Country update **EGYPT**

Summary

Egypt's economy is slowly recovering from the turmoil surrounding the Arab spring and subsequent events. With an elected government in place, some of the uncertainty of the past years has been removed. This should clear the way for IMF negotiations over a USD 4.8bn loan, next November. The loan will be needed to finance an increasing public debt and boost FX reserves, which dropped to an all-time low last summer. Although we expect GDP growth to come in at a low 2.2% in 2012, the return of both investors and tourist should spur growth in 2013, to over 3%. Still, this will not be enough to create jobs for Egypt's unemployed youth.

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EGYPT

National facts		
Type of government	Republic	
Capital	Cairo	
Surface area (thousand sq km)	997	
Population (millions)	82.5	
Main languages	Arab (100%)	
Main religions	Muslim/Sunnite (90%)	
	Coptic/Christian (10%)	
Head of State (president)	Mohammed Morsy	
Head of Government (PM)	Hisham Qandil	
Monetary unit	EGP (Egyptian pound)	
Economy		**2011**
Economic size	*bn USD*	*% world total*
Nominal GDP	231	0.33
Nominal GDP at PPP	519	0.65
Export value of goods and services	47	0.21
IMF quotum (in mln SDR)	944	0.43
Economic structure	*2011*	*5-year av.*
Real GDP growth	1.8	6.2
Agriculture (% of GDP)	15	14
Industry (% of GDP)	38	38
Services (% of GDP)	48	48
Standards of living	*USD*	*% world av.*
Nominal GDP per head	2800	26
Nominal GDP per head at PPP	6287	50
Real GDP per head	1551	19

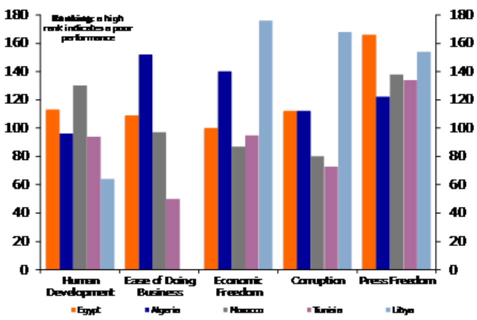
Social and governance indicators			rank / total
Human Development Index (rank)			113 / 187
Ease of doing business (rank)			109 / 185
Economic freedom index (rank)			100 / 179
Corruption perceptions index (rank)			112 / 183
Press freedom index (rank)			166 / 178
Gini index (income distribution)			31
Population below $1.25 per day (PPP)			n.a.
Foreign trade			**2010**
Main export partners (%)		*Main import partners (%)*	
US	8	US	9
Spain	6	China	9
India	5	Italy	8
Italy	2	Germany	6
Main export products (%)			*2011*
Crude petroleum & -products			50
Finished goods (incl textiles)			38
Semi finished products			8
Iron & steel			1
Main import products (%)			
Semi-finished goods			29
Consumer goods			24
Capital goods			20
Petroleum & products			11
Openness of the economy			
Export value of G&S (% of GDP)			20
Import value of G&S (% of GDP)			27
Inward FDI (% of GDP)			-0.2

Source: EIU, CIA World Factbook, UN, Heritage Foundation, Transparency International, Reporters Without Borders, World Bank.

Introduction and update

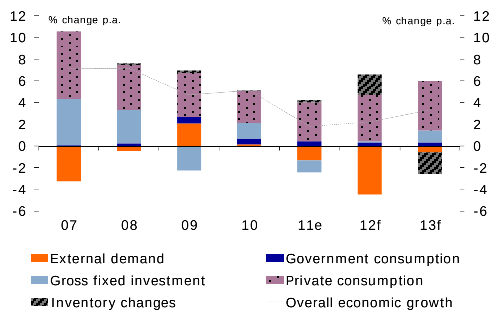
Egypt's economy is slowly recovering from the revolution in the spring of 2011, as well as the political and social turmoil since then. Both foreign investors and tourists pulled out of the country. As a result, the current account deficit increased from 2.6% of GDP in 2010, to 3.2% of GDP in 2011. In addition, foreign exchange reserves fell sharply, from USD 22bn last October, to USD 15.7bn now. GDP growth dropped to a low 1.8% in 2011, from 5.1% the year before. Furthermore, increased public spending and reduced tax income resulted in an expected budget deficit of 10% of

Figure 1: Social indicators



Source: EIU

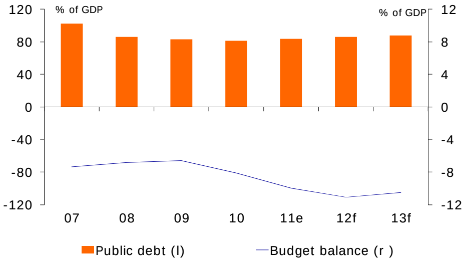
Figure 2: Growth performance



Source: EIU

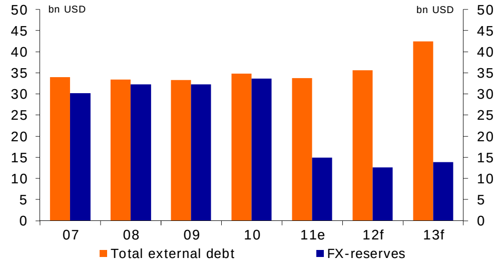
GDP in 2011, which further adds to an already high public debt level of 84% of GDP in 2011. All in all, it is estimated that the government of Egypt requires roughly USD 11bn in the next two years to prevent a fiscal and /or balance of payments crisis. Further unrest would only increase this number and thus the risk of crisis. It is hoped that if the country obtains the USD 4.8bn IMF loan, currently under negotiation, it would be able to attract investors and bilateral donor support.
Still, recent developments are encouraging. In last quarter (April-July) of Egypt's fiscal year , we saw the economy grow by 3.3% y-o-y, while investments rose by nearly 14%. For 2012, we expect an 2.2% growth rate. In 2013, the recovery is expected to gain pace with a growth rate of 3.3%, as both investors and tourists are returning. Still, higher growth is needed to create jobs for the many unemployed youth in Egypt.

Figure 3: Public finances



Source: EIU

Figure 4: FX reserves and debt



Source: EcoWin

Political transition

Without doubt, Egypt's transition process following the revolution in 2011 has been a bumpy one. Amidst ongoing protests and social tensions, the power struggle between the military and the widely popular Muslim Brotherhood has been a source of large political risks. In addition, as became very clear last September when protesters attacked the US embassy in Cairo, full stability is yet to be achieved. Nonetheless, over the past months Egypt's political situation stabilized considerably. During free and fair elections last June, Egyptians elected Muslim Brotherhood's Mohammed Morsy as their new president. Morsy immediately calmed fears of him having an Islamist agenda, by appointing a technocratic and largely secular government. In addition, his firing of two high-ranked military officials strengthened his government's position vis-à-vis the military, while his efforts to improve international relations helped secure emergency funds from the Gulf countries. But, it has not all been smooth sailing. Amidst the attack on the US embassy last September, Morsy was faced with the choice between maintaining domestic support and ensuring sound relations with the US. His decision to keep the peace domestically and thus not to denounce the protests has been subject to criticism and has been used as evidence by those wishing to portrait the government as anti-US and pro-Islam. Such imagery is dangerous as it could well deter foreign investors.

The next step in Egypt's transition process will be the draft of a new constitution, which is to be followed by a new round of parliamentary elections. Although the draft is near completion, disagreements and tensions within the responsible assembly could delay the final approval of the draft. We therefore do not expect parliamentary elections before the end of 2012.

IMF to the rescue?

At the start of November 2012, an IMF delegation will visit Egypt to discuss a USD 4.8bn loan. The loan is needed to support public finances and simultaneously strengthen FX reserves. In order to secure the loan, the government needs to show that it is willing to cut spending on fuel subsidies, so as to trim down the budget deficit, as fuel subsidies make up 20% of public spending. To this end, it has implemented a law forcing shops to close after 10pm. The idea behind the law is that while it saves energy, and thus reduces costs, it will not lead to the type of protests that a subsidy cut will likely induce. Unfortunately, this law will be hard to enforce and will not save enough energy to have a real impact. Plus, if it is enforced, the loss in revenue from the fall in economic activity, could very well outweigh the cut in spending. Nonetheless, given the sensitivities attached to this fuel subsidy, we do not expect more drastic measures in the immediate term. Instead, we think it likely that the IMF will agree to delayed measures over the course of 2013 and 2014.

Country update EGYPT

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Selection of economic indicators	2007	2008	2009	2010	2011e	2012f	2013f
Key country risk indicators							
GDP (% real change pa)	7.1	7.2	4.7	5.1	1.8	2.2	3.3
Consumer prices (average % change pa)	9.5	18.3	11.8	11.1	10.2	7.6	8.2
Current account balance (% of GDP)	0.1	-0.8	-1.7	-2.6	-3.3	-3.2	-3.3
Total foreign exchange reserves (m USD)	30188	32216	32253	33612	14916	12560	13840
Economic growth							
GDP (% real change pa)	7.1	7.2	4.7	5.1	1.8	2.2	3.3
Gross fixed investment (% real change pa)	23.7	14.8	-10.2	7.7	-5.6	0.7	6.0
Private consumption (% real change pa)	8.8	5.7	5.7	4.1	5.0	5.9	6.0
Government consumption (% real change pa)	0.2	2.1	5.6	4.5	3.8	3.1	3.0
Exports of G&S (% real change pa)	20.2	28.8	-14.5	-3.0	3.7	-4.2	11.0
Imports of G&S (% real change pa)	30.5	26.3	-17.9	-3.2	8.1	10.6	10.3
Economic policy							
Budget balance (% of GDP)	-7.3	-6.8	-6.6	-8.1	-10.0	-11.1	-10.5
Public debt (% of GDP)	102	86	83	81	84	86	88
Money market interest rate (%)	6.9	11.6	9.8	9.3	14.0	14.5	11.8
M2 growth (% change pa)	19	10	9	12	7	17	9
Consumer prices (average % change pa)	9.5	18.3	11.8	11.1	10.2	7.6	8.2
Exchange rate LCU to USD (average)	5.6	5.4	5.5	5.6	5.9	6.1	6.8
Recorded unemployment (%)	n.a	n.a	n.a	n.a	n.a	n.a	n.a
Balance of payments (m USD)							
Current account balance	194	-1331	-3195	-5596	-7581	-8130	-8250
Trade balance	-20801	-26774	-22475	-27673	-28218	-33240	-34640
Export value of goods	24455	29849	23089	25024	27913	26080	28580
Import value of goods	45256	56623	45564	52698	56132	59320	63220
Services balance	11195	14312	13242	15482	11732	12820	13910
Income balance	1478	1373	-1922	-5843	-6315	-6820	-5520
Transfer balance	8322	9758	7960	12439	15221	19110	17990
Net direct investment flows	10913	7575	6141	5210	-1108	3850	2860
Net portfolio investment flows	-4217	-7650	-527	8942	-10072	-610	840
Net debt flows	2054	-80	-251	1864	-2123	2870	7230
Other capital flows (negative is flight)	-3151	3960	-2085	-8561	2751	230	-1570
Change in international reserves	5793	2475	84	1859	-18133	-1800	1110
External position (m USD)							
Total foreign debt	33998	33365	33308	34844	33751	35570	42480
Short-term debt	2236	2843	2561	3149	3026	4170	4380
Total debt service due, incl. short-term debt	4243	4983	5755	5537	7295	6540	7680
Total foreign exchange reserves	30188	32216	32253	33612	14916	12560	13840
International investment position	-8364	-27028	n.a.	n.a.	n.a.	n.a.	n.a.
Total assets	76365	67351	n.a.	n.a.	n.a.	n.a.	n.a.
Total liabilities	84729	94379	n.a.	n.a.	n.a.	n.a.	n.a.
Key ratios for balance of payments, external solvency and external liquidity							
Trade balance (% of GDP)	-15.7	-16.2	-12.0	-12.9	-12.2	-13.0	-13.6
Current account balance (% of GDP)	0.1	-0.8	-1.7	-2.6	-3.3	-3.2	-3.3
Inward FDI (% of GDP)	8.8	5.8	3.6	3.0	-0.2	1.6	1.3
Foreign debt (% of GDP)	26	20	18	16	15	14	17
Foreign debt (% of XGSIT)	61	49	62	56	53	53	60
International investment position (% of GDP)	-6.3	-16.4	n.a.	n.a.	n.a.	n.a.	n.a.
Debt service ratio (% of XGSIT)	8	7	11	9	12	10	11
Interest service ratio incl. arrears (% of XGSIT)	2	1	2	1	1	1	1
FX-reserves import cover (months)	5.4	5.4	7.2	6.3	6.3	2.6	2.1
FX-reserves debt service cover (%)	711	647	560	607	204	192	180
Liquidity ratio	173	171	166	157	159	127	124

Source: EIU