costs, moving forward in the reform of the commodity subsidy system, and raising the efficiency of investment spending. Attention should also be paid to raising the transparency and efficiency of public budget management and reducing deficits. These reforms must also be accompanied by parallel efforts to raise the efficiency of public debt management and increasing the average maturity of issues, and financing thereof from sources that ensure fiscal sustainability.

From the International Press

After the Panama Papers .. How Some Countries Become Havens for Tax Evasion?
Argaam:

The leaks of Mossack Fonseca, which is a law firm headquartered in Panama, shed light on the complex ways pursued by some of the wealthy to exploit offshore confidential tax systems.

The so-called tax heaven countries are characterized by charging low taxes and sometimes tax-exempting residents and non-residents and by lack of transparency and exchange of information.

The Conversation developed a report on key characteristics of these countries, in which it highlighted methods pursued by those wishing to avoid paying taxes in their home countries.

The Panamanian Company Unveils a Secret World

- The secret files leaked from Mossack Fonseca show that tax havens are used by individuals and companies to hide money from investigators.
- Ways of gaining such money are not necessarily illegal. Public figures such as politicians wish to keep the information on the size of their money secret, and to achieve that they hide their identities using a number of complex legal mechanisms.
- Whether the tax-evader is a rich businessperson or a drug trafficker, the tricks used to prevent keeping track of their finances are similar.
- Panama is not the only tax haven. According to the Financial Secrecy Index 2015, developed by the Tax Justice Network in Switzerland, Hong Kong, the US, Singapore, and the Cayman Islands have legislations regarding secrecy and the scope of offshore financial services.

Shell Companies

- The tax evasion journey begins by establishing an offshore shell company with the help of a law firm such as "Mossack Fonseca."
- These companies demonstrate what looks like a commercial activity, but are in fact shell companies. They manage the money they receive and conceal the identity of its owner.
- Such shell companies compose of lawyers and accountants whose role is to sign documents and put their names on company letters and documents.
- The names of the shell companies' owners are kept secret, so they can hide revenue resulting from any crime or use it for illegal purposes and no monitoring entity can track it.

In Tax Haven Countries:

- Very few questions about the source of funds are asked. Such funds can be used to carry out legal activities such as investment in real estate or illegal activities such as offering bribes.
- The ownership of shell companies can be transferred easily through equity or bond holders. Such procedures were canceled in the UK in 2015. The US has stopped selling bonds of this kind since 1982 in an effort to increase transparency.
- Some countries entered into tax information exchange agreements with tax havens to allow their governments to impose local tax laws interchangeably on demand. Panama signed such agreements with the US only.

Politicians under Pressure

- The leaked papers revealed by the International Consortium of Investigative Journalists put the Prime Minister of Iceland and British Prime Minister under severe pressure.
- The leaks showed that the wife of the Prime Minister of Iceland owned a shell company in the British Virgin Islands called "Wintris Inc" that acquired millions of dollars in bonds in three large Icelandic banks, which collapsed in 2008.

The Legal Situation

- It is not legally prohibited to deal with tax havens. In fact, there may be some legitimate reasons for such acts, especially for investors in hedge funds.
- Investors from unstable countries resort heavily to tax havens, due to their exposure to risks in their home countries from either their governments or criminal gangs.
- Lack of transparency and lack of information sharing can be exploited for illegal purposes, including money laundering, bribery, corruption, tax evasion and other illegal activities.
- Privacy protection laws ensure that offshore tax authorities do not access information concerning complex entities located in tax havens, one of the main reasons for lack of information exchange.
- In 2013, a report by "The Economist" said that about $20 trillion is hidden in offshore accounts around the world, and is mostly used in illegal activities.

Implications for Egypt:

The issue of international tax evasion is one of the issues that Egypt needs to pay attention to urgently in light of its escalation at the international level. Tracking such companies at the international level is very difficult, and requires lawyers with wide experience. Sometimes, a series of companies are affiliated. To prove corruption requires strenuous efforts, and a political will that some countries may lack.

The surprise in the leaks is not the nature, size or quality of shareholders only, particularly that some of the involved names disclose their shares in these companies in their tax reports or financial disclosures, and thus they are not violating the international law. However, the situation turned to hiding information for manipulation or tax evasion purposes, which is the real violation that actually requires tracking and study, and needs international cooperation to face up to such practices, being harmful to the economy.

The Ministry of Finance has previously issued a statement making it clear that Egypt has tax legislations that allow tracking international tax evasions and tax avoidances. Also, Egypt has entered into several agreements to avoid double taxation that allow exchange of information with various countries to combat tax avoidance and evasion. Egypt is also a signatory to multilateral agreements to achieve this goal. All these mechanisms will enable the tax administration in Egypt to obtain information related to international tax evasions and face up to such operations.

The Income Tax Law No. 91/ 2005 addresses these situations by activating the neutral price principle, which governs transactions between related parties in a way that ensures that the real price is set to prevent tax fraud. There are also articles related to rules of combating tax avoidance, whether public or private.

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Global Financial Market Performance

Reuters, Argaam

Japanese stocks fell at the end of Friday trading session, due to investors' profit-taking in the wake of strong gains in the past sessions and worrying Chinese economic data. The Japanese "Nikki" index fell by 0.4 percent to 16,848 points, but scored 6.5 percent in weekly gains. The "Topix" index also fell by about 0.7 percent to 1361 points.

The Chinese stocks fell at the end of Friday's session due to the country's economic growth data, and speculations that the authorities would not launch new stimulus measures. The "Shanghai" Composite Index fell 0.1 percent to 3078 points at closing, but scored a weekly gain of 3.1 percent.

The US stocks fell during Friday trading in conjunction with the fall in oil prices and its negative impact on energy sector performance, in addition to the release of mixed economic data, but the major indices registered weekly gains.

The "Dow Jones" Industrial index fell 28.9 points to 17,897.4 points. The "NASDAQ" index also fell (- 7.6 points) to 4938.2 points, while the "S&P 500" benchmark declined (- 2.1 points) to 2080.7 points.

At a weekly level, the "Dow Jones" index achieved 1.8 percent in gains, "NASDAQ" rose by 1.8 percent, and the broader "S&P 500" recorded weekly gains of 1.6 percent.

In the European markets, "Stoxx Europe 600" benchmark index fell by 0.4 percent to 342.7 points, and achieved gains of 3.3 percent, which are the first since March 11th, and the biggest weekly gains since February.

Also, the British "FTSE 100" index dropped (- 21.3 points) to 6343.7 points. The German "DAX" index fell (-42 points) to 10,051.5 points, while the French "CAC" index declined (- 16.3 points) to 4495.1 points.

On the other hand, gold futures for June delivery jumped at settlement by 0.7 percent, or by $8.10 to $1234.60 an ounce. The precious metal recorded a weekly loss of about 0.8 percent.

In oil markets, the US "NYMEX" fell by 2.8 percent or by $1.14 and closed at $40.36 a barrel, achieving weekly gains of 1.6 percent. The "Brent" index also fell by 1.7 percent or by 74 cents to close at $43.10 a barrel, recording weekly gains of about 2.7 percent.

Markets are watching closely an important meeting on Sunday between major "OPEC" producers, including Saudi Arabia and non-OPEC members such as Russia, to discuss a production freeze proposal.

Implications for Egypt

According to recent financial reports, a significant increase occurred in the impact transmission of shocks from emerging markets to stock prices and exchange rates in advanced economies and emerging markets. This explains more than one-third of the variation in asset yields in these countries. The causes of structural changes in financial markets include expansion of the investment funds sector, which currently includes more individual investors than before. In addition, there has been an increase in the impact of developments in economic fundamentals on developed and emerging market equity markets.

Reports noted that the impact of China's slow economic growth on the local and global equity markets was significant, pointing out that China's stock markets have been adversely affected by devaluation of the Chinese currency in August 2015. They were also affected later by negative data reported about key manufacturing sectors.

The reports showed that increased financial integration among financial markets has contributed to strengthening the impact transmission of equity markets from emerging markets to developed economies at rates ranging between 30 percent and 40 percent. According to the reports, it is believed that the IPO market would acquire more momentum when markets stabilize after the recovery of oil prices. There is also another positive trend, namely, the growing acceptance of Islamic financial products in the global capital markets, which would increase the number of issuances.

We believe that the current situation highlights the powerful opportunities availed by the Egyptian Stock Exchange, which is one of the largest emerging markets in terms of growth during the first quarter of the year and size of available liquidity that is clear from capital increases over the past two years, surpassing EGP 25 billion. Add to this the strong issuances the market has witnessed more recently. The market saw the conduct of a large issuance in excess of one billion pounds in recent days. Such issuance avails greater opportunities to expand significantly the financing of infrastructure and energy projects. It also provides support for small and medium enterprises and helps improve state-owned asset management and the possibility of relying on the money market as a primary financing platform. This will have a positive impact on the growth process during the coming period, but that would require making visible the progress achieved by the Egyptian Stock Exchange in governance and protection of shareholders' equity. It is worth noting that the Egyptian Stock Exchange was selected by the World Bank as one of the best six markets that achieved improvement in the protection of shareholders' rights.