



# EGYPT

## OUTLOOK

By Glenn Wepener

### Economic Growth

In 2019, Egypt's economy expanded by 5.6%, and prior to Covid-19 appeared on course to grow by 5.9% in 2020. Despite the challenges posed by the pandemic, Egypt was the only economy in the MENA region to record a positive growth rate last year (+2.75%), and one of just sixteen countries globally to grow by 1% or more. This was due in part to the government's early decision to approach the IMF for US\$2.8 billion in funding via the 'Rapid Financing Facility' and access a US\$5.2 billion standby arrangement.

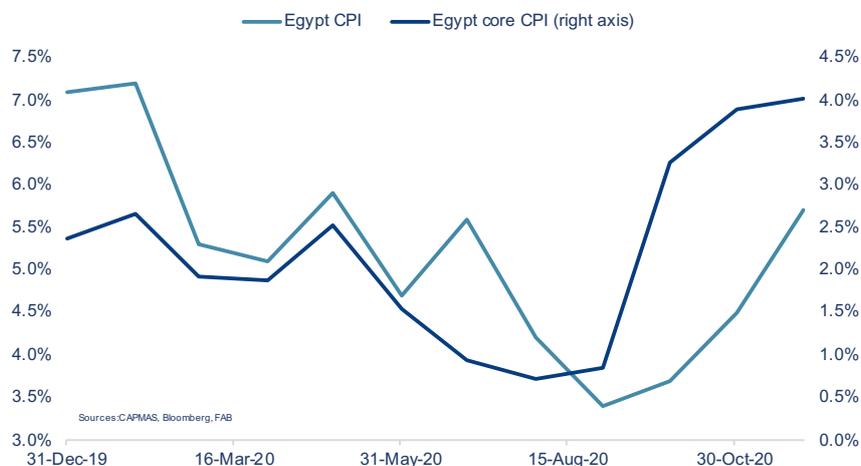
The request's quick approval by the IMF allowed the authorities to swiftly implement an emergency response package. They increased overall health spending by 26%, provided support to the private sector, helped stimulate consumer spending, and introduced

various social measures to protect the more vulnerable sections of the population. This was done without undermining the gains achieved by a strict adherence to a wide-ranging structural economic reform programme in the previous four years.

Despite this forced jump in both spending and borrowing in order to combat the economic impact of the virus, last November Egypt's Finance Minister, Dr. Mohammed Maait said the government was aiming to lower the budget deficit to 6.5% of GDP during the 2021/22 fiscal year (from 7.9% in 2019/20), and to cut its debt load to 77% of GDP by 2024, from the current level of 87%.

### Inflation

During the 2019/20 fiscal year, core domestic inflation recorded the steepest rate of annual decline among all emerging markets, falling to 5.7%, from 13.9% in 2018/19. In October, 2020, headline inflation stood at 4.5% year-on-year after hitting a nine-month low of 3.4% in August. Conversely, the unemployment rate rose to a two-year high of 9.6% during Q2 20, before declining again to 7.3% in Q3 20, according to official data.



## The Local Currency

On the exchange rate side, the value of the Egyptian pound versus the US dollar fell between March and June 2020, as foreign investors liquidated some of their Egyptian T-Bill/Bond holdings on concerns regarding the potential impact of Covid-19. However, these hard-currency outflows have since reversed as the outlook for the global economy began to brighten and overseas portfolio managers made a hasty return to the still-attractive high yields offered by Egyptian assets.

Such inflows are predicted to continue for the time being, also boosted by the passing of a draft law late last year which lifted all fees and taxes on the purchase of Egyptian bonds by foreigners. As a result, the Central Bank's foreign exchange reserves rebounded from US\$36 billion in May 2020, to US\$39.2 billion in October 2020, although that was still off the record peak of US\$45.5 billion attained in February that year.

The USD/EGP exchange rate has resumed its slow grind lower, and appears on track to test the 15.00 support level during the first half of 2021, with the topside likely capped at around 16.20 barring any major unexpected event. Meanwhile, with regard to interest rate policy, we expect the central bank to only lower its benchmark rates by 50-75bp during 2021.

## Key Sectors

Agriculture, tourism, manufacturing, construction, natural gas and telecommunications are the dominant sectors within the economy, and these should all play their part in driving its recovery this year and beyond.

As a major employer and generator of foreign exchange, tourism (along with agriculture) remains the most strategically important sector for Egypt, but was probably the hardest hit by the pandemic as the number of foreign visitor arrivals collapsed, leading to tourism-related revenues falling to just US\$308 million during Q220, compared to US\$3.18 billion during the same period of 2019.

In an attempt to cushion the blow to businesses involved in this particular industry, the government implemented various measures including: an exemption from paying their electricity, water and gas bills until the end of 2020, a rescheduling of debts including those accrued prior to the outbreak of Covid-19, with no repayments due until 1 January, 2021, and the waiving of all visa-related fees for tourists visiting South Sinai, the Red Sea, Luxor and Aswan until 30 April 2021.

There is a reasonable possibility that foreign travellers will soon begin returning to Egypt, due to Egypt's close proximity to Europe (its largest tourist market), along with the introduction of coronavirus vaccination jabs in the



UK, EU and certain other major economies such as China during the early part of 2021. However, a return to the sort of tourist arrival numbers recorded back in 2019 is probably unlikely until 2022 at the earliest.

Agriculture, which makes up 14% of GDP and represents 55% of employment in rural areas, has seen its output improve sharply over the past few years, with the export of close to five million tons of agricultural products reported despite the particular difficulties of 2020. This was driven by the development of better irrigation, as well as more efficient production and supply-chain systems.

The availability of fresh water is obviously key to this sector's long-term survival, and further underlines the importance of a final resolution between Egypt, Sudan and Ethiopia over the latter's controversial 'Grand Renaissance Dam' project on the Nile River.

Egypt's discovery of large offshore reserves of natural gas in 2015 has been a game changer for the country's energy security, with the development of this resource attracting billions of dollars in investments and resulting in Egypt quickly becoming self-sufficient in – and subsequently an exporter of – natural gas. The huge Al Zohr field alone already supplies 50% of domestic demand.

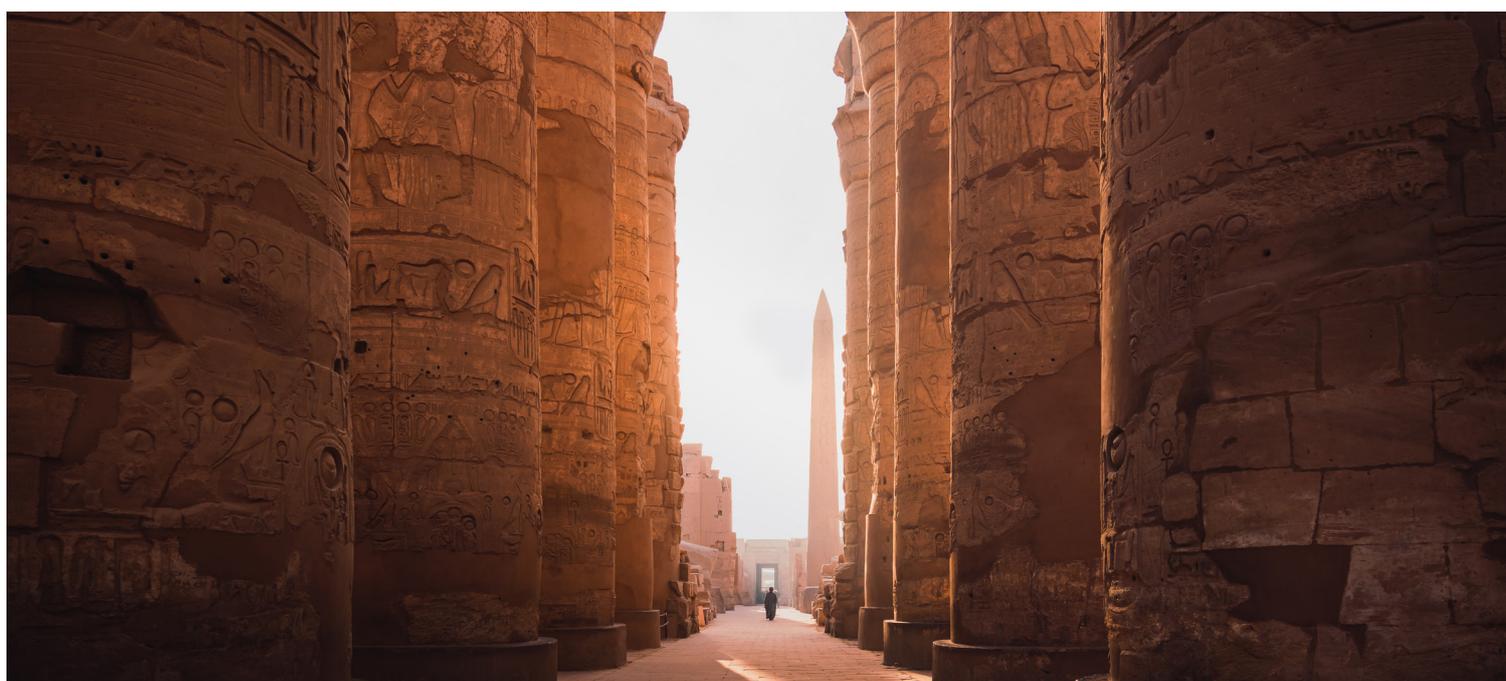
Further significant gas discoveries have since been made, and this, combined with the relatively low cost of

extraction as well as Egypt's geographical position will help it become a regional gas hub in the years to come. Meanwhile, the country's dependence on oil imports has also fallen slightly as local crude output jumped to 650,000 barrels/day late last year, the highest level since the 1950s.

The telecommunications sector has recorded a growth rate of 12%-14% per annum since 2017. This performance has been supported by the removal of historic red tape, large government-led infrastructure projects including the ongoing establishment of a new administrative city, the introduction of new-generation networks, and a drive to install fibre-optic cables, which will in turn soon help provide reliable internet connections to the majority of the country's 98 million people.

Egypt has a diverse manufacturing industry, including automotive, food and beverages, building materials, fertiliser, pharmaceuticals, textiles, plastics, and sanitary ware.

Certain segments clearly suffered more than others during the pandemic, however most of these should start to benefit as the global economy recovers this year, especially in the second half. Meanwhile, an unnecessarily time-consuming and restrictive regulatory environment – especially for SMEs – is slowly being streamlined. This, combined with the development and expansion of new



industrial zones, such as the one situated at Port Suez, is attracting both local and international players, which should help lower unemployment and boost exports.

Finally, the local construction sector, which saw a marked slowdown last year, should rebound strongly in 2021 and is expected to continue to expand over the next five years. According to a Fitch Ratings report published in April 2020, Egypt is set to become the largest construction and building market in the MENA region by 2029, buoyed by a pipeline of major ongoing and planned projects, including those linked to 'green' developments. Global Data said, in a June, 2020, report, that it expects Egypt's construction industry to grow by an average yearly rate of 9.6% until 2024, supported in part by Cairo's urban redevelopment programme.

## US-Egypt Relations

President Abdel Fattah el-Sisi was one of the first Arab leaders to congratulate Joe Biden on his victory in the 2020 US elections, adding that he was "looking forward to working and cooperating with the new President-elect to boost the strategic bilateral relations between Egypt and the United States for the best interest of the two countries and their friendly people."

Good relations between Washington and Cairo have been strategically important for decades, and it was clear they were particularly warm during the Trump administration. However, despite the general expectation that Biden will conduct US foreign policy in a very different manner, no real marked change in diplomatic or commercial ties between these two countries should be expected over the next four years.

Egypt remains an important US ally within the region, especially when it comes to defense and intelligence sharing. There are over 1,300 US companies operating in Egypt, and bilateral trade totaled US\$8.6 billion in 2019.

## Outlook

It is worth noting that Egypt was one of the few countries within the region to maintain stable credit ratings last year, and this underlines the success achieved following structural economic reforms implemented by the government since 2016.

It is fair to assume that Egypt will continue to move forward with its economic reform programme in the years ahead, with the support and guidance of the IMF and the World Bank. As outlined above and looking ahead, as those sections of the Egyptian economy hit hardest by the pandemic such as tourism, construction and manufacturing begin to recover, GDP growth is expected to rebound to 4.5% in FY 2021/22, and to accelerate further to 5.25% in 2022/23.