If experience is any guide, President Abdel Fattah al-Sisi's management of the Egyptian economy is in for a rough ride.

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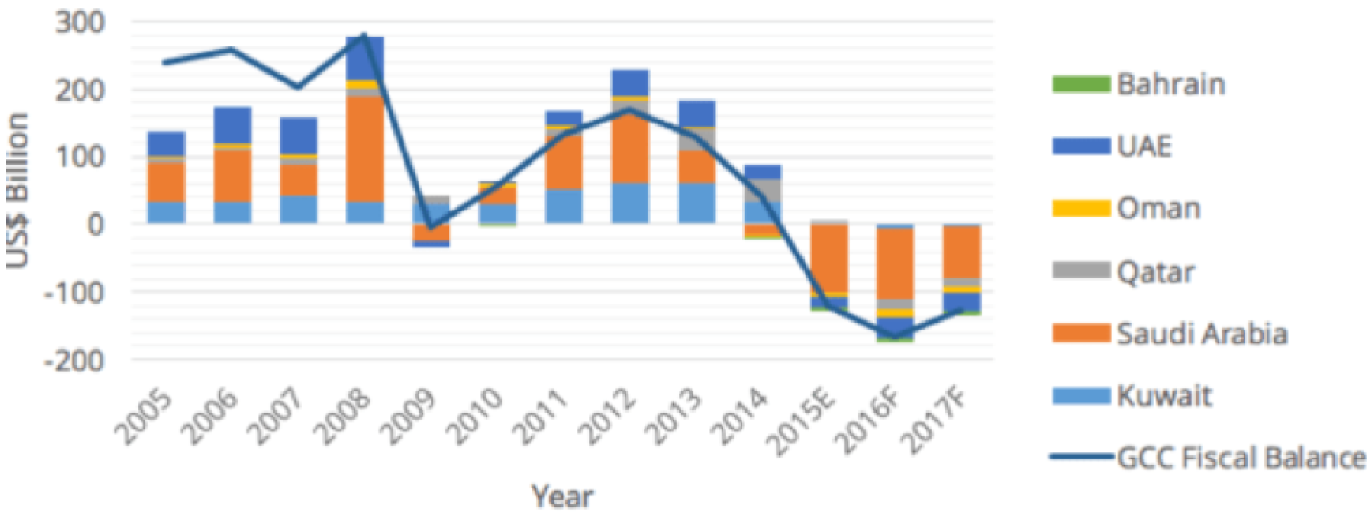
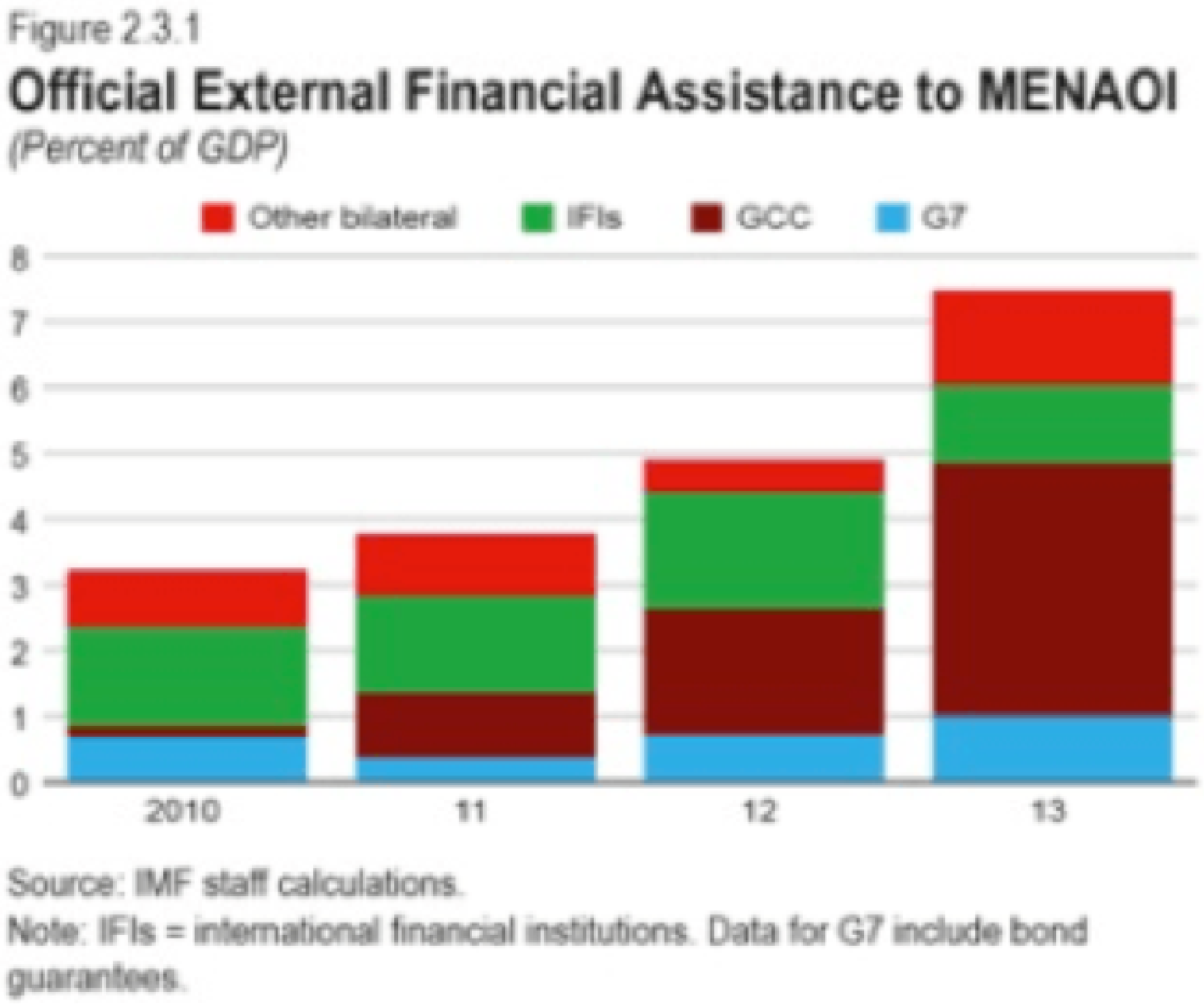
If experience is any guide, President Abdel Fattah al-Sisi's management of the Egyptian economy is in for a rough ride. Sisi now contends that it is up to the Egyptian people to make meaningful economic reforms. In an apparent admission that things have not gone according to plan, he said, "The fighter does not fight alone; his support system – the people – should fight with him."

Egypt has finally pursued a loan agreement with the International Monetary Fund, after months of wishful thinking that the Gulf states would both deliver and extend the largesse they promised in 2013 in the aftermath of Sisi's ascendance to power and the dismantling of the presidency of Mohamed Morsi. Circumstances have changed since 2013, for both the Gulf states and Egypt. Oil prices crashed dramatically in late 2014 and have since failed to rebound, putting all six GCC states into fiscal deficits.



Egypt has failed to implement meaningful subsidy reforms, or to attract foreign investment. Gulf state investment in housing development and infrastructure promised as part of the very optimistic Sharm el Sheikh economic conference in March 2015 has not been delivered. Terrorism has depressed the tourism sector, and many of the proposed investments of Sharm el Sheikh have failed to materialize, including the massive new capital city plan. According to The Economist, annual inflation is at 14 percent and rising, and youth unemployment is at 40 percent.



Egypt is nearing a breaking point and its recent shift in reliance on the Gulf, over the United States and multilateral lenders, could prove a serious miscalculation. After 2013, Egypt relied heavily on Gulf donors and delayed making requests to international financial institutions for loans. In fact, Gulf aid and loans to Egypt (and many other Middle East and North Africa oil importers) has significantly replaced the traditional role of IFIs. The problem with a reliance on the Gulf states is that, unlike multilateral banks and aid organizations, Egypt’s financial health comes second to their own in a time of reduced fiscal revenue. To dig out of its current economic situation, Egypt (specifically Sisi) will need to mend ties with Western donors and IFIs, as well as continue to placate Gulf state donors and investment partners.

Caught between Lenders

One problem is that securing the IMF loan will require that Egypt negotiate additional funds from bilateral sources, most likely the Gulf states. Egypt's financing needs are simply too big for one loan to cover. The IMF has stretched its own lending capacity so that Egypt qualifies not just for a traditional Stand-By Agreement, where repayments are usually in shorter time frames of three to five years, but also an Extended Fund Facility, which will allow Egypt more time to repay the debt, as much as 10 years, and allow the amount of debt to increase above normal allotments in the fund's drawing rights provisions. According to a report by the bank EFG Hermes, the IMF loan is expected to be about $12 billion, though Egypt's financing needs for the next three years are closer to $21 billion. The World Bank and the African Development Bank are expected to lend part of the remaining $9 billion funding gap, but the Gulf states are being tapped for as much as $6 billion. As of August 23, the United Arab Emirates had publicly acknowledged a deposit (though not confirmed by the Central Bank of Egypt) of $1 billion. This is small change compared to the Gulf states' deposits made in 2013 as well the promised investment and aid-in-kind announced. Still undelivered is $4 billion committed by the UAE and Saudi Arabia three years ago.

Country	2011	2012	2013	2014	2015	2016
United Arab Emirates	$3 billion (including $1.5 billion Khalifa bin Zayed fund for housing and SME support) Private reported aid: $22.8 million	$3 billion (including $1.5 billion Khalifa bin Zayed fund for housing and SME support) Private reported aid: $22.8 million	A grant of $1 billion and a further $2 billion deposit to the Central Bank of Egypt; in kind (petroleum and gas) $225 million	$3.21 billion as investment in infrastructure development, and petroleum and agriculture sectors	$4 billion aid package committed to Egypt: $2 billion to the Central Bank of Egypt and $2 billion project finance	Recommitted support/not delivered: $4 billion – half as foreign direct investment and half as a central bank deposit; $1 billion reported Central Bank of Egypt deposit in August

Kingdom of Saudi Arabia			$5 billion aid package: $1 billion cash grant, $2 billion in kind (petroleum and gas), $2 billion deposit to the Central Bank of Egypt		$1 billion pledge to the Central Bank of Egypt; $3 billion investment pledge – thought to combine public and private enterprise, though they are unspecified in media accounts and not included in official ministry announcements	Reported to receive $500 million cash grant as first payment of a $1.5 billion loan from KSA, part of a larger $25 billion package that includes an investment fund and infrastructure projects
Qatar	$500 million cash grant, $2 billion Central Bank of Egypt deposit	$1 billion cash grant; approx. $4 billion Central Bank of Egypt deposit				
Kuwait			$1 billion cash grant; $2 billion Central Bank of Egypt deposit		$4 billion investment pledge	

If the Gulf states had delivered on all of their aid promises to Egypt between 2013 and 2016, would Egypt be in its current financial crisis? The answer is probably yes, and this is why the Gulf states have not delivered on expected deposits and investments. They have considered it wasted money (and their own balance sheets have created domestic demands on spending as well). Even if projects in real estate investment, including construction of the new administrative capital city, had proceeded as planned, there is little indication that these would have addressed problems of youth unemployment or low income housing demand. The investor and public policy priorities were never fully aligned. Add to that a government that was not interested in eliminating a bloated public sector and its affiliated business interests, the reform agenda was doomed to fail. According to Sisi, the army and its Engineering Authority are managing the work of over 2,000 public and private companies in the mega-construction and infrastructure investment schemes. The inability of the state, and the armed forces, to relinquish control over big and small market forces, including the price of meat and the delivery of foodstuffs, continues to stifle economic recovery.

IFIs and the donor community do not always get things right either. The Gulf Cooperation Council replaced the role of IFIs in Egypt in the last three years. The lack of conditionality on the aid and loans, and the volatility of the support is now very evident. Moreover, the interests of Gulf states in promoting their own development agendas, hiring Gulf state-related entities to do construction and infrastructure projects inside Egypt, might not align with the long-term development needs of Egyptians. When those projects are not deemed profitable, or the companies themselves are struggling, the development agenda becomes secondary to both Gulf state and corporate demands.

Calculations change and relationships evolve. Egypt is still important to the Gulf, and the Gulf states cannot afford Egypt in revolution, or simply financial free-fall. As the Gulf states are more integrated into both regional and international economies, they also need Egypt to recover. Egypt’s stability hangs in the balance, with two essential demands: It must raise as much as $5 billion from the Gulf and the Sisi government must secure the remaining policy conditions through Parliament to finalize the IMF deal. The first order of business is to stabilize the depreciation of the Egyptian pound, which continues to decline in value. Bankers expect a float or a major devaluation in the coming weeks. Next, the government must be able to generate revenue internally through an effective tax regime and privatization of state-owned banks and petroleum businesses. The Sisi government has thus far been unable to make meaningful value added tax or income tax reforms, in policy and enforcement. Tourism continues to suffer, particularly as flights remain banned between Russia and Egypt. Remittances from the Gulf have suffered as well, as layoffs in construction firms have hit Egyptian laborers hard.

The Gulf states, particularly the UAE, have pledged to continue to support Egypt, but not to the degree of their stated support in 2013. Their priorities have shifted, as have their resources. However, the region itself is more intertwined, and the stability of Egypt will certainly have ramifications for the Gulf states. It is in the interest of the Gulf states to invest in peace and stability in Egypt. The question is how much will it cost, and is Sisi a credible manager of that investment. There is also an opportunity for the Gulf states to work in partnership with IFIs like the IMF in Egypt’s recovery. This could be an important learning process in the delivery, transparency, and institutionalization of Gulf aid and foreign direct investment, and serve to encourage better coordination among the GCC states in their respective economic statecraft objectives.

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