PIIE PETERSON INSTITUTE FOR INTERNATIONAL ECONOMICS

POLICY BRIEF

24-6 Egypt's 2023–24 Economic Crisis

Will This Time Be Different?

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I. INTRODUCTION

The modern history of Egypt has been marked by recurring economic crises temporarily resolved by an infusion of assistance from international lenders. Most recently, the country narrowly averted a full-blown crisis earlier in 2024. This crisis was one in a series attributable to Egypt's longstanding insistence on maintaining an overvalued currency through fixed exchange rates. It was also exacerbated to some degree by events beyond its control, including the global economic downturn of the COVID-19 pandemic and disrupted food supplies feeding inflation due to the war in Ukraine. In addition, the war in Gaza since October 2023 has intensified the strains because of interruptions in vital sources of foreign exchange earnings.

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In this as in previous instances, international assistance has been provided at least in part because of Egypt's critical importance for stability in the Middle East. The recent crisis was stabilized when the International Monetary Fund (IMF) led the international community, including wealthy nations in the Persian Gulf region, in mobilizing substantial financial support to address Egypt's large financing needs.

In accepting the most recent assistance to shore up foreign exchange reserves, the Egyptian authorities enacted a series of measures to stabilize the economy, allowing significant devaluations of the exchange rate in 2023 and 2024 and committing to a more flexible exchange rate regime—the latter encouraged by international lenders. To its credit, the government has also taken some difficult steps to curb budgetary spending, including reducing subsidies.

And the authorities have indicated that they will curtail the role of the military in the economy—a longstanding reform that was committed to before and not undertaken. These interventions have temporarily remedied the situation. But have they improved the country's economic trajectory for the long term? The answer is less certain.

The key question now is: Will Egypt undertake deeper reforms that will durably fix its recurring economic difficulties, or will it again postpone reforms, betting that the current crisis will pass and that the international community will bail it out again in future crises? This Policy Brief traces the origins and developments of the current crisis, and the country's history of repeated balance of payments (BOP) crises.

Egypt has gone through at least eight such crises since its establishment as a republic in 1952. The chronic problem has been a pattern of BOP difficulties that have often required the abandonment of a fixed or highly stabilized exchange rate but been followed by a return to stable exchange rates once the crisis has subsided. This pattern is rooted not just in a belief in the merits of fixed exchange rates but also in Egypt's political economy, especially its state-/military-dominated governance structure.

Because of its importance as the most populous country in the world's most volatile region, Egypt has been able time and again to rely on international financial support thanks to its "too strategic to fail" position. But it is not clear that the latest crisis and the most recent IMF program (which was agreed in December 2022 and resumed in March 2024) can break this cycle and foster genuine economic resilience through deep reform of the country's institutions and policies.

Egypt's geopolitical significance may well enable it to continue securing international bailouts without fundamental reform. The country's elites have strong incentives to maintain the status quo, making unlikely the implementation of necessary reforms, such as reducing the military's economic role and ending cronyism. Furthermore, Egypt's ability to secure geopolitical rents, including in the form of support from the international financial organizations and major donors, allows the authorities to continue to bet on weathering future crises without significant reforms.

This Policy Brief is organized as follows: Section II reviews the recent crisis, section III examines the key features of Egypt's BOP crises since 1952, section IV presents some thoughts on the reasons behind the pattern of repeated crises, and section V discusses the prospects of Egypt breaking its pattern of crises and reform.

II. THE 2023–24 CRISIS

Egypt has been grappling with deep-seated economic challenges for years, due to distorted prices and incentives, sprawling but misdirected subsidies, pervasive governance shortcomings, and weak macroeconomic policies. These factors have led to long-running fiscal and current account deficits, low growth, escalating youth unemployment, burgeoning debt, and at times rapid inflation.[1] Central to these issues has been the government's insistence on intervening to

1 On Egypt's debt problems, see Mazarei (2023).

stabilize the exchange rate against a backdrop of dwindling foreign investment and aid, notably from Gulf Cooperation Council (GCC) countries,[2] and declining remittances. This confluence of factors, coupled with the effects of the COVID-19 pandemic and the war in Ukraine, eroded Egypt's foreign reserves and commercial banks' net foreign exchange positions to dangerously low levels, increased the gap between the official and parallel market exchange rates, and led to high inflation and a backlog of external payments, all threatening economic stability.

The situation took a dire turn with the outbreak of the war in Gaza in October 2023. The ensuing interruptions in navigation on the Red Sea and in tourism exacerbated Egypt's woes and introduced new adversities, particularly affecting vital sources of foreign exchange earnings from tourism and the Suez Canal (UNDP 2024). The ripple effects of this turmoil manifested in a precipitous decline in the exchange rate on the parallel market (whose premium exceeded 100 percent), rising credit default swap rates, an increasingly pessimistic outlook from credit rating agencies, and a widening of the current account deficit.[3] Facing a looming economic crisis, Egypt found itself at a crossroads, necessitating immediate and decisive action.

But the Gaza war also raised Egypt's geopolitical significance, catalyzing immediate international financial support. Several international partners, previously hesitant because of Egypt's reluctance to undertake substantive reforms, rallied to its aid. The European Union, IMF, UAE, and World Bank provided a financial infusion of over $50 billion, enabling Egypt to avert a potential BOP disaster. The country already had agreed on a program with the IMF in December 2022, but that had been suspended because of Egypt's lack of reforms (IMF 2023). It was resuscitated and augmented from about $3 billion to $8 billion in March 2024 as geopolitics intervened.

Compelled by its worsening situation due to the war in Gaza, and to facilitate external assistance, Egypt agreed to enact a series of economic measures. The main step thus far has been a sharp devaluation of the exchange rate by 38 percent and unification of the exchange rate system, supported by a hike in interest rates by 600 basis points.[4] In addition, Egypt has pledged to curtail the proliferation of large infrastructure projects and reform the subsidy system, to control budgetary spending. It has also pledged to mitigate the military's pervasive influence over the economy and improve the playing field for the private sector.[5] And in June 2024, to help address its fiscal budget problems, Egypt raised the price of subsidized bread by 300 percent, a major step with potentially serious political consequences due to its widespread impact on the general population.

2 The GCC countries are Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, and the United Arab Emirates (UAE).

3 Egypt's external current account deficit was expected to jump to 6.3 percent of GDP in FY2023/24 (July 2023–June 2024) from 1.2 percent of GDP a year earlier (IMF 2024a).

4 Prior to the liberalization, there were tight restrictions on the provision of foreign exchange by the banking system. The liberalization of the foreign exchange system included clearance of the backlog on foreign exchange payments in the banking system (IMF 2024b). The limit on international currency transfers was also removed in June 2024.

5 Steps to be taken to support the private sector include strengthening the independence of the competition authority, streamlining investment procedures, and reducing corruption.

Most of the foregoing have been longstanding but unfulfilled commitments to the IMF in previous programs. Yet the measures were met with optimism in capital markets, leading lenders to momentarily overlook Egypt's continuing hesitation to truly dismantle its policy framework that has led to successive cycles of exchange rate fixing or stabilization and devaluations.

III. EIGHT BALANCE OF PAYMENTS (BOP) CRISES SINCE 1952

Since 1952, Egypt has experienced eight significant balance of payments crises, each following a familiar pattern: structural current account and budget deficits financed by external assistance and debt, leading to occasional BOP and fiscal crises.[6] Throughout this period, Egypt's trade policies have been characterized by import substitution, the budget has suffered from structural weaknesses due to excess spending (including on food and fuel subsidies), and revenue sources (e.g., associated with the Suez Canal, petroleum exports, and international aid) have been susceptible to exogenous shocks.

Table 1 describes the eight BOP difficulties and devaluations, six of them associated with the use of IMF financing. Table 2 shows the changes in Egypt's de facto exchange rate regime since 1999. Because the IMF database does not report such data for earlier years, we report in table 3 the classification of Egypt's de facto exchange rate regime in 1931–2019 based on the work of Ethan Ilzetzki, Carmen Reinhart, and Kenneth Rogoff (2021).[7]

The nationalist, state-led, and inward-looking economic framework that Egypt adopted in 1952 involved significant economic controls, state intervention, widespread nationalizations, and land reform. Over the decades since, Egypt has faced numerous domestic political changes, wars, shifts in global political alignments, regional conflicts, and terms-of-trade shocks. These factors have contributed to the recurring pattern of BOP difficulties.

What emerges from our examination is a consistent pattern of BOP difficulties against the backdrop of exchange rate pegs, often involving segmentation of the foreign currency market and multiple exchange rates, as well as currency substitution.[8] This has led to repeated overvaluation of the real effective exchange rate (REER), sometimes accompanied by tightening of exchange rate restrictions. These overvaluations have typically necessitated abrupt adjustments through devaluations or, in more recent years, temporary

6 There was also a crisis in 1876, brought about by a debt default. In the mid-1800s, Egypt embarked on ambitious modernization projects, including the construction of railways, telegraph lines, and the Suez Canal. These projects, while crucial for development, were financed primarily through external debt, and by 1876 the country faced a severe financial crisis due to its inability to service this mounting debt, culminating in a default. This default led to the establishment of the Caisse de la Dette Publique, an international commission designed to oversee Egypt's debt repayment and manage its finances. This early instance of international financial oversight highlighted Egypt's early struggles with external debt and set a precedent for future economic interventions.

7 The Ilzetzki, Reinhart, and Rogoff (2021) data, which are broadly in line with IMF data, also show episodes when Egypt used multiple exchange rates.

8 On currency substitution in Egypt, see El-Erian (1987).

Table 1
Egypt's eight balance of payments (BOP) crises, 1956–2024

	Year	Episode	Devaluation date/details	Description
1	1956	**The Suez Crisis**	Partial devaluation	Borrowed $15 million in 1956 from the IMF to stabilize the economy during the Suez Crisis
2	1960s	**Repegging of 1962 & Subsequent BOP Pressures**	Switch from sterling peg to US dollar peg in 1962. Devaluation from E£1 = US$2.87 to E£1 = US$2.30 (20% devaluation)	Two Stand-By Arrangements from the IMF totaling 82 million SDR in 1962 and 1964
3	1970s	**The 1973 Multiple Exchange Rate System**	Partial devaluation	By adding a premium/surcharge of 50–55% to the official exchange rate ($2.56), the Egyptian pound was effectively devalued to $1.70–1.64
4	1978–79	**The 1979 Devaluation**	Devaluation in 1979 from E£1 = US$2.5 to E£1 = US$1.43 (a 44% devaluation)	Secured an IMF Extended Fund Facility worth SDR 600 million in 1978.
5	1989–91	**Devaluations of 1989 and 1991**	Devaluations: E£1 = US$0.91 (a 36% devaluation) in 1989, E£1 = US$0.5 in 1990 (a 45% devaluation), and E£1 = US$0.3 in 1991 (a 40% devaluation)	IMF Stand-By Arrangements of 1987 and 1991; Paris Club Debt Treatments in 1987 and 1991
6	2002–03	**The 2002 Devaluation & the 2003 Float**	Depreciation to E£1 = US$0.22 in 2002; float in January 2003	Float aimed to eliminate the parallel market for foreign exchange
7	2016	**The 2016 Devaluation**	Depreciation to E£1 = US$0.06 in November 2016 (a 45% devaluation)	Transitioned to a liberalized exchange rate regime briefly as part of an IMF Extended Fund Facility program
8	2023–24	**Two Devaluations of 2023 and 2024**	Depreciation to E£1 = US$0.03 in January 2023 (a 40 percent devaluation); flotation in March 2024 with the pound valued officially at about US$0.02	Flotation aimed to curb inflation and attract foreign investment, increasing the IMF bailout loan to $8 billion

SDRs = Special Drawing Rights
Source: Authors' analysis based on various sources.

Table 2

Egypt's de facto exchange rate regimes, 1999–2024: IMF data

Year	Category	IMF program arranged or resumed
1999	Conventional pegged arrangement	
2000	Pegged exchange rate within horizontal bands	
2001	Pegged exchange rate within horizontal bands	
2002	Managed floating with no predetermined path for the exchange rate	
2003	Managed floating with no predetermined path for the exchange rate	
2004	Managed floating with no predetermined path for the exchange rate	
2005	Conventional pegged arrangement	
2006	Conventional pegged arrangement	
2007	Managed floating with no predetermined path for the exchange rate	
2008	Other managed arrangement	
2009	Other managed arrangement	
2010	Crawl-like arrangement	
2011	Stabilized arrangement	
2012	Crawl-like arrangement	
2013	Stabilized arrangement	
2014	Stabilized arrangement	
2015	Other managed arrangement	
2016	Floating	EFF
2017	Stabilized arrangement	
2018	Stabilized arrangement	
2019	Crawl-like arrangement	
2020	Stabilized arrangement	RFI, SBA
2021	Stabilized arrangement	
2022	Floating	EFF
2023	Stabilized arrangement	
2024	Floating	EFF

Source: IMF AREAER database (IMF 2022), authors' classifications.

Note: The *Annual Report on Exchange Arrangements and Exchange Restrictions* (AREAER) tracks the exchange rate and trade regimes of all members of the International Monetary Fund (IMF). Data on the classification of arrangements are available from 1999 to 2007 and from 2008 to 2021, with the later period reflecting a revised methodology. The authors extended the data for 2022 to 2024, for which the AREAER database has yet to report. Light blue shading under the Category column signifies a de facto floating exchange rate regime.

The Extended Fund Facility (EFF) provides financial assistance to countries facing serious medium-term balance of payments problems due to structural weaknesses that require time to address. The Stand-by Arrangement (SBA) offers short-term financial assistance to countries experiencing balance of payments issues. The Rapid Financing Instrument (RFI) provides prompt financial assistance to any IMF member country with an urgent balance of payments need. The SBA and RFI programs for Egypt, arranged in the context of COVID-19 in 2020, did not include extensive conditionality.

Table 3
Egypt's de facto exchange rate regimes, 1931–2019, based on Ilzetzki, Reinhart, and Rogoff (2021)

Date	Classification Primary/Secondary/Tertiary	Comments
September 29, 1931–1950	Peg	UK pound. Suspension of Gold Standard, remained in Sterling Area until July 14, 1947 but continued to be linked to the pound.
1950–May 7, 1962	Managed floating/Multiple exchange rates	Links to US dollar
May 7, 1962–July 25, 1971	De facto crawling band /Multiple exchange rates	+/–5% band; US dollar. Official rate is pegged to US dollar and periodically adjusted. Parallel market premium remains consistently above 150%.
July 25, 1971–October 8, 1991	De facto crawling band /Multiple exchange rates	+/–5% band; US dollar
October 8, 1991–January 30, 2001	De facto peg to US dollar/Multiple exchange rates	Parallel market premium is in single digits through December 1998, when the data ends.
January 30, 2001–June 2015	De facto crawling peg	US dollar. On January 30, 2001 rates are unified. A horizontal +/–1% band is announced.
July 2015–December 2019	De facto crawling band	US dollar +/–2%

Source: Ilzetzki, Reinhart, and Rogoff (2021).

moves to a floating exchange rate, followed by a quick return to a highly stable or fixed exchange rate regime. Figures 1 and 2 show developments in the exchange rate and the REER of the Egyptian pound (E£) since 1952.

There have been subtle forms of devaluation at times, such as the introduction of more depreciated rates alongside the main par exchange rate, sometimes in the form of premia and surcharges over the base exchange rate (Hansen and Nashashibi 1975). In nearly all episodes, Egypt borrowed from the IMF, sometimes using facilities that involved conditionality and sometimes those that did not, as well as from other sources (table 4).

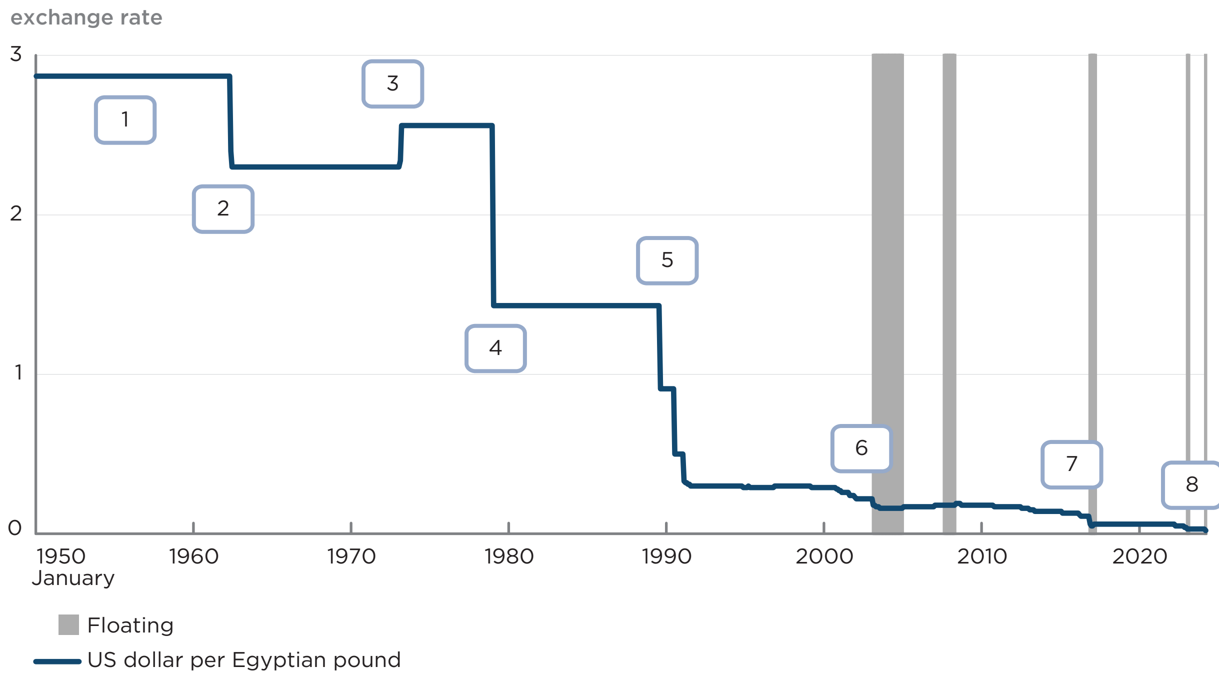
As illustrated in the following sections, Egypt's eight BOP crises—roughly one per decade—reflect a pattern of preceding overvaluation and restrictive exchange rate measures, and subsequent devaluations or temporary floating regimes.

1. The 1956 Suez Crisis

President Gamal Abdel Nasser's nationalization of the Suez Canal in July 1956 led to military intervention by Britain, France, and Israel, severely disrupting trade and resulting in economic turmoil for Egypt (Boughton 1997, Ikram 2021). This period also saw Egypt's geopolitical reorientation toward the Soviet Union and the Eastern Bloc. Egypt's foreign currency holdings in Britain, France, and the United States were frozen (Owen 1991).

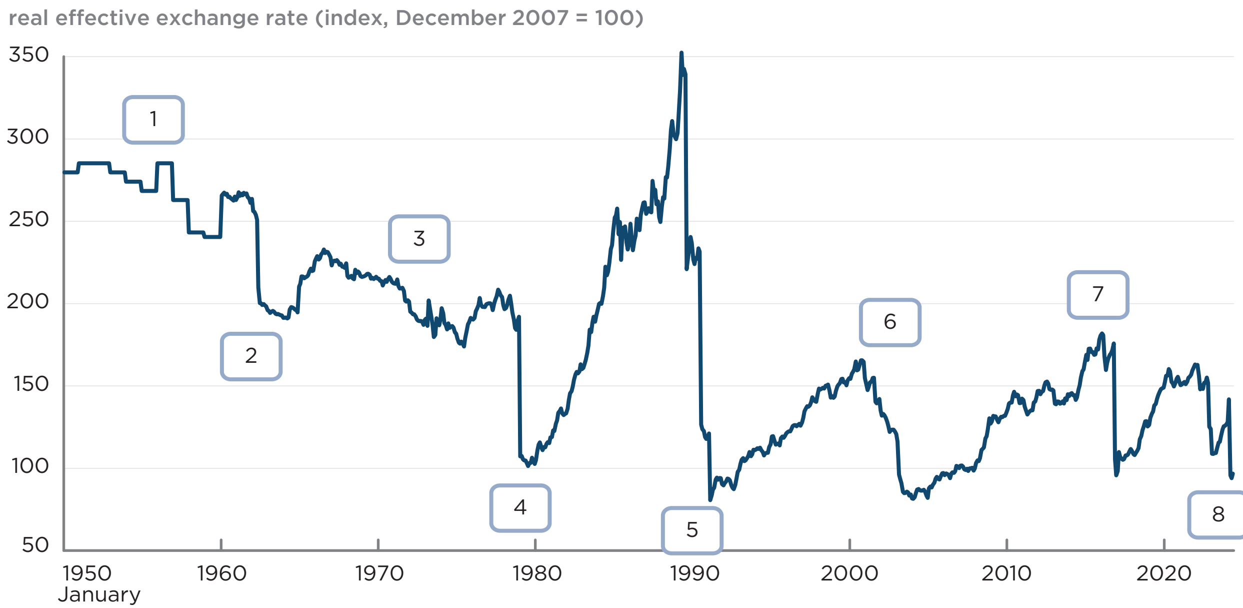
To manage the economic fallout, Egypt borrowed SDR15 million from the IMF in September 1956 and a de facto devaluation was implemented through an

Figure 1
Official exchange rate of Egypt in the context of eight financial crises, 1950–2024



Source: CEIC data. Classification of floating regime is based on IMF classification.

Figure 2
Real effective exchange rate of Egypt, in the context of eight financial crises, 1952–2024



Source: Darvas Real Effective Exchange Rate Database; IMF AREAER Database (IMF 2022); authors' classifications.

Table 4
Egypt's history of IMF borrowings, 1956–2024

Facility	Date	Amount agreed (in millions of SDRs)	Amount drawn (in millions of SDRs)	Quota (in millions of SDRs)	Percent of quota (percent)	Major event
Major Programs						
Stand-By Arrangement	May-1962	43	43	90	47	Devaluation
Stand-By Arrangement	May-1964	40	40	120	33	
Stand-By Arrangement	Apr-1977	125	105	188	66	Devaluation
Extended Fund Facility	Jul-1978	600	75	288	208	
Stand-By Arrangement	May-1987	250	116	342	73	Devaluation
Stand-By Arrangement	May-1991	234	147	463	51	Devaluation
Extended Fund Facility	Nov-2016	8,597	8,597	2,037	422	Devaluation
Extended Fund Facility	Dec-2022	2,350	261	2,037	115	Devaluation
Extended Fund Facility (Augmentation)	Mar-2024	3,762	618	2,037	185	Devaluation
Other Arrangements with No/Limited Conditionality						
Gold Tranche Borrowing	Sep-1956	15	15	60	25	Suez Crisis
First Credit Tranche Borrowing	Feb-1957	15	15	60	25	Suez Crisis
Compensatory Financing Facility	Oct-1963	16	16	90	18	
Compensatory Financing Facility	Mar-1968	23	23	150	15	
Upper Credit Tranche Borrowing	Mar-1968	40	40	150	27	
First Credit Tranche Borrowing	Jul-1970	18	18	150	12	
First Credit Tranche Borrowing	Sep-1971	32	32	188	17	
Rapid Financing Instrument	May-2020	2,037	2,037	2,037	100	COVID-19
Stand-By Arrangement	Jun-2020	3,764	2,606	2,037	185	COVID-19
Other Arrangements with No Amounts Drawn						
Extended Fund Facility	Sep-1993	400	—	678	59	
Stand-By Arrangement	Oct-1996	271	—	678	40	
Stand-By Arrangement*	Jun-2011	1,883	—	944	200	Revolution
Stand-By Arrangement*	Nov-2012	3,160	—	944	335	Revolution

SDRs = Special Drawing Rights
*These two arrangements were announced as staff-level agreements but were not submitted to the IMF Board for approval.

export premium system from 1957 to 1961, varying by currency and destination, along with import fees and surcharges.[9] By 1958 the export premium extended to all commodities except rice and oil products, and in 1959 a new premium system for convertible currency transactions was established. As the balance of payments improved, the premia were reduced, achieving an effective premium of 19 percent on imports of essentials compared with 10 percent on exports. Egypt undertook a partial devaluation (without altering the official exchange rate), which stabilized the balance of payments without changing the nominal exchange rate.[10]

2. Repegging of 1962 and Subsequent Pressures

During the 1960s the role of the state in the economy was expanded, and the financial sector and major enterprises came under public ownership (Mohieldin and Kouchouk 2003). Egypt faced economic challenges due to high government expenditures on military and infrastructure projects, including the 1967 war with Israel and the Aswan High Dam (built between 1960 and 1970). Political instability further strained the economy.

To stabilize the economy, Egypt switched from a sterling peg to a US dollar peg in 1962, devaluing the currency from $2.87 to $2.30 per Egyptian pound, a 20 percent devaluation. The devaluation was supported by two IMF Stand-By Arrangements (1962 and 1964) totaling SDR82 million[11] as well as a Compensatory Financing Facility of SDR16 million in 1963. These efforts aimed to address fiscal and external imbalances, stabilize the balance of payments, and support economic reforms, but political instability and the war with Israel interrupted progress toward these goals.[12]

3. The 1973 Multiple Exchange Rate System

In the 1970s Egypt faced economic pressures due to the October 1973 war and subsequent reconstruction needs. To manage foreign exchange shortages and improve trade balances a premium/surcharge of 50–55 percent was added to

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9 The Egyptian pound remained pegged to the British pound, but the crisis led to increased REER volatility. There was a de facto devaluation in 1958 through the introduction of an "export pound," which entailed a 21 percent effective exchange rate depreciation for some transactions (IMF 1958).

10 Egypt entered barter agreements with Western countries, inflating import prices and offering substantial discounts on Egyptian cotton, which the USSR and Czechoslovakia reexported at up to 28 percent discounts. The export premiums led to an 8 percent rise in wholesale prices and a scarcity of imported goods such as tea, coffee, fuel, and paper. Import fees included a 10 percent fee on all imports against convertible currencies and additional surcharges on nonessentials. By 1959, premiums for cotton exports averaged 25–30 percent, and import premiums were set at 27.5 percent (Hansen and Nashashibi 1975).

11 As per IMF reporting, the disbursements in 1962 and 1964 are reported here in SDR, although the SDR was created in 1969. The SDR figures are calculated based on the IMF's calculations of what the SDR equivalent of US dollar amounts would have been.

12 The two IMF Stand-By Arrangements were an important undertaking given Egypt's tensions with the West. Egypt also received IMF assistance under the Compensatory Financing Facility in 1963. These arrangements aimed to stabilize the balance of payments and support economic reforms. Although an agreement was reached in principle with the IMF in early 1967 for additional support, the program was not fully realized until March 1968, when it had limited impact due to the ongoing economic and political challenges (de Vries 1976).

the official exchange rate ($2.56), effectively devaluing the Egyptian pound to $1.70–$1.64, without altering the official nominal exchange rate.[13]

4. The 1979 Devaluation

Following the October 1973 war, President Anwar Sadat initiated a transition from socialist policies to an open-door economic policy (*Infitah*) to liberalize the economy and attract foreign investment, including for reconstruction.[14] Steps were taken to expand the role of the private sector, but these reforms were slow and accompanied by rising inflation and budget deficits. At the same time, Egypt's reorientation away from the Eastern Bloc to a pro-Western political stance and economic model, coupled with domestic political fragility, induced donors, including the IMF and World Bank, to be much more supportive (Ikram 2021).

In 1977 the removal of food and gas subsidies led to widespread riots due to a sharp rise in food prices. In 1978 an IMF Extended Fund Facility worth SDR600 million provided additional financial support for economic stabilization and reforms. The significant devaluation of the Egyptian pound in 1979—from $2.56 to $1.43, a 44 percent decrease—aimed to address growing trade deficits and stimulate economic growth.

5. Devaluations of 1989 and 1991

In the early 1980s Egypt faced economic pressures from declines in oil prices, remittances, and tourism revenues. These factors, combined with elevated levels of public spending, led to significant fiscal deficits and external imbalances, including the accumulation of sizable external debt, which reached 175 percent of GDP by 1988 (Mohieldin and Kouchouk 2003, Ikram 2021). The situation was exacerbated by the spillovers of the First Gulf War in 1990.

To address the overvalued exchange rate and improve export competitiveness, in 1986–87 Egypt implemented a reform program that included restructuring the multiple exchange rate system and devaluing the currency. The central bank devalued the Egyptian pound three times in 1989–91: from $0.91 to $0.50 to $0.30—devaluations of 35 percent, 45 percent, and 40 percent, respectively, resulting in an 80 percent reduction in the value of the Egyptian pound within three years. The REER showed considerable volatility during this period, reflecting these economic adjustments. The aforementioned devaluations occurred in the context of the IMF support program, and Egypt de facto unified its multiple exchange rate system.[15]

13 In early 1973 there were discussions with the IMF about a new program, but they were interrupted when Egypt failed to devalue its currency. In September 1973, however, Egypt did undertake some trade reforms and the exchange rate was de facto devalued by 50–55 percent (World Bank 1974).

14 Until 1973, Egypt's main donors were the Arab countries and the Soviet Union. After that, the United States became an increasingly important donor (Ikram 2006).

15 The Egyptian pound was used as the nominal anchor, supported by tightened fiscal and monetary policies (Subramanian 1997). Despite these measures, there was significant hesitation with overall economic reforms, casting doubt on Egypt's commitment to reform (Ikram 2021).

Egypt also secured a Paris Club debt treatment in 1987 that reduced its debt by $7.1 billion, and a subsequent treatment in 1990–91 addressed a larger debt burden of $21.1 billion. The IMF also played a role during this period, with Stand-By Arrangements in 1987 and 1991 supporting the debt write-offs and committing Egypt to privatization and economic liberalization.

6. The 2002 Devaluation and the 2003 Float

In the early 2000s Egypt experienced foreign currency shortages and a more active parallel market for foreign exchange due to the spillovers of the 9-11 attacks and the Second Gulf War. To address these issues, the central bank depreciated the Egyptian currency in 2002 to E£1 = $0.22 and transitioned to a managed float in January 2003. This shift aimed to eliminate the parallel market for foreign exchange, facilitate a more market-responsive currency valuation, and improve investor confidence.

7. The 2016 Devaluation

By 2016 Egypt again contended with severe economic challenges, including high inflation, a large budget deficit, and a significant foreign currency shortage. These were compounded by political instability following the 2011 revolution. In November 2016 the central bank devalued the pound to $0.06, a 45 percent devaluation, and transitioned to a liberalized exchange rate regime.[16] The devaluation, part of a broader economic reform package supported by an SDR8.6 billion loan from the IMF, aimed to address the acute foreign currency shortage and restore investor confidence. The reforms included measures to reduce subsidies, increase taxes, and implement structural reforms to enhance economic growth and stability. The REER also underwent a major adjustment, indicating improved external competitiveness.

8. Two Devaluations of 2023 and 2024

Egypt faced another severe economic crisis in 2023, exacerbated by the COVID-19 pandemic, the war in Ukraine, and the war in Gaza. To curb inflation and attract foreign investment, the government devalued the currency in January 2023 to $0.03, a 40 percent devaluation, and floated it in March 2024, with the pound officially valued at about $0.02. The float is meant to achieve a sustainable exchange rate, improve investor confidence, and address external imbalances. The IMF resumed and increased its loan from $3 billion to $8 billion to support the country's economic reforms, which included curbing large infrastructure projects, reforming the subsidy system, and reducing the military's economic influence.

The 2023–24 Crisis in Historical Context

The current economic crisis in Egypt is characterized by familiar patterns that have plagued the Egyptian economy for decades, including an overvalued exchange rate due to a nonfloating exchange rate system, persistent BOP

16 The 2016 IMF program came after two staff-level agreements for IMF programs with Egypt in June 2011 and November 2012, after the Arab Spring, but they did not move forward.

deficits, and IMF pressure to devalue the currency in exchange for emergency assistance. These cyclical crises have highlighted the structural vulnerabilities in Egypt's economic framework and the challenges of implementing durable reforms.

Egypt's policy approach, intended to stabilize prices and attract foreign investment, has often led to significant misalignments between the official exchange rate and the parallel market rate. The disparity between these rates reflects underlying economic imbalances, including fiscal deficits, low productivity, and inadequate foreign reserves. Such imbalances have precipitated external pressures on the currency, necessitating periodic devaluations to realign the exchange rate with market realities.

Another persistent feature of Egypt's economic crises has been its recurring BOP deficits. These deficits stem from structural issues such as import dependence, insufficient export growth, and high levels of government expenditure, and these imbalances have resulted in dwindling foreign reserves, prompting the need for external financial assistance. The IMF has frequently played a pivotal role in providing emergency support, but conditional on the implementation of economic reforms, including the requirement for Egypt to devalue its currency and move toward a more flexible exchange rate regime. Such measures are aimed at restoring external competitiveness and stabilizing the economy.

Yet, despite repeated interventions and devaluations, Egypt has typically reverted to its practices of exchange rate stabilization and management. This pattern demonstrates a sustained reluctance to commit to a floating exchange rate system. The return to a fixed exchange rate regime is driven by sociopolitical considerations, including fears of inflation, particularly in food prices, and the potential for social unrest. Additionally, the military's significant influence over the economy combined with geopolitical dynamics have reinforced the preference for maintaining a stable, albeit overvalued, exchange rate.

The current crisis, exacerbated by recent global and regional shocks, mirrors these historical patterns. Egypt's significant devaluations in March 2023 and flotation in March 2024, supported by the IMF bailout, aimed to curb inflation, attract foreign investment, and address external imbalances. But the sustainability of these reforms remains uncertain, given Egypt's historical tendency to revert to fixed exchange rate policies and delay necessary structural adjustments.

IV. WHY EGYPT REPEATEDLY FACES BOP CRISES

Analysis of Egypt's historical record and the present crisis shows that three key features have consistently contributed to the country's repeated economic crises: (1) fixed exchange rates amid persistent internal and external imbalances; (2) reliance on geopolitical rents, often leading to the need for IMF programs; and (3) governance issues, including the dominant role of the state and military, low accountability, and cronyism.

In our view, understanding Egypt's exchange rate policy requires consideration of the broader economic and political economy model, of the significant role of the state and military, and of the government's use of subsidies. These elements shape the economic landscape and influence the outcomes and

effectiveness of exchange rate decisions. The military's substantial economic influence and the extensive subsidy system create a context that complicates exchange rate stabilization efforts and their outcomes.

Exchange Rate Policy and Underlying Fears

Since its establishment as a republic in 1952, Egypt has experienced a recurring pattern of structural budget and current account deficits, often financed by external assistance and debt, contributing to occasional debt crises. Since the authorities have not adequately adjusted fiscal and monetary policies to address Egypt's imbalances, there has been a need for a steady depreciation of the exchange rate. However, the country has generally maintained fixed or highly stable exchange rates, an approach that, along with its current account difficulties, has repeatedly led to BOP problems. In response, the authorities have been forced to make discrete changes in the exchange rate policy, such as step devaluations and/or sudden implementation of a crawling peg or a float, although these have regularly been followed by reversion to exchange rate stabilization. These adjustments have also often been accompanied by multiple exchange rates, exchange and trade restrictions, and central bank interventions. Typically, devaluations or changes in the exchange rate regime have occurred after difficult negotiations with the IMF, as Egypt often resists the Fund's conditions on exchange rate policy, subsidy reform, and privatization.

Flexible exchange rates offer benefits for many economies by preserving external competitiveness and allowing for better adjustment to shocks (Irwin and Obstfeld 2024). Yet Egypt has long hesitated to adopt a flexible exchange rate system. While it is reasonable to debate whether the extent of exchange rate flexibility (e.g., a managed float) is suitable for Egypt, it is clear that the country's prevailing policy of fixed or highly stabilized exchange rate has not served Egypt well. The factors behind this preference are rooted in both economic and sociopolitical considerations.

Import substitution policies and elasticity pessimism: Since 1952 Egypt's development strategy has focused on import substitution. This approach typically involves maintaining high tariffs and an overvalued exchange rate to reduce the costs of imports of intermediate inputs for import-substituting products. Additionally, there has been a prevailing sense of elasticity pessimism, which has led to skepticism about the benefits of a depreciated exchange rate for promoting exports as well as a fear of contractionary devaluations.

Fear of inflation and social instability: Central to Egypt's concern about a flexible exchange rate is the risk of inflation, especially for food prices. Egypt is the world's largest wheat importer. Any significant currency devaluation could sharply increase food import costs, raising the price of bread and other staples.[17] This scenario could threaten social stability since affordable food and fuel are

17 The latest World Bank data indicate that poverty stood at 29.7 percent in 2019. Given the high rates of inflation, poverty is likely to have gotten worse since then.

crucial to Egypt's social contract.[18] To support the population and manage these risks, the government has kept food and fuel prices low through controls and subsidies. This policy relies heavily on maintaining a stable exchange rate. The authorities have at times tried to reform the subsidy system, but these efforts have been generally ineffective in improving the system or in making it better targeted.

Fear of escalating debt service payments: Another potential concern driving Egypt's exchange rate policy is its large external debt, which the IMF projects will exceed 59 percent of GDP in FY2023/24 (IMF 2024a).[19] Much of this debt is in foreign currencies. Any devaluation of the Egyptian pound would increase the debt servicing burden.

Aside from these reasons, which Egypt has in common with many other developing and emerging-market economies, geopolitics and Egypt's economic governance model have also played key roles.

The Geopolitical Safety Net and Complacency Toward Reform

Egypt's persistence in maintaining its exchange rate policy has been facilitated by the availability of external financing. This support has often come in the form of loans (from both official lenders and the markets, the latter often being short term), grants, and debt relief from a variety of international partners, motivated heavily by Egypt's strategic geopolitical significance. Such financial inflows have provided the necessary liquidity to uphold the country's exchange rate peg and finance the budget over long periods, effectively postponing the need for more fundamental economic adjustments.[20] However, this reliance on external capital flows to sustain an artificially stable exchange rate and repay prior external debt has masked underlying economic vulnerabilities, delaying the adoption of reforms essential for long-term financial sustainability.

Egypt holds a pivotal role in Middle Eastern politics because of its strategic position, including control over the Suez Canal, its military strength, and its 1979 peace treaty with Israel. This status more or less ensures a continuous flow of international aid and support, particularly during crises. Financial support has been provided in recent years not only by the United States, its allies, and the international financial organizations but also by China (CRS 2023). However, this geopolitical prominence has led to reliance on a "geopolitical safety net," enabling Egypt to stall necessary economic reforms.[21]

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18 IMF data show that in 2023 total implicit and explicit energy subsidies amounted to 23.8 percent of GDP, a high figure by international comparison.

19 The IMF projects Egypt's overall public debt to reach 96.4 percent of GDP in FY2023/24. Part of this debt is denominated in foreign currency, and part of the domestic-currency public debt is owed to foreign creditors, creating a call on Egypt's foreign assets if they choose to exit.

20 Among the emerging-market and middle-income economies for which the IMF's April 2024 *Fiscal Monitor* provides information, Egypt has the largest gross financing needs in 2024—almost 34 percent of GDP. Such large needs have kept Egypt on the cusp of liquidity difficulties.

21 For example, in 1991 Egypt received debt relief from the United States and others for contributing to the First Gulf War.

But the country's geopolitical importance is not constant; it varies, influenced by shifts in regional dynamics and global strategic interests. Before the escalation in Gaza, Egypt experienced a noticeable dip in its geopolitical standing, evidenced by reduced aid from GCC countries and a decreased willingness among international financial institutions to provide financial lifelines.

The resurgence of Egypt's geopolitical importance during the Gaza conflict seemed to reinforce the government's dependence on "geopolitical rents," allowing continued delays in economic reforms. Anticipation of such international aid during crises—and Egypt has generally been proven right in this expectation—has lessened the drive to tackle core economic challenges such as the military's dominance in various economic sectors, the urgency of subsidy reform, and the need for a more flexible exchange rate policy.

State- and Military-Dominated Economy

Egypt's economy is state dominated, the military plays a pivotal role (Sayigh 2019), and cronyism has increased since the 1990s, with greater participation from the main political party (Diwan, Keefer, and Schiffbauer 2019; Ikram 2021). Politically connected firms have thrived thanks to better access to public resources and lighter regulation.

The military controls significant aspects of the economy, including public enterprises and parts of the private sector, and benefits from preferential tax treatment, reduced import duties, subsidized energy, and access to foreign currency. Many state-controlled areas, including those managed by the military, focus on import substitution and prefer maintaining an overvalued exchange rate. Since the 2013 coup, the military's economic advantages have grown. It oversees major construction projects and infrastructure, significantly increasing government debt. This shift has exacerbated structural economic issues, such as unemployment (especially among youth), low productivity, and limited investment in areas other than energy and real estate.

The military is now a major landowner, and its political influence allows it to secure contracts and enjoy tax and customs exemptions, giving it an edge over civilian competitors. Profits from military-led economic activities rarely benefit civilian state agencies, underscoring how political control trumps economic efficiency and productivity growth.[22] The opacity of military finances and tax exemptions also raises concerns about accountability and fairness.

Although the military's role in some countries' political and economic systems has supported structural transformation and growth (e.g., Pinochet's Chile, pre-1988 South Korea, and early-1980s Turkey), Egypt's military has often exercised interventionist and inward-looking economic policies. This centralized control model hinders efficiency and responsiveness, which might be more achievable under a private enterprise system. These factors contribute to Egypt's low growth rates and persistent fiscal and BOP difficulties.

There are lessons from other countries' experience under military rule. In South Korea the military recognized the importance of a switch to outward-oriented economic policies, albeit combined with industrial policies, including through the incentive system. With concerns about a decline in US support,

22 On Egypt's low productivity, see Morsy and Levy (2020).

starting in the 1960s Korean leaders linked the need for security and economic development (Ikram and Nassar 2022) and changed the course of economic policies and practices toward a more competitive, export-oriented economy. Pakistan, on the other hand, has remained unchanged in terms of economic strategy. The military still has tight control over the country's politics and economy—although compared with Egypt, Pakistan has allowed greater civilian participation.[23] And Pakistan has continued to rely on geopolitical rents as a financial safety net, although its geopolitical significance has declined since the end of the US engagement in Afghanistan. The elites, both military and civilian, have thus far felt that they can maintain their interests and survive economically and politically without substantial reform. Consequently, they—much like Egypt—have experienced episodic crises with similar policies (including exchange rate policy).

V. WILL THIS TIME BE DIFFERENT?

Again and again, Egypt's pursuit of fixed or highly stabilized exchange rates has contributed to its BOP difficulties. Flexible exchange rates are not a remedy for all macroeconomic difficulties of emerging-market countries, including due to the decline in the sensitivity of trade to exchange rate movements with the greater use of dollar invoicing and the globalization of value chains. That said, Egypt needs to consider a much more flexible exchange rate to insulate itself from adverse global economic shocks and allow greater policy space to address the consequences of its structural external and fiscal imbalances (figure 3), especially given its longstanding reliance on international capital flows.

Decades of recurring crises make clear that Egypt needs to change course, with reforms involving governance and institutions. There are two paths before it: one narrow, challenging, and filled with potential; the other well-trodden, familiar, and likely to create risks of future crises. Let's consider the options.

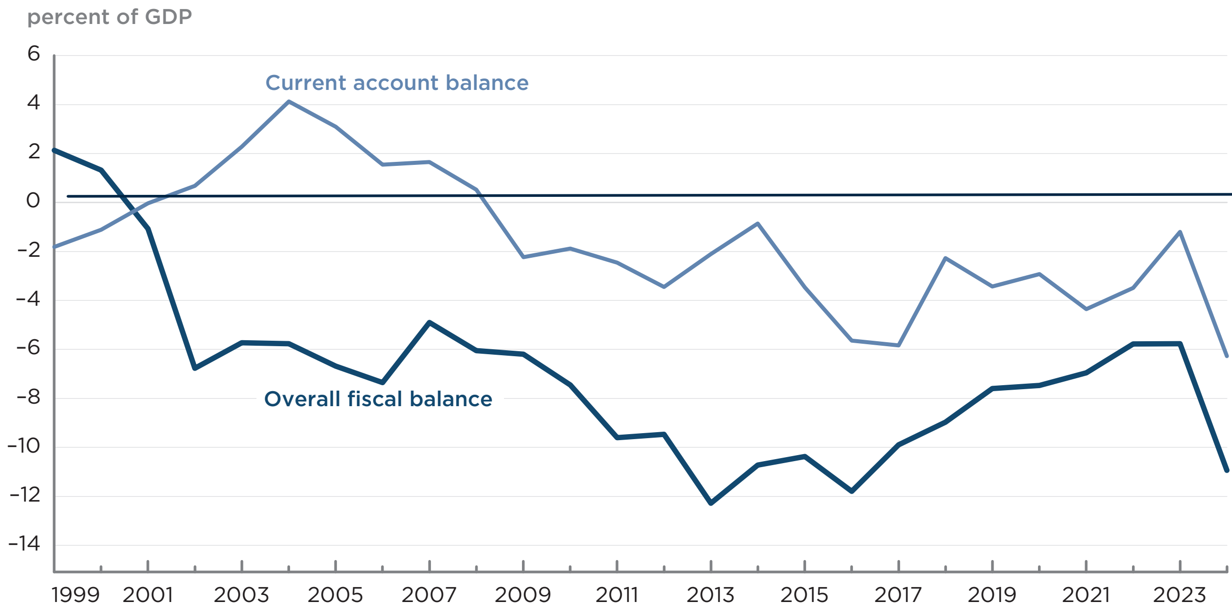
Scenario 1: Breaking Free

This path involves a series of bold, sustained reforms aimed at addressing the very foundations of Egypt's economic woes.

Governance reform is the first, and perhaps most challenging, pillar. Reducing the military's economic dominance involves promoting transparency and enforcing anticorruption measures. This means redefining the state-market relationship to allow for private sector growth, innovation, and diversification beyond military-controlled sectors. It also involves creating an environment where fair competition can thrive. Increased accountability is essential. This accountability can be achieved by strengthening judicial independence, improving public financial management, and fostering a culture of meritocracy. Such steps would help build trust in the system, drive economic efficiency, and facilitate management of public finances. But the military may accede to reform only if the prevailing political economy model becomes clearly untenable.

23 Malik and Tudor (2024) argue that the military and other elites' hold on Pakistan could decline due to the rise of the middle class, the breakdown of traditional authority patterns, and a deepening economic crisis.

Figure 3
Fiscal and current account balances of Egypt, 1999–2024



Source: IMF World Economic Outlook (WEO) Database.

Next, reconsider the reliance on geopolitical rents. Historically, Egypt has used its strategic position to secure a steady flow of international aid. This has often delayed necessary reforms. To break this pattern, Egypt must leverage its strategic importance not just for short-term aid but as a catalyst for lasting economic stability and growth. Diversifying the economic base, promoting private sector growth, and attracting foreign direct investment in nontraditional sectors are crucial steps. Stronger institutions, for example better regulations, are also needed to manage resources effectively and reduce fiscal dependence on external lifelines.

Finally, abandon the fixed exchange rate. A flexible exchange rate allows the currency to float, adjusting to market realities. This could mitigate imbalances and enhance competitiveness. Of course, the transition won't be easy. Inflationary pressures, especially on food prices, are a significant concern. But with targeted social safety nets, the government can protect the most vulnerable while allowing the economy to breathe. Adopting a flexible exchange rate also means promoting greater financial self-sufficiency and reducing dependence on external financing. In this context, subsidy reforms and creating an investment-friendly environment would be key complementary policies.

Scenario 2: The Perpetual Cycle

In this scenario, Egypt sticks with what it knows: It returns to fixed exchange rates, leans on geopolitical rents, and allows the military to remain deeply embedded in the economy. This is the well-rehearsed playbook. But this approach, as history shows, is a bit like trying to keep a beach ball submerged. Eventually, the forces of market reality push it back up.

The overvalued exchange rate leads to persistent external imbalances. The currency misalignment becomes glaringly obvious, and BOP deficits swell.

Import dependence remains high, exports don't grow enough, and government spending continues to rise. Foreign exchange reserves dwindle, and the cycle of calling for international help begins anew. Enter the IMF and the familiar script of devaluations and promised reforms. These interventions offer temporary relief, but they rarely address the root causes, leaving the underlying issues to fester until the next crisis.

Meanwhile, governance issues persist. The military's grip on significant sectors of the economy and the prevalence of cronyism stifle efficiency and innovation. Growth remains sluggish, and socioeconomic problems continue unabated. The scene is set for yet another cycle of crisis and bailout.

Looking Ahead

Will this time be different? Probably not, as the chances of change are small. Several factors will likely allow a continuation of the status quo (as outlined in scenario 2). A number of groups, including the military, the bureaucracy, and parts of the private sector, have sizable, deep-rooted interests in the status quo. They are not going to be agents of change, unless the regime's existence is at risk, and, arguably, the current crisis still appears to be politically manageable to the insiders.[24] Public resistance has been limited, and the flow of geopolitical rents and the switch in market sentiment has allowed Egypt to muddle through.

Therefore, it is hard to imagine that Egypt's current economic difficulties will induce the authorities to embark on deep reforms. We are inclined to believe that the recurring cycles of economic difficulties—including insufficient job creation, structural deficits in fiscal and external balances, and reliance on fixed or overly stable exchange rates—are likely to continue. And the international community, including the IMF and World Bank, will likely continue to provide a financial safety net to Egypt.

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24 The economic deterioration of the last few years has perhaps not been severe enough to induce such change. Research in this area shows that crises need to be severe for there to be change (Drazen and Easterly 2003).

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