EGYPT MACROECONOMIC OVERVIEW

FY2020/21 INDICATORS AND PRIORITIES FOR FY2021/22

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www.lynxegypt.com info@lynxegypt.com 4 Latin America Street, Garden City, Cairo +2 02 27944331

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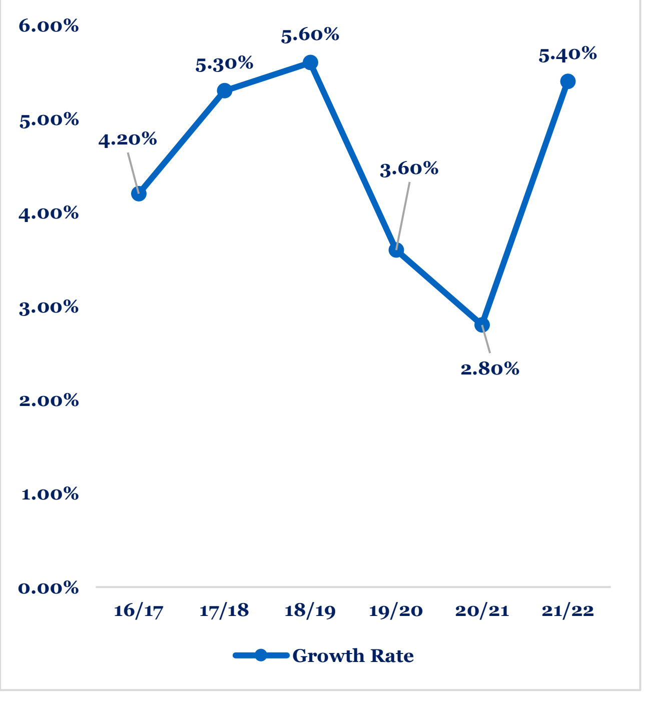
Executive Summary

- Egypt achieved an annual growth rate of 2.8% in FY2020/21 through consistent performance in the construction, communications, and agriculture sectors. This growth continued despite drawbacks in the tourism and manufacturing sectors because of the global lockdown measures of major international markets. Growth direction was boosted by debt-funded public investments towards social protection and services projects. Most public investments projects headed towards labor-intensive construction projects.
- The Ministry of Finance (MoF) achieved a primary surplus of 0.9% in FY2020/21, exceeding its earlier target of 0.5% on the back of saving in commodities procurement, energy subsidy bill, and wages' bill. The Government of Egypt (GoE) extended its rebound to the 2% primary surplus target till FY2022/23 with a 1.5% target set for FY2021/22 to provide for the increasing public investments bill.
- The GoE will focus on expanding its tax bill for FY2021/22 through the long-anticipated value-added tax (VAT) for e-commerce businesses and inclusion of informal enterprises by expanding the implementation coverage of the e-invoice and e-receipt taxation systems. Efforts to improve the financial performances of state-owned enterprises (SoEs) are ongoing through economic feasibility assessments and mergers between redundant enterprises.
- The GoE is expected to redirect cuts in its fuel subsidy bill (34.7% decline v. FY2020/21) and announce restructuring measures of the bread loaves subsidy bill (estimated at EGP 50 billion in direct subsidy beside indirect mazot subsidy for bakeries) to enhance social protection frameworks. Challenges are expected while implementing these reforms due to the social impact of both subsidy measures. By way of example, 63.6 million (out of 100 million) Egyptians benefit from the bread loaves subsidy.
- The National Current Account is still yet to recover from the setbacks of COVID-19 despite consistent performance by the Suez Canal and an anticipated all-time increase in value of remittances. The expanding deficit in trade balance along with the delayed recovery of the tourism sector led to a 2.1% deficit in H1 FY2020/21; down from a 1.3% deficit in H1 FY2019/20. A swift rebound in the tourism sector is expected by H2 FY2021/22 pending on the pace of Egypt's COVID-19 vaccination program. (Egypt remains on the red-zone list of several countries.) Nonetheless, the resumption of direct Russian flights to Egyptian Red Sea resorts is expected to bring in 3 – 4 million tourists per year, indicating a possible arrival level exceeding pre-COVID-19 ones.
- In H1 2020/21, the Central Bank of Egypt (CBE) introduced two rate cuts of 50 bps, and then maintained a conservative policy- with no rate cuts- in H2 2020/21. These cuts have yet to reflect in the interbank rate. With inflation rates remaining below the lower bound of CBE and International Monetary (IMF) targets of 7% (+/-2%) – at a moderate average between 4 – 5 % in H2 - the real interest rate may settle well above the nominal one. Nonetheless, inflation is expected to rebound towards CBE's range of 7% in FY2021/22 as economic activities recover, as well as the IMF's expected overall rate cuts of 100 bps to promote economic activity, while easing interest obligations on the treasury.
- Additionally, Egypt's net foreign reserves have been steadily maintained, landing at USD 40.609 billion in July 2021. These reserves are expected to continue this stable trend with modest increases.

Real Sector

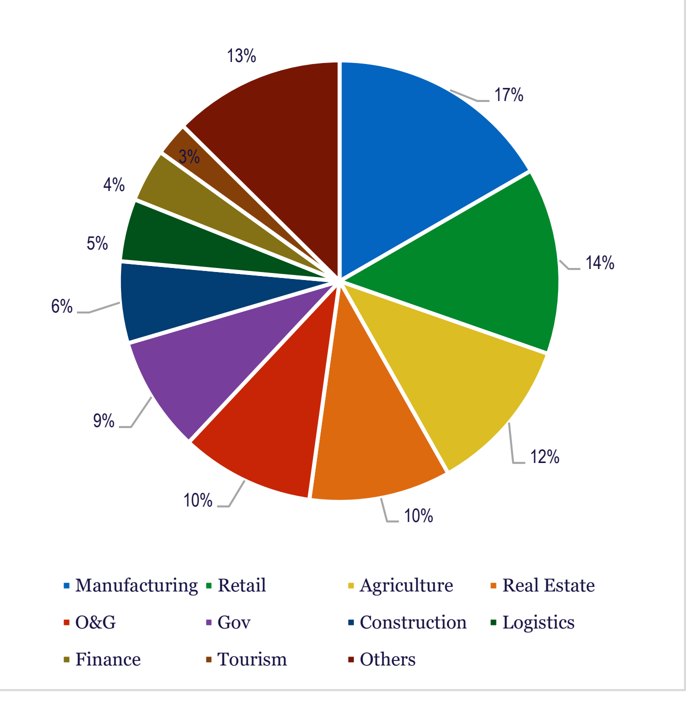
- The Egyptian economy maintained a growth rate in FY2020/21 at 2.8%; a downtick from a recorded 3.6% growth in FY2019/20 on the back of global extensive lockdown measures in H1 2020/21 that hindered the manufacturing, oil and gas, as well as tourism sectors. Nonetheless, the GoE mitigated a second round of limited lockdown measures to avoid further economic damage. H2 FY2020/21 witnessed the beginning of a nationwide COVID-19 vaccination campaign, albeit at a slow pace due to procurement challenges and dependence on GAVI and bilateral supply chains.
- A slight rebound in economic activity was also visible in H2 FY2020/21 due to increases in inbound tourists, the reopening of major bilateral trade destinations, and a steady growth in the construction, communications, and transportation sectors.

Real Growth Rate



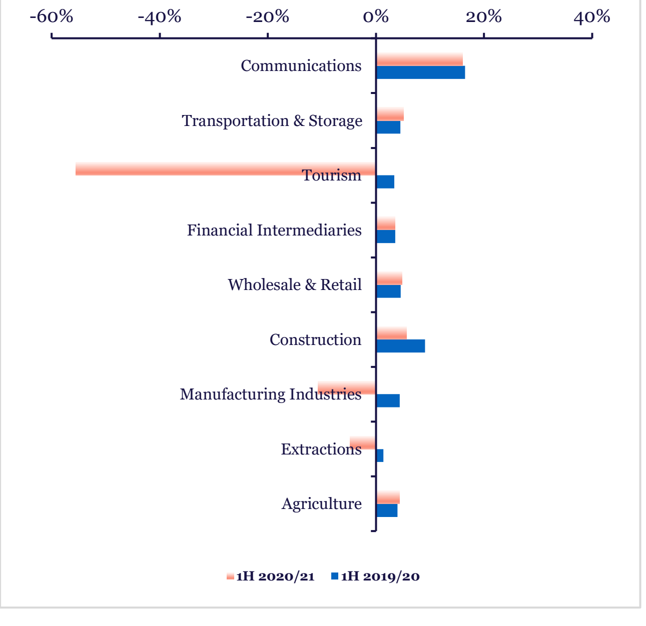
Source: Ministry of Planning and Economic Development

GDP breakdown by Sector



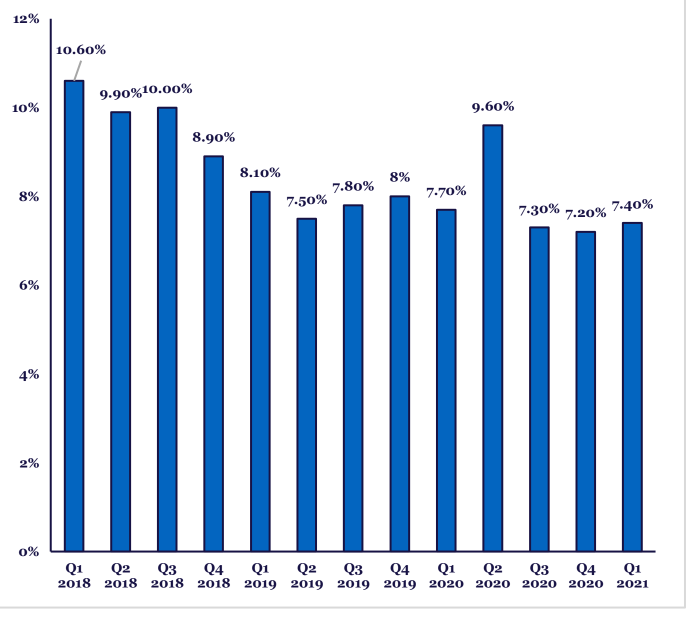
Source: Central Bank of Egypt

Growth by Sector



Source: Central Bank of Egypt

Unemployment



Source: Central Bank of Egypt

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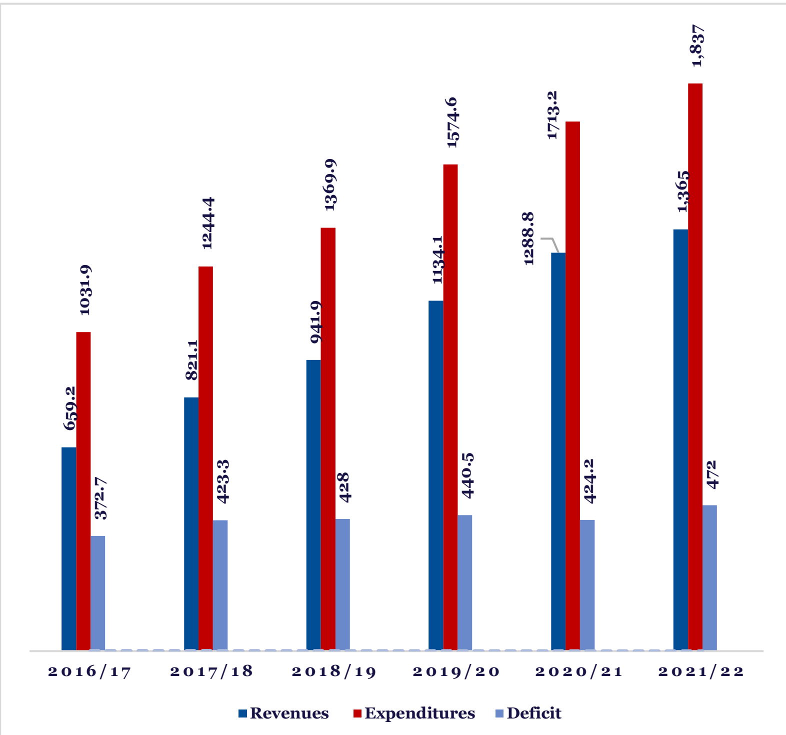
Fiscal Sector

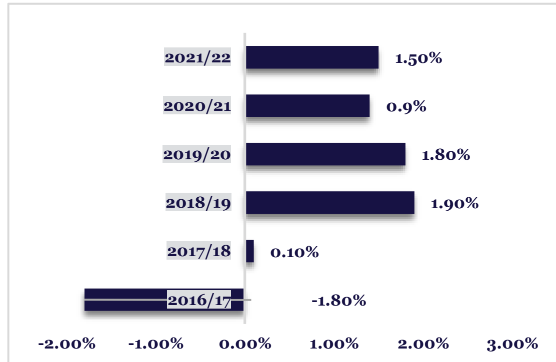
- Building on the implemented measures to expand the taxation framework, Egypt maintained a primary surplus of 0.9% in FY2020/21 on the back of tax collection digitization efforts and leveraging reduced (actual) spending towards strategic commodities procurement, subsidy bill, and public investments.
- Moving forward, Egypt is targeting to achieve a primary surplus of 1.5% while slightly lowering its debt-to-GDP to 89.5% from 89.8% recorded in FY2020/21. The delay in progressing with the debt control measures will be directed towards increasing injection of public investments in education, healthcare, and infrastructure.
- Fiscal reforms on revenue mobilization and fiscal performances of SoEs are essential in limiting non-essential expenditures. Increases in subsidy bills associated with the budget benchmark pricing of wheat and oil can also be expected (wheat @ USD 255/ton; brent @ USD 60/barrel).

Budget Overview (EGP Bn)



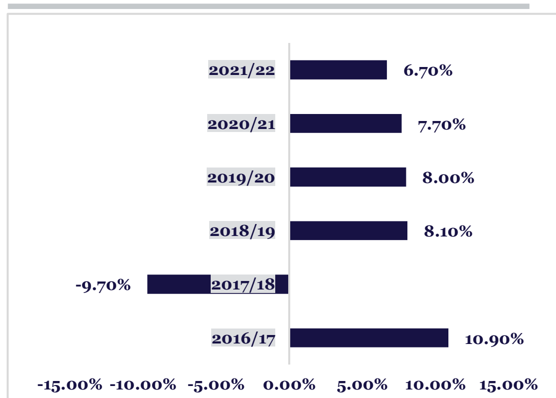
Source: Ministry of Finance

Primary Surplus



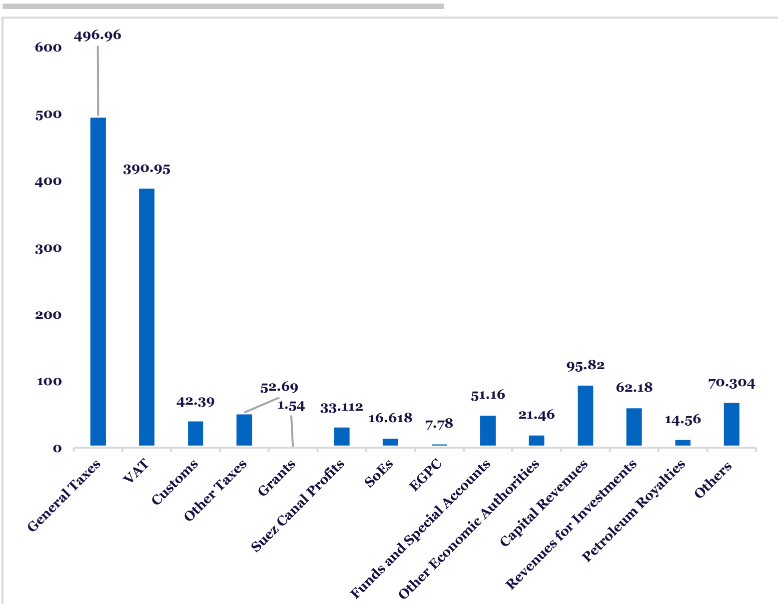
Source: Ministry of Finance

Overall Budget Deficit – (% of GDP)



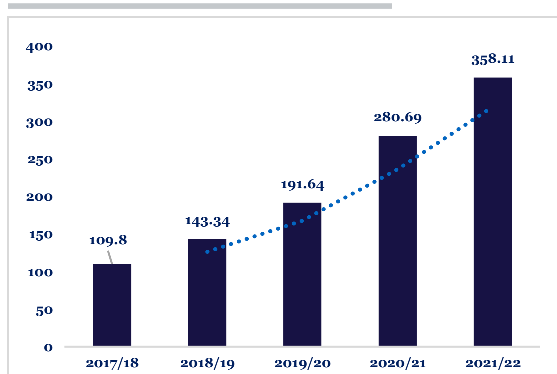
Source: Ministry of Finance

Revenue Sources – FY2021/22



Source: Ministry of Finance

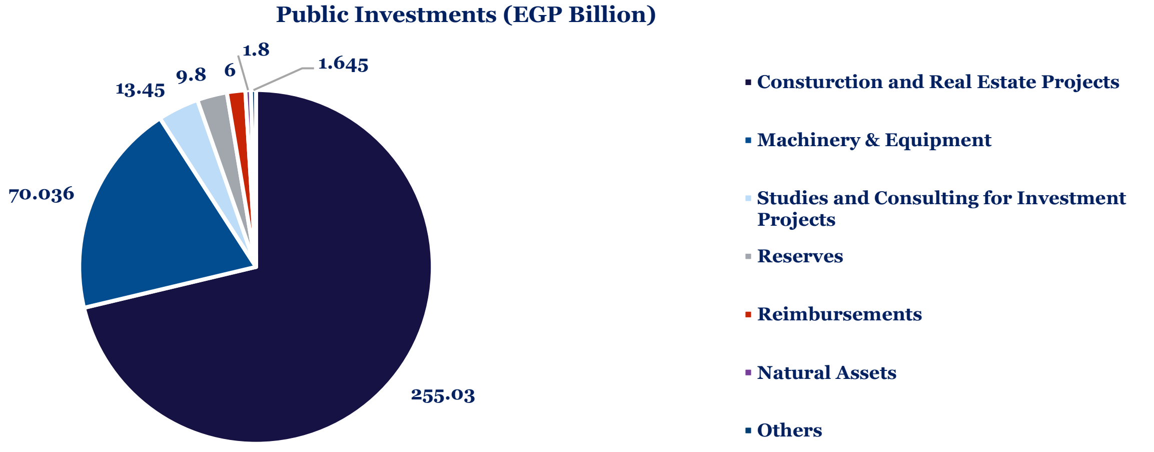
Government Investments

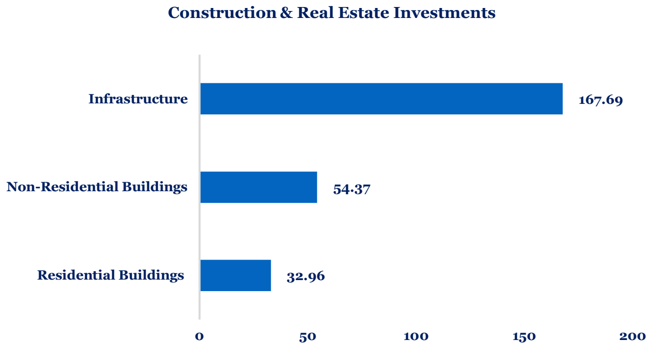


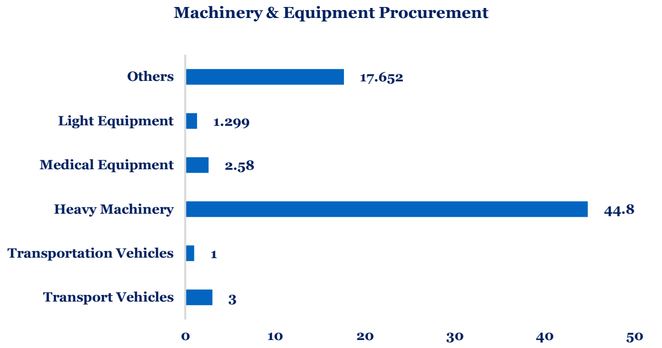
Source: Ministry of Finance

Fiscal Sector

Public Investments Profile – FY2021/22

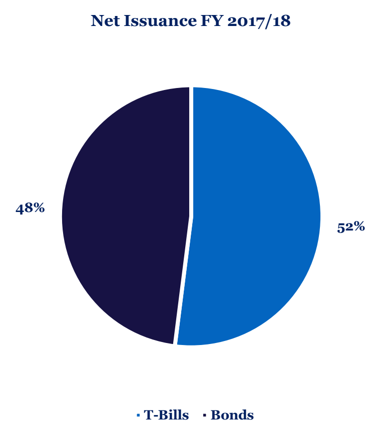


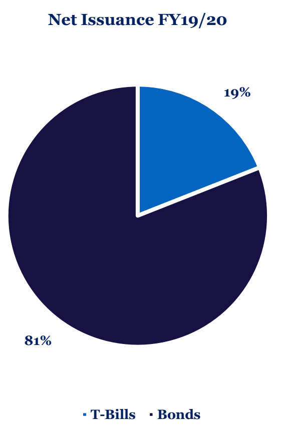


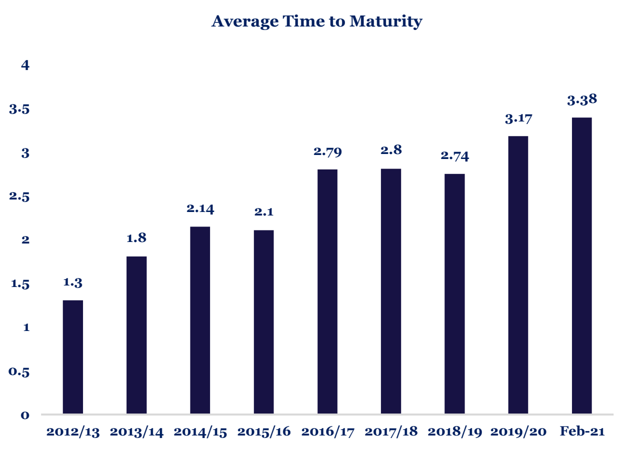


- The FY2021/22 investment bill will witness increased spending on labor-intensive sectors, particularly construction and infrastructure projects. The bill also includes a 67% y-o-y increase in construction and infrastructure spending as part of the 3-year "Hayah Karima" (Decent Life) initiative, which focuses on elevating infrastructure in rural regions.
- Nonetheless, most of the public investments bill is expected to be covered through the state's administrative agencies (EGP 208 billion) and public services agencies (EGP 115 billion).

Public Debt Profile





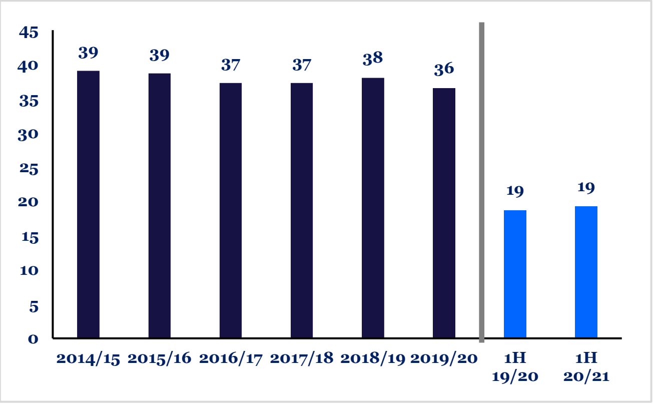


- Egypt's median debt age continued its upward rise towards the 4-years average time to maturity through maintaining conservative issuances of T-bills, and the introduction of Islamic-finance (Sukuk) and green bonds debt tools.
- The increasing expenditure towards debt service continues to put pressure on budgetary provisions and on the ability of the GoE to direct required spending towards public social services.
- With further commitments towards IMF-supported reformed looming in FY2023/24 and FY2024/25, the easing of Egypt's vulnerability towards another outflow of non-resident portfolio investors remains a priority.

 Source: Ministry of Finance

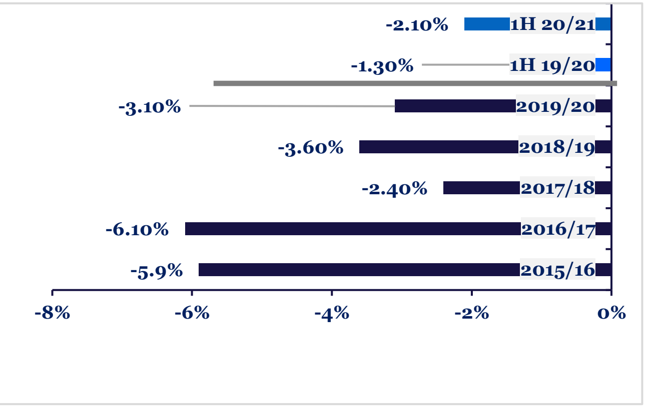
External Sector

Trade Deficit – (USD Bn)



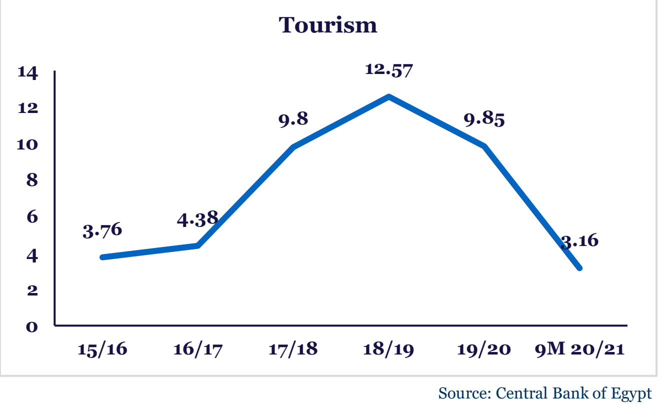
Source: Central Bank of Egypt

Current Account Deficit- % of GDP

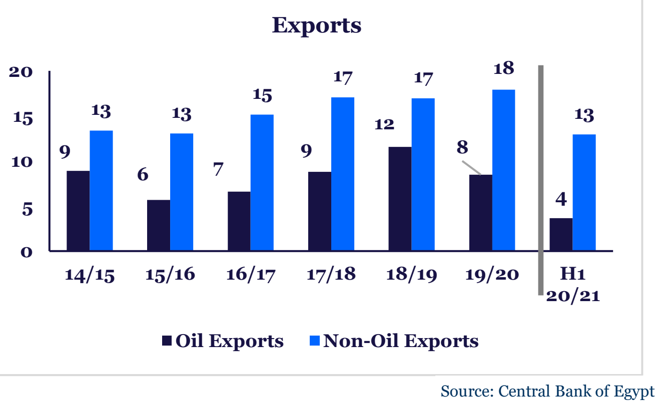


Source: Central Bank of Egypt

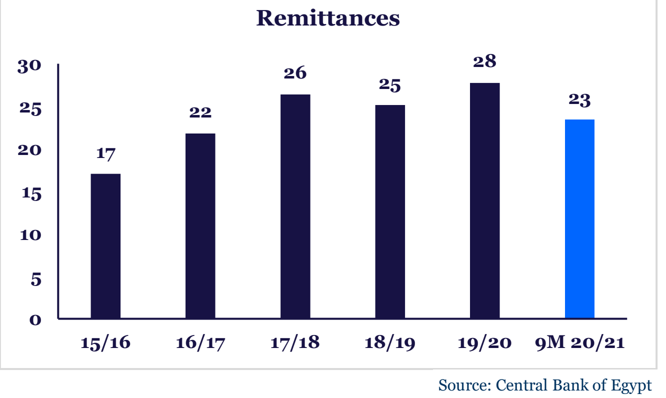
Current Account Receipts – (USD Bn)



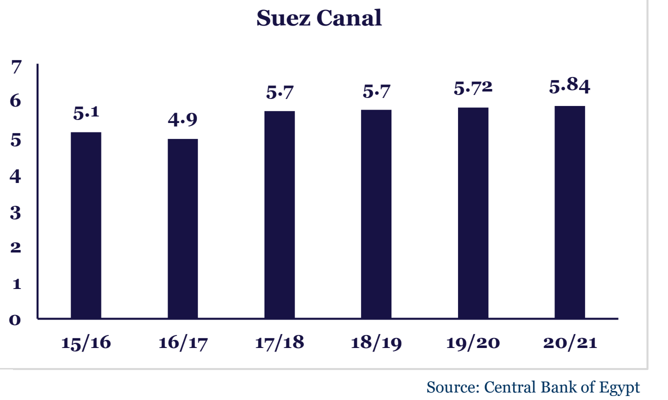
Source: Central Bank of Egypt



Source: Central Bank of Egypt



Source: Central Bank of Egypt



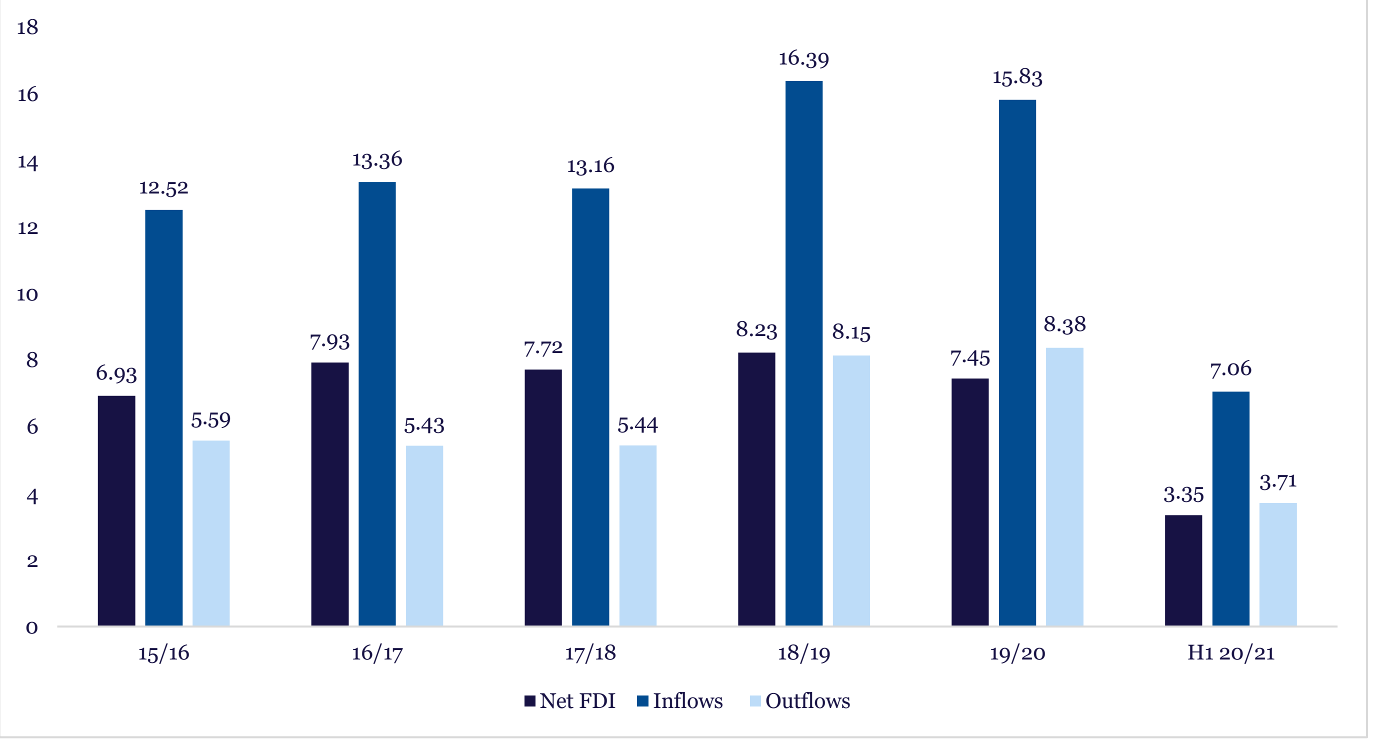
Source: Central Bank of Egypt

- Egypt's main current account receipts scored strong performances in FY2020/21 on the back of rebounding international trade and overall economic activity. Egypt's agricultural exports maintained its strong performance leveraging new market destinations for citrus fruits. Considerable performances regarding exports of electronic devices, engineering products, and jewelry products were also recorded. The resumption of liquified natural gas (LNG) shipments from the Idku and Damietta LNG plants in H2 2020/21 is set to reflect on full year figures and FY2021/22 stats.
- However, the stagnation of tourism activity in H1 2020/21 led to a steep decline in tourism receipts by more than 75% (from pre-COVID-19 levels). The tourism receipts are expected to increase considerably in FY2021/22 on the back of the resumption of Russian direct flights to Egypt beginning Q1 FY2021/22. The Ministry of Tourism anticipates the arrival of 3-4 million Russian tourists per year.
- Consistent growth in remittances and Suez Canal receipts sustain their contribution to the balancing of current account deficit moving forward.

Foreign Direct Investment (FDI)

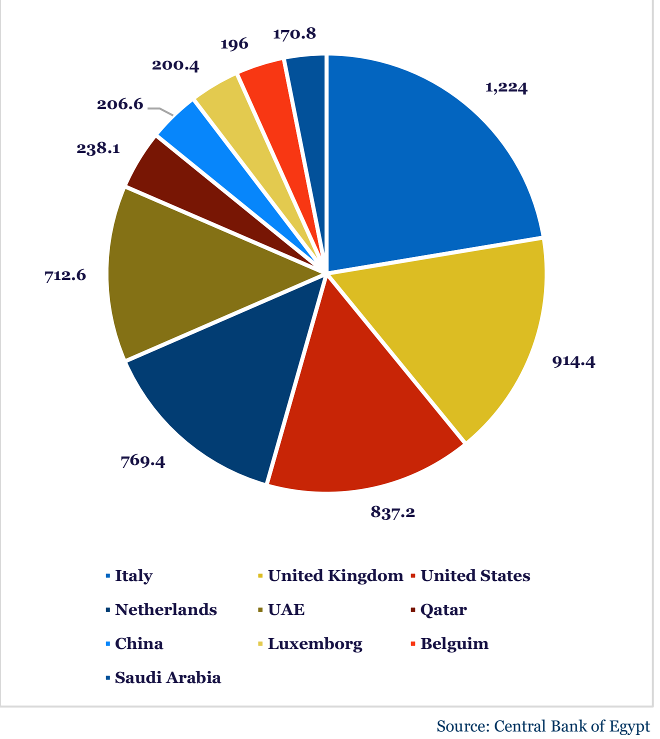
- FDI net inflows in FY2020/21 H1 amounted to USD 3.35 billion, maintaining Egypt's ranking as the largest FDI recipient in Africa during the ast 3 years.

Net FDI flows (FY15/16 - H1 FY20/21)



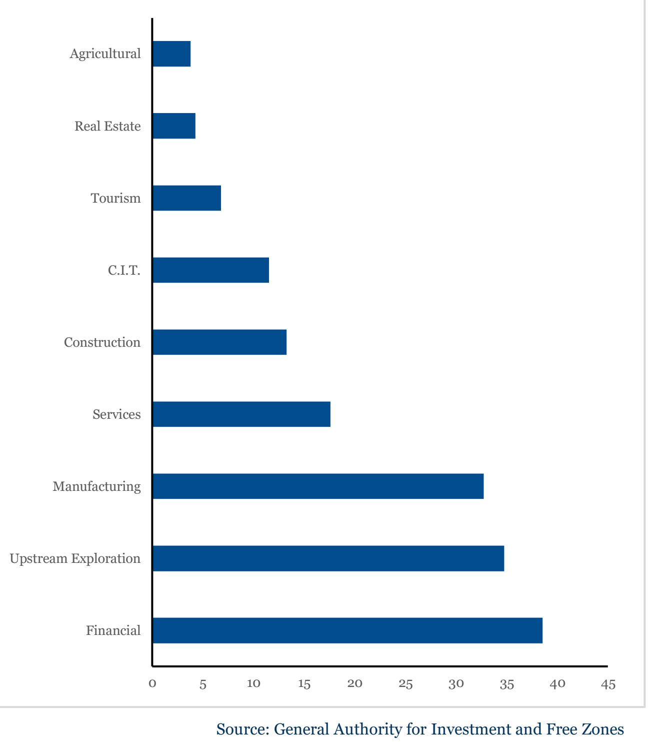
Source: Central Bank of Egypt

Net FDI by Source – (USD Bn)



Source: Central Bank of Egypt

FDI Stock – (USD Bn)

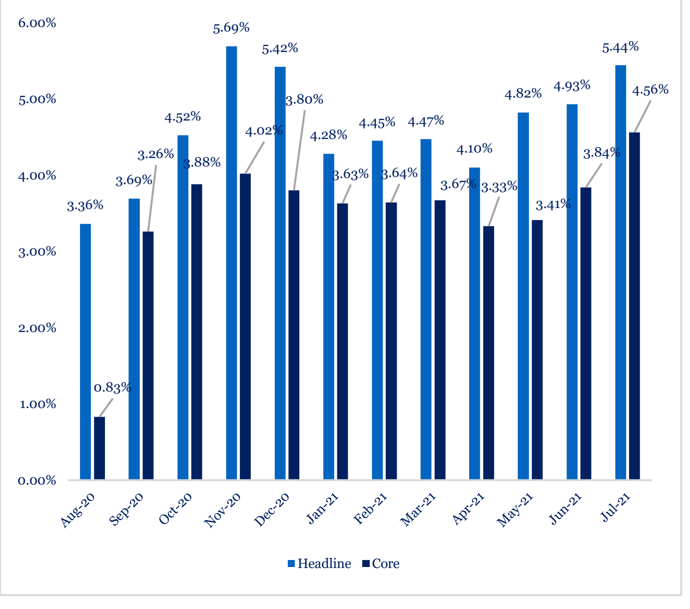


Source: General Authority for Investment and Free Zones

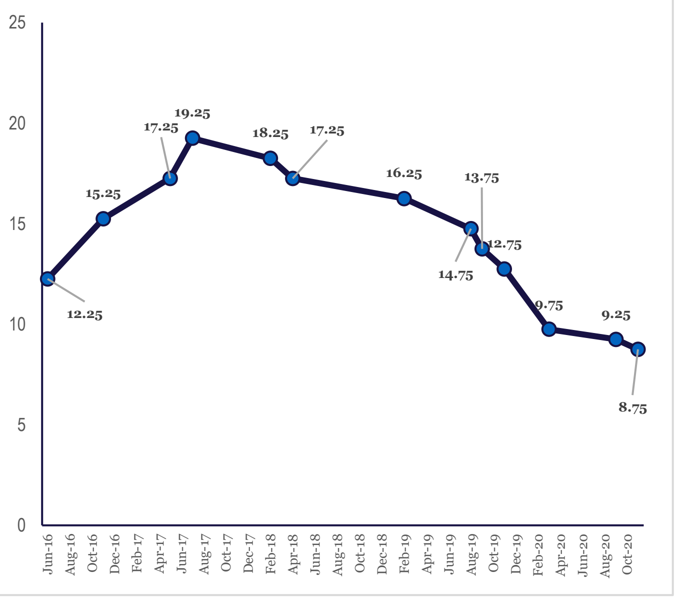
Monetary Sector

- After introducing two rate cuts of 50 bps in H1 2020/21, the CBE adopted a conservative policy in H2 2020/21 on interest rates, including monitoring the inflationary performance as economic activity regained its course. The inflationary performance remained consistently moderate averaging between 4-5 % in H2 2020/21, mainly due to the fluctuations of consumer goods and energy prices.
- Inflation remained below the lower bound of CBE and IMF targets of 7% (+/-2%) during most of FY2020/21 triggering an Article IV consultation. The IMF expects overall rate cuts of 100 bps to promote economic movement while easing interest obligations on the treasury. Egypt's inflation performance is expected to rebound towards the CBE's range of 7% in FY2021/22 on the back of rebounding economic activities, pending vaccination pace.
- The CBE maintained slightly rebounding course towards pre-pandemic foreign reserves levels as it recorded almost USD 41 billion by the end of FY2020/21.

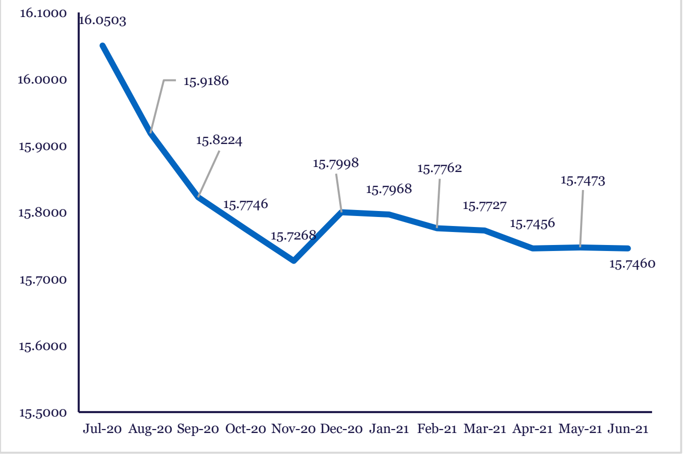
Inflation Rate – y-o-y (%)



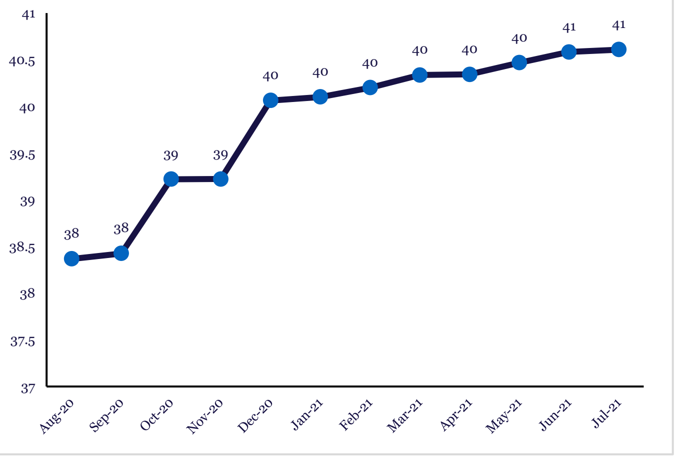
Interest Rate – CBE Main Operations (%)



EGP:USD Exchange Rate



Foreign Reserves (USD Bn)



Source: Central Bank of Egypt

Reforms and Forecasts

Targeted Policies

Revenue Mobilization Strategy

- The GoE will update and introduce its Medium-Term Revenue Strategy (MTRS) to increase the government revenue streams, improve compliance and performance of both tax and custom regimes, in addition to automating the tax process to ensure compliance and enhanced collection.
- The strategy will also introduce new fees including a green fee on the consumption of fuel-based products (gasoline & diesel) and implementing the new personal tax regime effective FY 2020/21 to provide enhanced tax brackets.
- The GoE will seek to apply VAT on e-commerce and digital services and eliminate profit-based tax incentives.

Fostering Private Sector Development

- Seeking a bigger role for the private sector in the economy, the GoE is expected to reduce the role of SoE participation in economic activities through several regulatory, legislative, and financial measures.
- Key measures expected to include enhancing the independence of regulatory authorities through expanding the role of the Egyptian Competition Authority while removing conflicts in regulatory functions among various other agencies.
- The GoE has also signaled its intention to adopt measures to improve the playing field between public and private players, including asserting equal access to industrial land allocation and credit, as well as equal rules on taxation and procurement with SoEs. A more competitive environment for private sector players to enhance its role in GoE-backed mega projects and tenders will also be targeted.

Greater Participation in Global Trade

- The GoE will aim to tackle underutilized potential in global trade participation through facilitating access-to-market for both exports and imports
- The elimination of non-tariff barriers received common ground of understanding between both the GoE and the IMF through enhancing and digitizing custom clearance procedures through the newly introduced ACI system; the system is expected to avail a more lenient access procedures for goods and technologies
- The GoE will also target reforms to ensure predictability of customs procedures, including set timeframes for clearance based on grading-criteria, more lenient sampling procedures for registered, frequent market players.
- Egypt also remains lagging behind in unlocking the potential of its regional and multilateral trade agreements; GoE efforts to support industries with targeted continental markets were announced.

Associated Risks

Vulnerability towards EMs outflow

- Egypt seeks to launch an ambitious strategy to enhance its financial market to avoid the risks associated with another outflow of foreign non-resident portfolio investments. An outflow of USD 14 billion occurred March-April 2020 causing huge risks for Egypt's external position.
- Risks are also associated with tightening of US monetary policy resulting in a wave of outflows from emerging markets and reducing the attractiveness of debt tools.
- IMF encouraged Egypt to ease its monetary policy to reduce the high real interest rates while ensuring the transmission of rate cuts to interbank rates.

Fiscal & External Conditions

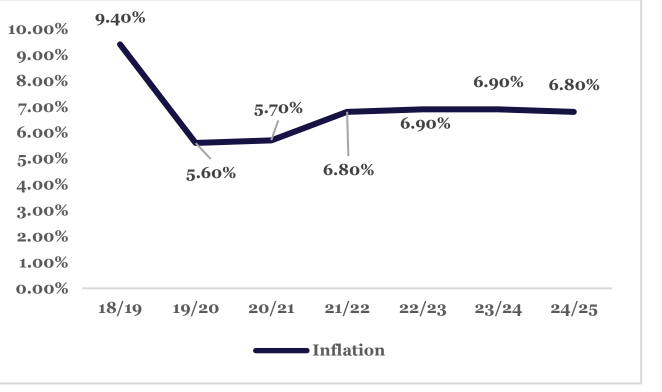
- Egypt's efforts to improve both fiscal and external conditions to fulfil its obligations towards IMF-backed reforms in FY2023/24 and FY/2024/25 are key.
- The improvements in the state's fiscal position through implementing the Public Debt Management Strategy as well as the recently approved restructure of the National Investment Bank (NIB) remain critical. The GoE is set to address the risks associated with the NIB through usage of cash, performing loans, and government securities.
- The GoE is set to recoup equity through swapping non-performing loan collateral for higher-quality government assets.

Source: International Monetary Fund

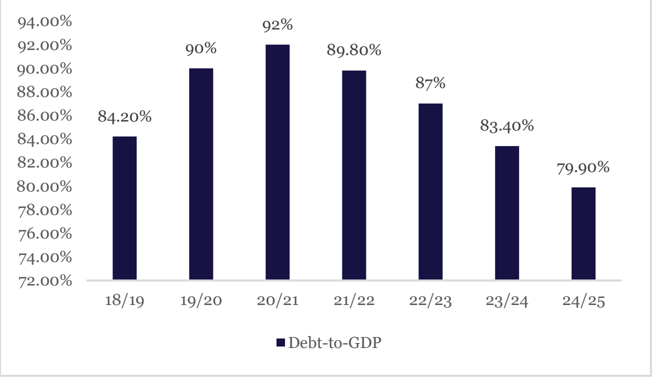
IMF Medium-Term Forecasts

Growth Rate - (%)

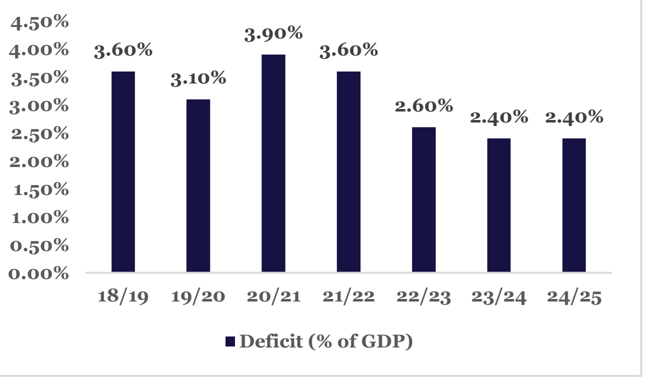
Inflation - (%)



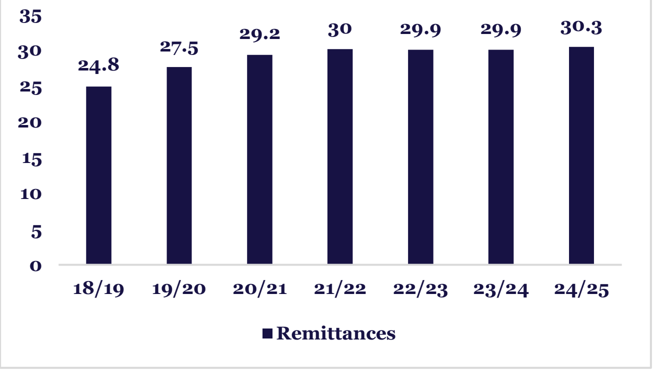
Debt-to-GDP – (%)



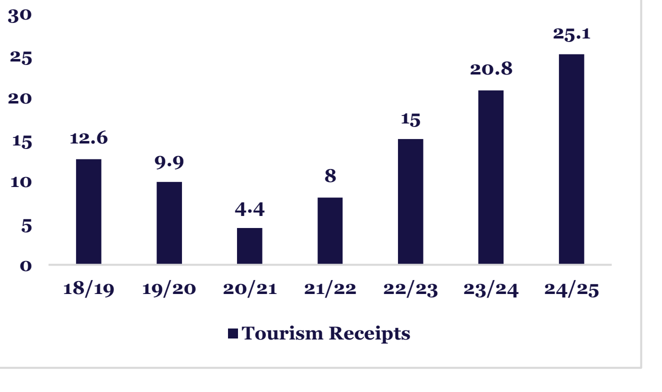
Current Account Deficit – (% of GDP)



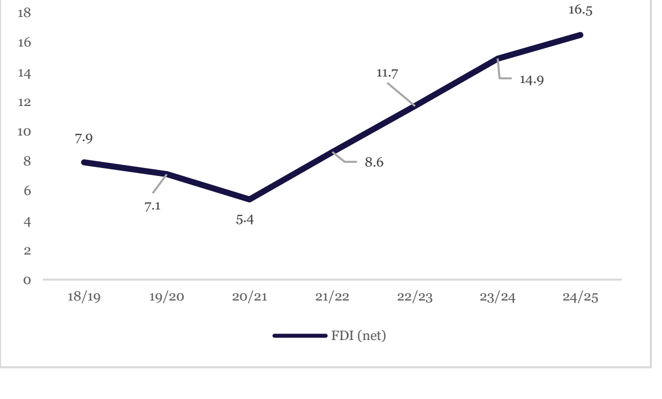
Remittances – (USD Bn)



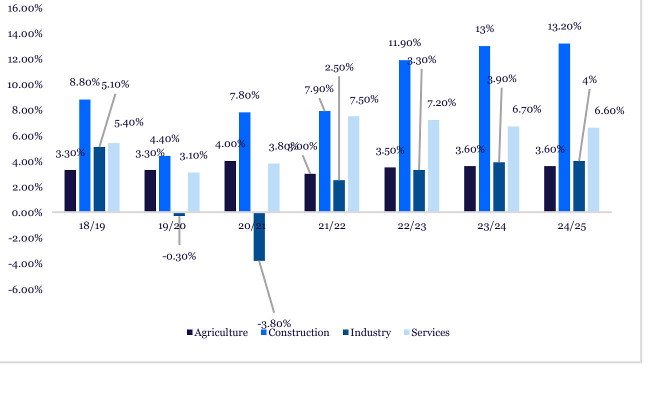
Tourism Receipts – (USD Bn)



Foreign Direct Investment – (USD Bn)



Growth by Sector at Factor Cost – (%)



Source: International Monetary Fund

*Earlier forecasts as per the IMF's August 2020 issue

Thank you

www.lynxegypt.com info@lynxegypt.com 4 Latin America Street, Garden City, Cairo +2 02 27944331