The Impact of the Financial Crisis on the Developing Countries

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Abstract

The financial crisis has already become a cliché. Stories of bank bailouts, job losses and company closures that were big news in September 2008 are now almost routine. But one thing we have not known until now is exactly how the shockwaves from the crisis have travelled around the world, and how big those shocks are going to be.

During the period 2003-2007, the developing counties experienced an impressive economic boom, growing at a rate of 7% per year. The boom was fuelled by a mix of three ingredients prevailing in global markets: exceptional financing, high commodity prices and large flows of remittances. These conditions have been replaced since September 2008, by the effects of the financial crisis and the worst recession since the Great Depression.

This paper aims to study the causes of this financial crisis and the impact of this financial crisis on developing countries. We will begin with the background about the causes of this financial crisis and the channels of transmission of the crisis. In the final section this paper discusses the impact of this crisis on the Egyptian economy.

Keywords: Financial Crisis, Developing Countries, Capital Flows

JEL Classifications: O11, O50, P34
1. Introduction

Without doubt we are in the middle of a severe financial crisis, the worst since the great depression. A large part of the wealth we thought we had has evaporated. For example, the value of corporate equities has come down substantially during the past decade, from $19.4 trillion in 1999 to $15.2 trillion in 2008. Household net worth in the US (including nonprofit organizations) has gone from $42.1 trillion to $51.7 trillion in 2008.1 At the same time, the consumer price index (CPI) increased by 29% from 1999 to 2008, and the number of households in the US increased to 117 million in 2008 from 104 million in 1999. (Jagannathan et al, 2009)

As a result, the net worth per household in real terms (1999 dollars) declined sharply from $402,000 in 1999 to $343,000 in 2008, i.e., a 15% drop during the past decade. Averages mask the magnitude of the sufferings of the masses. The unemployment rate captures the difficult times of the average citizen even better: it has gone up from 4.4% in 1999 to 7.2% in 2008 – and is currently estimated to be 9.5% (July 2009.) (Krugman, 2008 ; Jagannathan et al, 2009)

This raises the question, why are we in such a financial crisis? The standard answer is easy credit and lax regulation led to the crisis. But then, what caused easy credit and lax regulation? According to popular press, it is due to the savings glut in Asia and the fact that a major part of these savings flow into the US resulting in too much money chasing too few opportunities in the US financial system. Why is there too much saving in Asia and why do those savings flow to the US? Asians just like to save and Americans just like to consume more! According to this logic all that is needed to remedy the situation is to induce Asians to save less and consume more.

In this paper we will first examine the causes, effects, policies, and prospects for the financial crisis and how the financial crisis led to recession in advanced countries and a sharp slowdown in emerging markets. The organization of this paper will be as follows: section 2 shows the causes of the financial crisis, section 3 presents the channels of transmission the crisis. Section 4 shows the impact of this crisis on Egypt. Section 5 presents the concluding marks.
2. Causes of the crisis

There are several papers that introduced the causes of the financial crisis (Blundell-Wignall and Lee, 2008; Krugman, 2008; Soros, 2008) we can summarize these causes as follows:

1. The U.S. dollar is generally weak, and for some good reasons:

a) The war on Iraq has drained the U.S. government financially. To date, the Congress has appropriated almost $356 billion dollars, and the cost of war is escalating. The cost of war is $8 billion per month or $96 billion a year. The war itself is breeding ground for a financial crisis.

The United States is the greatest debtor in the world, and its national debt is currently 8.3 trillion. The current national debt does not include the future obligations for Social Security and Medicare payments. This does not bode well for long-term growth in a debt-ridden economy, making it more vulnerable to a financial crisis.

b) The federal deficit is increasing at an alarming rate, not to mention the unbalanced trade deficit with the rest of the world. This may trigger a global financial crisis caused by the U.S. dollar.

Since President Nixon took the gold standard out of the dollar, the American government has been printing dollars like there is no tomorrow. Some day and somehow these dollars will come home to roost. The dollar’s real worth is only a perception, and such perception may change drastically any time. After all, the dollar is nothing more than fiat money (printed out of thin air), and all fiat money in history eventually went down the drain and became worthless. What makes you think the U.S. dollar is in any way different? A financial crisis may be caused by the devaluation of the U.S. dollar.

c) More and more central banks have announced that they are moving away from the U.S. dollars. Who can blame them? In other words, they may not continue to support the dollars - and that is not good for interest rate, which does not bode well for the stock market, the housing market, and the consumers, who contribute to some 70 percent of the U.S. economy. Without foreign support, rising interest rate may precipitate a financial crisis.

2. The U.S. stock market is still on the upward climb. But the raging bull may have aged, and aged far too much, and is now losing its energy. Frankly, how much further can it run? With little room for upward swing, a severe downturn for the stock market is more likely than not. What goes up must come down, and a financial crisis may accompany the downward swing.
3. The housing market does not bode well. With housing prices continually spiraling down, foreclosures reaching new records, and one trillion dollars worth of mortgages reportedly going to be reset in the year ahead, the U.S. housing market may be heading towards a “harder-than-soft landing.” The worse may not be over as the media would suggest. Max Fraad Wolff in the Asia Times, says housing prices fall 30 percent in a downturn, over a period of about four years. If that is so, this one may still have a long, long way to go down, and a financial crisis may be as inevitable as sunset.

4. No housing boom, no consumer spending. No consumer spending, no economic growth. Without the boom, there will be a bust. This is the major concern for Ben Bernanke, the Federal Reserve Chairman. Shouldn’t it be your concern too for a potential financial crisis?

The U.S. economy depends on consumer spending (70 percent of GDP). Unfortunately, consumers are not earning any more money. So the only way they can increase spending is by borrowing. And what can they borrow against, except their houses? The American culture of spending more than they can earn with the money they don’t have has to come to an end sooner or later. The day of reckoning is inevitable. Hopefully, you are not one of those individuals who endorse and perpetuate this culture of unrestrained spending. Be prepared: any decline in housing may knock the wind out of the consumer, and out of the economy. Expect the unexpected: any downturn in the economy may play havoc with your personal finance. Be prepared for a financial crisis.

The housing boom has created as much as 43 percent of the new jobs added since 2001. An housing boom cannot last forever. Once it is over, many people may lose both their jobs and their credit, and in such times what they need most is what most don’t have - savings. Don’t let yourself be mired in such a dire financial situation.

5. The United States is continuously facing new challenges, not just in the war against terrorism, but the undermining of its overall economic structure. These challenges may bring about a financial crisis.

The United States is gradually losing its financial advantage. While Wall Street still dominates the money world, but not as much as it used to be, now huge fortunes are being made overseas, thanks to the continual trade surpluses enjoyed by the Asian countries. The United States is becoming more dependent on its economic rivals for money, and that is not good.

3. Channels of transmission of the crisis

A preview of the analysis for this year’s Global Economic Prospects report, to be published December 9, 2008, shows that real GDP growth will slow down across developing regions in 2009.
"The direct impact of the crisis is less dramatic in the financial sectors of the poorest countries," said Uri Dadush, Director Development Prospects Group, "but they will be hit nevertheless by slower export growth—global trade is expected to decline by 2.5 percent in 2009—reduced remittances by migrant workers; and lower commodity prices that will affect commodity-exporting countries."

Commenting on the projected decline in world trade, which would be the first such drop since 1982, Mr. Zoellick said, "One of the primary drivers of this is the credit crunch. It's not just the lack of demand for the product, but there's a big gap in trade finance and, it appears, even working capital for some of the shipping firms. So, we at the World Bank had already expanded a trade finance facility that's a pool to $1.5 billion, and we're looking about expanding that."

Table 1 shows the GDP growth forecast for developing countries and these rates decreased across all developing regions.

Table 1: Real GDP growth forecast for developing regions
(percentage change from previous year)

<table>
<thead>
<tr>
<th>Region</th>
<th>2008</th>
<th>2009</th>
</tr>
</thead>
<tbody>
<tr>
<td>East Asia and the Pacific</td>
<td>8.8</td>
<td>6.7</td>
</tr>
<tr>
<td>Europe and Central Asia</td>
<td>6</td>
<td>3.5</td>
</tr>
<tr>
<td>Latin America &amp; Caribbean</td>
<td>4.5</td>
<td>2.1</td>
</tr>
<tr>
<td>Middle East &amp; North Africa</td>
<td>5.7</td>
<td>3.5</td>
</tr>
<tr>
<td>South Asia</td>
<td>6.3</td>
<td>5.4</td>
</tr>
<tr>
<td>Sub-Saharan Africa</td>
<td>5.4</td>
<td>4.6</td>
</tr>
</tbody>
</table>

Source: World Bank, 2009

The crisis can be seen as being driven by the reversal of the three positive shocks that developing countries experienced during the recent booms: rapid growth of remittances, capital flows and trade. We start with a short look at remittances, where the information is not abundant. Then we deal more extensively with capital flows and trade.
3.1 Remittances

For some regions, there is strong evidence of reduced dynamism of remittances. In the case of Latin America, in particular, remittances grew very slowly both in 2007 and 2008, falling as a proportion of GDP in both years, in sharp contrast with the rapid growth earlier in the decade (Griffith-Jones and Ocampo, 2009). The direct sensitivity of migrant incomes to construction activity, which has been falling for three years now, seems to be an important explanation for the absolute reduction of remittances from the U.S to Mexico in 2008, but absolute reductions are still an exception (Lin, 2008).

In contrast, other areas of destinations of migrants, particularly the gulf countries, continued to boom until the third quarter of 2008, and have experienced no significant slowdown in remittances yet. This effect seems to have prevailed so far, but is likely to chain as a result of the steep fall in oil prices. Overall, the World Bank has estimated that remittances to the developing world experienced a lower, but still positive and fairly strong growth in 2008 (7% in 2008 vs. 16% in 2007). However, in 2009 they will face a reduction either small (-1%) or large (-6%) (Razin et al, 2008).

Remittance flows to developing countries are expected to be $304 billion in 2009, down from an estimated $328 billion in 2008, said the World Bank today, releasing new migration and remittances brief to coincide with an International Diaspora and Development Conference running from July 13-14.

The predicted decline in remittances by -7.3% this year is far smaller than that for private flows to developing countries. According to the World Bank, remittances are relatively resilient because, while new migration flows have declined, the number of migrants living overseas has been relatively unaffected by the crisis.

However, sources of risk to the outlook include uncertainty about the depth and duration of the current crisis, unpredictable movements in exchange rates, and the possibility that immigration controls may be tightened further in major destination countries.

"There is a risk that rising unemployment will trigger further immigration restrictions in major destination countries. Such restrictions would curb remittances more than forecast and would slow the global recovery in the same way as
protectionism against trade would endanger a global upturn," explained Hans Timmer, Director of the World Bank’s Development Prospects Group.

Remittances have slowed in many corridors since the last quarter of 2008. In line with a recent downward revision in the World Bank’s forecast of global economic growth, the new update (2009-2011) highlights the impact of the present financial crisis on the remittance flows and, describes broad regional and country specific trends.

Remittance flows to Latin America have been falling in large part because of a slowdown in the US construction sector. The new forecasts show a -6.9 percent decline in remittances for the Latin America and Caribbean region. Sub-Saharan Africa is also likely to experience a -8.3 percent slowdown in its remittance flows.

However, flows to South Asia and East Asia have been strong; but remittances are expected to decline somewhat in 2009. India, China and Mexico retain their position as the top recipients of migrant remittances among developing countries.

Smaller economies such as Tajikistan, Moldova, Tonga, Lesotho, and Guyana are the top recipients in terms of the share of remittances in GDP; which exceeded a quarter of their GDP.

"Remittances provide a lifeline to many poor countries. Although they remain resilient, even a small decline of 7 or 10 percent can pose significant hardships to the people and to governments, especially those facing external financing gaps. Reducing remittance fees and developing innovative tools to leverage remittances for financial inclusion and capital market access should be a part of our response to the financial crisis," said Dilip Ratha, Lead Economist in the Development Prospects Group of the World Bank.

Overall, remittances are likely to show resilience and are, therefore, unlikely to be a major channel of transmission of the crisis.

3.2 Capital Flows

In contrast, one of the key channels for transmission of the crisis from developed to developing countries is via private capital flows. The effects take place both through volumes and associated costs of such flows.
As regards volumes of flows, Foreign Direct Investment (FDI) continued to grow through 2008. Private financial flows peaked from mid 2006 to mid 2007. After short weakening during the third quarter of 2007 due to the sub-prime crisis, they recovered and boomed again during the first quarter of 2008 but dropped very sharply since the third quarter of 2008 and become negative in some cases during the last quarter of the year.

In terms of the cost of financing, although spreads for emerging market bonds have been increasing since mid 2007, this effect was largely counteracted by the reduction of reference interest rates (generally the 10-year U.S. Treasury bond), so that yields did not show a strong upward trend. It was only in June 2008 that yields increased substantially and exploded after the global financial meltdown of mid September 2008.

This behavior of the quantity and price of financial flows has been a major mechanism transmitting movements in stock markets from industrial to developing countries. On average, when measured in dollar terms, stock markets have experienced a stronger contraction in emerging markets since their peak in late October - early November 2007 than stock markets

This impact of the global financial crisis has been more severe for emerging market than for low-income countries, which are less integrated into international private capital markets. Indeed, capital flows to low-income Africa have been relatively limited. It is unfortunate, nonetheless, that the bond issuance that some Sub-Saharan African countries had begun to make has also stopped. Hardest hit were the transition economies of Central and Eastern Europe, where the combination of adverse expectations generated by large current account deficits, high vulnerability of the domestic financial system, or both, led to rapid withdrawals of private capital flows. The reversal of portfolio flows in East and South Asia was large and even surprising in several cases. For South Korea, for example, the Institute of International Finance estimates that foreign investors withdrew a massive net $45 billion in 2008. Countries like India and Taiwan (PRC) also saw negative portfolio investment flows. In Latin America, Brazil and Mexico were hit by losses in derivative markets and, in the first case, by the unwinding of the carry trade. South Africa was also severely hit.
To see which countries are most affected, and why, the following table shows the financial inflows and export earnings in 2008, and the inflows that are now predicted for 2009, for 16 low and middle-income countries. We then compared to the inflows in 2007, before the crisis hit, to get an indication of the impact of the crisis so far. The results are in the table below. Every single country in our sample, and sub-Saharan Africa as a whole, is predicted to see a real drop in inflows between 2007 and 2008.

Table 2: Financial inflows and export earnings, 2007-2009 (Current US$, millions)

<table>
<thead>
<tr>
<th>Country</th>
<th>Total inflows 2007</th>
<th>Total inflows 2008</th>
<th>% change 2007-08</th>
<th>predicted inflows 2009</th>
<th>% change 2007-09</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sub-Saharan Africa</td>
<td>368,373</td>
<td>371,536</td>
<td>0.86</td>
<td>319,077</td>
<td>-13.38</td>
</tr>
<tr>
<td>South Africa</td>
<td>118,022</td>
<td>95,203</td>
<td>-19.33</td>
<td>62,307</td>
<td>-47.21</td>
</tr>
<tr>
<td>Estonia</td>
<td>19,509</td>
<td>16,052</td>
<td>-17.72</td>
<td>11,200</td>
<td>-42.59</td>
</tr>
<tr>
<td>Korea</td>
<td>391,344</td>
<td>391,437</td>
<td>0.02</td>
<td>243,458</td>
<td>-37.79</td>
</tr>
<tr>
<td>Turkey</td>
<td>167,316</td>
<td>147,738</td>
<td>-11.70</td>
<td>109,871</td>
<td>-34.33</td>
</tr>
<tr>
<td>Brazil</td>
<td>255,005</td>
<td>219,845</td>
<td>-13.79</td>
<td>176,816</td>
<td>-30.66</td>
</tr>
<tr>
<td>Russia</td>
<td>481,195</td>
<td>500,475</td>
<td>4.01</td>
<td>338,667</td>
<td>-29.62</td>
</tr>
<tr>
<td>India</td>
<td>247,932</td>
<td>222,825</td>
<td>-10.13</td>
<td>175,344</td>
<td>-29.28</td>
</tr>
<tr>
<td>Nigeria</td>
<td>95,500</td>
<td>115,777</td>
<td>21.23</td>
<td>71,133</td>
<td>-25.52</td>
</tr>
<tr>
<td>Venezuela</td>
<td>68,934</td>
<td>94,021</td>
<td>36.39</td>
<td>52,862</td>
<td>-23.32</td>
</tr>
<tr>
<td>China</td>
<td>1,372,763</td>
<td>1,446,750</td>
<td>5.39</td>
<td>1,075,844</td>
<td>-21.63</td>
</tr>
<tr>
<td>Ghana</td>
<td>6,748</td>
<td>6,698</td>
<td>-0.74</td>
<td>5,260</td>
<td>-22.05</td>
</tr>
<tr>
<td>Jamaica</td>
<td>5,466</td>
<td>5,282</td>
<td>-3.37</td>
<td>4,468</td>
<td>-18.26</td>
</tr>
<tr>
<td>Malaysia</td>
<td>193,857</td>
<td>199,362</td>
<td>2.84</td>
<td>161,791</td>
<td>-16.54</td>
</tr>
<tr>
<td>Uganda</td>
<td>4,650</td>
<td>4,601</td>
<td>-1.05</td>
<td>4,228</td>
<td>-9.08</td>
</tr>
<tr>
<td>Chile</td>
<td>79,619</td>
<td>75,627</td>
<td>-5.01</td>
<td>74,591</td>
<td>-6.32</td>
</tr>
<tr>
<td>Mali</td>
<td>2,776</td>
<td>2,782</td>
<td>0.22</td>
<td>2,600</td>
<td>-6.34</td>
</tr>
</tbody>
</table>

Source: Action Aid, March 2009

3.3 Trade

In recent decades, world trade has shown two important characteristics. First of all, it has tended to expand more rapidly than world production, a process that has been
accompanied by a rapid diversification in the trade structure. Thus, during the recent boom, in 2003-2006, world trade grew at an annual rate of 9.3%, more than twice the rate of growth of world output (3.8%). Second, these rates of growth have been highly elastic to world output through the business cycle and have, therefore, been more volatile than world production. A major implication of this characteristic is that, although trade enhances world business cycle upswings, it equally tends to multiply downswings. Trade volumes contracted in 2001 and will again contract in 2009. The growth of trade volume experienced a strong slowdown since mid-2007, to a rate of around 2% by September 2008. This rate turned negative in November and December if we are to judge from reports that indicate that even China, the most dynamic world exporter, experienced negative export growth and even sharper negative import growth in those months.

While this recession in trade volumes will be the main channel of transmission of the crisis to exporters of manufactures and services (tourism being a major service export for many developing countries), price developments will dominate the export performance of exporters of primary goods. In recent years, the world economy experienced the most impressive commodity boom in more than a century, both in terms of duration (five years), intensity and product coverage (World Bank, 2009, chapter 2). The boom was more pronounced for minerals, including oil and other energy products, than for agricultural goods. This is reflected in the fact that whereas at the peak around the second quarter of 2008 the real prices of minerals exceeded the average of the 1970s by considerable margins (more in the case of energy products but also significantly in the case of metals), real agricultural prices went only briefly back to the level of the 1970s. It was, in other words, a boom of mineral, not agricultural prices (Ocampo and Parra, 2008). A major reflection of this fact is that, whereas the terms of trade of mineral exporting countries improved significantly, those of agricultural exporters remained flat and those of manufacturing exporters deteriorated (United Nations, 2009, Figure II.6).

This difference seems to reflect diverse determinants behind the associated price trends among commodity groups. For mineral exports, the dominant issue has been the underinvestment generated by a long period of low prices over the last two decades of the twentieth century. Given the higher demand propelled by rapid growth in the developing world and specifically, the high demand of China for metals, prices boomed. Investment increased, but there were significant lags in the transformation of new projects into increased supplies. In the case of agriculture, the disproportion between supply and demand was more moderate, though the growing demand for biofuels operated as a major mechanism of transmission of high energy prices into higher agricultural prices, particularly during the second semester of 2007 and the first semester of 2008 - the last phase of the commodity price boom.
Additional factors affecting commodity prices during the latest phase of the boom were dollar exchange rate volatility and financial speculation. These factors resulted in an unprecedented level of price volatility. The turnaround of price trends took place since July for most commodities and since August for energy products and therefore preceded the financial collapse of mid-September. But the worldwide credit freeze that followed led to a free fall for most commodities. Energy products and metals, which had experienced the most impressive price boom, were also hit more severely.

Prospects for commodity prices remain poor. They are already below (and, in some cases, including oil, well below) the most recent projections released by the World Bank, which forecasted a 25 per cent reduction in energy prices in 2009 and 23 per cent fall in non-energy commodity prices (World Bank, 2009, Table 1.4). The fact that many oil exporting countries and some metal exporters have stabilization funds in place will serve as an important cushion. For agricultural exporters, such a cushion does not generally exist.

Falling energy prices bring a major benefit for a significant number of energy importing developing countries. Indeed, one reason behind the large number of developing countries with growing current account deficits had been the effect of high energy prices. So, falling energy prices will affect energy exporting countries but benefit a relatively large number of energy importing developing countries. Falling prices will be reflected in reduced investment and economic activity in commodity dependent developing countries, the number of which is still relatively large, particularly in Africa, the Middle East, North Africa, and Latin America. Indeed, low commodity prices will be the major mechanism of transmission of the world crises to poor countries. For these countries, a major opportunity ahead is to redesign their trade strategy to reduce their commodity dependence.

4. The impact of the financial crisis on Egypt

Originating from the turmoil of the U.S. financial sector, the financial crisis has been spreading to most areas in the world, including Egypt. In the second half of 2008, the negative consequences of the financial crisis began to bite the Egyptian economy in many fields, particularly the prime sectors which contributed to the country's revenues.

At the beginning of the financial crisis, Prime Minister Ahmed Nazef has said the ongoing global crisis could impact his country on three aspects, namely the banking
sectors, the stock market and the growth rate of the economy. Egypt was confident that the banking system, which experienced reforms in the past years, is strong enough to face the challenges of the crisis.

Nazif has repeatedly voiced his confidence that the Egyptian banking system has the capability of fully absorbing the international financial crisis "without any negative impact."

The global meltdown has had calamitous consequences for Egypt's economy and 25 million strong labour force. A parliamentary report released in March 2009 revealed that gross domestic product (GDP) growth fell to 4.1 percent in the last quarter of 2008, from 7.2 percent during the previous fiscal year. As a result of the contraction, up to half a million Egyptians are expected to lose their jobs this year.

Companies suffering losses began restructuring and retrenching staff in late 2008. The first wave of layoffs and cutbacks targeted temporary staff and factory workers, among the lowest paid in the country. Over 100,000 workers were laid off during the six months ending March 2009, according to a senior official.

Retrenched workers say that managers pressured them into early retirement, or dismissed them without providing due severance packages continued employment. Firms have also slashed salaries and bonuses, withdrawn benefits, or transferred workers to lower-paying positions.

Egypt has committed 5.4 billion dollars to an economic stimulus plan to confront the repercussions of the global financial crisis. The allocation has been earmarked for infrastructure projects and export subsidies aimed at compensating for falling foreign direct investment (FDI) and declining overseas demand.

Labour rights groups argue that the government's economic policies target job creation, but are backed by a legal framework that protects the interests of the nation's business magnates. Companies have been given broad discretion in handling their workforce, leaving the door open to abuse.

Egypt's unemployment rate climbed to 9.4 percent in the first quarter of 2009, from 8.8 percent the previous quarter. The rising rate is a setback to poverty alleviation efforts, putting additional burden on the 15 million Egyptians living below the two dollars per day poverty line.

"When GDP growth falls and unemployment soars, it is always the poor who suffer most," says Abdel Fatah El-Gebaly, an economist at the Al-Ahram Centre for
Political and Strategic Studies. "The poverty rate in Egypt...will certainly increase as a result of this crisis."

Deteriorating economic conditions have compelled workers in many sectors to defy the state's long-standing ban on labour strikes. They say the illegal industrial action is necessary because the state colludes with companies to exploit cheap labour, and unions are toothless institutions controlled by the ruling party's cronies.

Striking workers have demanded wages and bonuses that have been withheld by their employers, as well as job security and better working conditions.

Labour rights groups have called for the government activate two national funds intended to support workers laid off as a result of a company's downsizing or going into bankruptcy. Yet both funds were designed in ways that, despite outward appearances, offer workers very little by way of assistance.

One fund may only be activated after a company is bankrupt, liquidated and its employees are dismissed by a court sentence - and even then is subject to approval. The other stipulates that in the case of a company's downsizing or closure, retrenched employees are to receive a monthly disbursement equal to 75 percent of their basic salary.

And there may be little incentive for the government to mend the holes in its unemployment assistance programmes. Egypt's 2009-10 state budget forecasts a deficit of 18 billion dollars, or 8.5 percent of GDP - a 25 percent increase over last year due to a sharp decline in revenues. Budget committees armed with scalpels appear unlikely to approve any measures that would increase expenditure.

(END/2009)

However, such impacts has spread to the country's major sources of revenues, including tourism industry, energy exports, Suez Canal tolls and remittances from expatriate workers.

Tourism industry has always been one of the major industries of Egypt. In 2008, it was reported that some 12.8 million people all over the world travelled to Egypt and brought some 11 billion U.S. dollars to the country's revenue, or some 8.5 percent of the Egyptian Gross Domestic Product (GDP).

But statistics indicate that the growth rate of foreign tourists has dropped since last October. The booking rate of the hotels in the Red Sea resorts was only some 40 percent.
According to the Egyptian Travel Agencies' Association, increase of foreign tourists in the next four years is only predicted at 6 percent, compared to some 16.6 percent in the past four years.

In the fiscal year of 2007-2008, remittances from expatriate workers reached 8.5 billion dollars. But most Egyptian emigrant workers live in Gulf countries, which are also struggling to get rid of the negative impacts of the financial crisis.

Some Egyptian workers in Gulf countries have been laid off due to shrinking investments. It is reported that some 30,000 Egyptian workers in Gulf countries are expected to return home and join the unemployed.

The revenue of the Suez Canal, which hit a record 5.2 billion dollars last year, has been one of the most stable sources of the Egyptian income. The revenue has also dropped recently due to decreased numbers of ships via the international waterway caused by the global crisis and the fears over the pirates off the Somali coasts near the Red Sea waters.

According to the state, Suez Canal revenues stood at 301.8 million dollars in February, or some 25 percent drop compared to the 408-million-dollar income the same period of last year.

The Egyptian government has vowed to take measures to boost the economy growth rate, but is still facing challenges to ride out the global crisis.

Conclusions

The recent crisis was initiated as a result the so-called mortgage crisis, The real estates in America are the largest source of lending and borrowing, where the citizen can buy his house from the bank funding under this property mortgaging. When the value of the property goes up, the property owner tries to get a new loan due to increase of real estate price, for a second class new mortgage. Hence the second class new mortgages are labeled and considered “Lower Quality Mortgages” as they are more vulnerable to risk if property values fell.

To sum up, If there are three elements we will have a financial problem
1. Increased Unstudied and borrowing and ill-considered rules of Banking credit
2. Concentration of risk in specific sectors
3. Lack of control and supervision
If we add to these three elements the loss or lack of confidence in the financial system, they will be sufficient to bring about a deep crisis, that does not affect only the financial sector but has an impact on the economic system as a whole and reflect on the rest of the world’s economies by financial globalization.

The crisis can be seen as being driven by the reversal of the three positive shocks that developing countries experienced during the recent booms: rapid growth of remittances, capital flows and trade. We found that the impact of the crisis on the developing countries through these channels is very big. Moreover, the impact of this crisis on the Egyptian economy is big as well.

References


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