ECONOMIC PULSE

OF EGYPT

January 2024

SUMMARY

Egypt's economic landscape reveals a tapestry of significant developments, responding dynamically to both internal and external factors. The Central Bank of Egypt's strategic response to a drop in monthly inflation, down to **33.7%** annually, includes a substantial **200 basis points increase** in key policy rates. While this bold move aims to tackle inflation, concerns loom over potential impacts on purchasing power and the pricing dynamics of goods and services.

Amid these challenges, positive signals emerge from the government's announcement of a robust **5.4% real GDP growth** in the first half of the fiscal year, surpassing the previous year's **5.2%**. The ambitious target of achieving **5.6% growth** in the second half positions the fiscal year for an overall commendable growth rate of **5.8%.**

Egypt's net foreign reserves experienced incremental growth in December, **reaching USD 35.22 billion,** marking the sixteenth consecutive month of recovery since September 2022. Despite external challenges in 2022, the country's resilient performance showcased consistent monthly gains and stability in its external financial position. The dominance of regional deposits, including contributions from Saudi Arabia, the UAE, Qatar, Kuwait, and Libya, played a pivotal role, accounting for over 85% of the total reserves.

However, the International Monetary Fund (IMF) introduces a note of caution by revising down Egypt's GDP **forecast for the fiscal year to 3%**, underscoring persistent economic challenges. The recent downgrade of Egypt's credit outlook by **Moody's to negative, while maintaining a Caa1 rating**, amplifies the severity of economic pressures. Notably, concerns heighten as interest payments could potentially absorb two-thirds of Egypt's revenue by the fiscal year's end. The depreciation of the Egyptian pound on the black market signals a tangible shortage of hard currency, introducing potential risks to the country's credit rating.

Simultaneously, the imminent agreement between the Egyptian government and the IMF marks a pivotal moment, aiming to unlock the remaining $3 billion loan tranches and secure additional support. **This strategic move, extending the loan duration beyond four years, is anticipated to stimulate a substantial $10 billion in support from development partners, with the loan's duration ranging between 5-6 years.**

SUMMARY

Addressing the pressing dollar crisis, various solutions are under consideration, with ongoing efforts to explore ideas for resolution. Notably, discussions on investment opportunities, particularly the **Ras El Hekma project**, have garnered attention. The rumored advance payment of **$22 billion** for the project has sparked interest, and the widespread dissemination of news surrounding the initiative has contributed to a decline in the parallel market's dollar price.

Aligning with broader economic reforms, the Central Bank seeks a reduction of the pound's exchange rate, and legislative initiatives emphasize a flexible exchange rate policy and the empowerment of the private sector. These measures, combined with expected financial assistance, form a comprehensive strategy to bridge the financing gap and cultivate an investment-friendly climate.

Concurrently, the **S&P Global PMI®** data for Egypt's non-oil private sector in December 2023 illustrated a resilient business landscape amidst challenges. Slowing demand, fueled by pound weakness and supply shortages, led to significant declines in both activity and new orders. Despite contending with rapid input cost inflation and reduced customer spending, businesses demonstrated resilience by effectively curbing price hikes. **Positive signals**, including the first increase in employment in three months and a recovery in future output expectations, underscored adaptability and forward-looking optimism. Businesses strategically stabilized backlogs of work, showcasing an optimistic outlook amid economic headwinds.

Adding to this resilience, the **Ministry of Finance's new policy on FX calculations for tax purposes complements the economic landscape.** Designed to address FX rate disparities, the policy allows businesses, particularly importers and exporters, to consider price differences between official and parallel market rates. With varying percentages for different periods in 2023, the scheme aims to alleviate the financial impact on businesses. However, restrictions focus on the FX difference between export revenues and import costs, intending to discourage currency trading on the parallel market.

IPA delves into these developments, offering an in-depth insight into the the progress made in terms of the structural reforms.

January

UPDATES
IN FIGURES

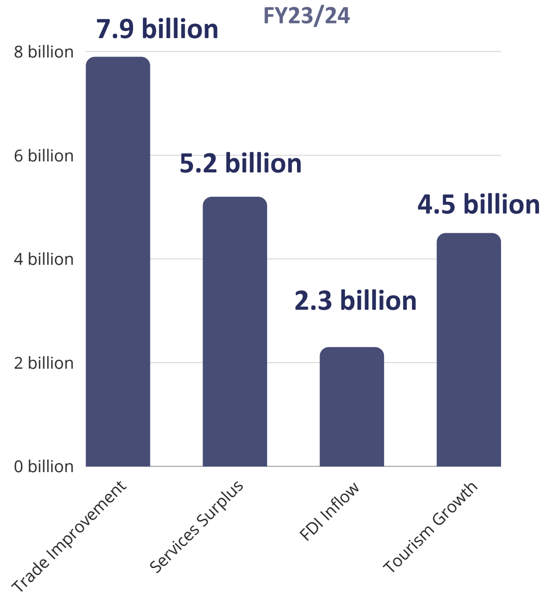
The first quarter of the fiscal year 2023/2024 witnessed notable developments in Egypt's economic transactions with the rest of the world, resulting in an overall **Balance of Payments (BOP) surplus of US$ 228.8 million**. While this marked a decrease compared to the previous year, the shift was influenced by various factors impacting the current account and capital and financial account.

FY23/24

(BOP) surplus of US$ 228.8 million

Positive Trends

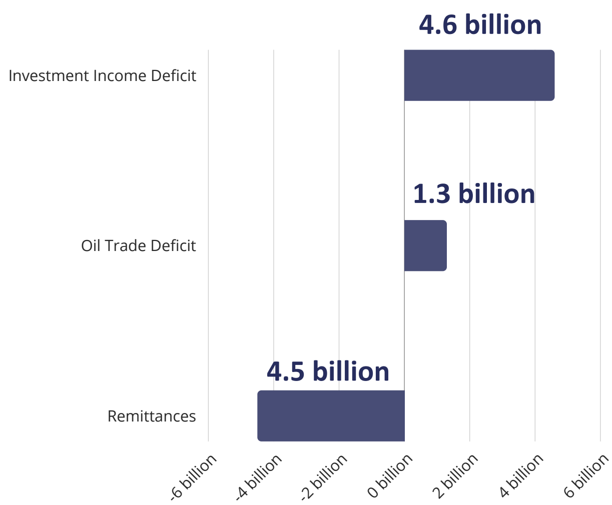
Egypt experienced positive economic trends, including a **12.7%** reduction in the trade deficit , a services surplus of **US$ 5.2 billion** driven by increased Suez Canal transit receipts and tourism revenues, a net inflow of **US$ 2.3 billion** in Foreign Direct Investment (FDI), and a **9.3%** growth in tourism revenues.



Source: CBE

Challenges and Constraints

Despite positive economic trends, challenges included a widened oil trade deficit of **US$ 1.3** billion due to declining exports, a **29.9%** drop in remittances to **US$ 4.5 billion**, and a **1.1% increase in the investment income deficit to US$ 4.6 billion.** These factors highlight nuances in Egypt's economic landscape during the quarter.



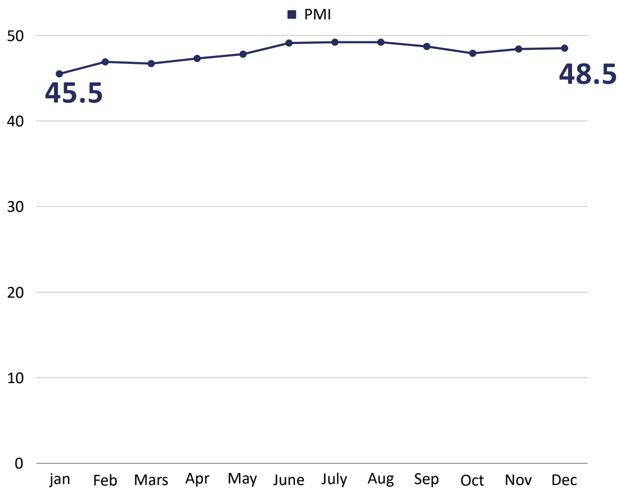
Source: CBE

January

UPDATES IN FIGURES

Challenges in Egypt's Non-Oil Private Sector

The latest S&P Global PMI® data for Egypt's non-oil private sector reveals ongoing challenges as conditions worsened at the end of 2023. Slowing demand, attributed to weakness in the pound and supply shortages, led to sharper declines in activity and new orders. Despite facing rapid input cost inflation and reduced customer spending, businesses showed resilience by containing price hikes. A modest increase in staffing numbers and a recovery in future output expectations offer some positive signals.



Source: S&P

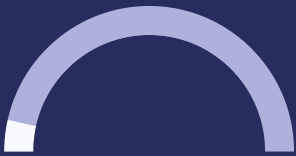
The composite PMI® posted **48.5** in December, indicating a modest deterioration in the health of the non-oil sector. While marginally higher than November's reading of 48.4, it reflects the impact of slowing demand and supply challenges.

Moody's has downgraded Egypt's credit outlook

Moody's estimates that interest payments will absorb two-thirds of Egypt's revenue by the end of the fiscal year. The Egyptian pound's decline on the black market highlights the severe shortage of hard currency, and Moody's suggests a potential rating downgrade if concerns arise about the government's ability to service its local currency debt or boost foreign reserves. An upgrade could occur with increased foreign exchange inflows. Moody's sees a high likelihood of the IMF program being boosted to cover Egypt's external funding gap in the 2024 and 2025 fiscal years. Confidence rebuilding will require an improvement in economic policy

Trade Balance

Egypt's trade deficit



$1.3 billion

The deficit of oil trade balance widened by US$ 1.2 billion to US$ 1.3 billion (against US$ 106.0 million), primarily due to the decline in oil exports, as shown below:

Oil Exports

$1.6 billion

Oil Imports

$2.9 billion

$ 40 Billion

Egyptian exports to the world in the fiscal year 2022/2023

$ 70.8 Billion

Egyptian imports from the world in the fiscal year 2022/2023

ECONOMIC GROWTH TARGETS

The Egyptian government aims to triple annual foreign exchange (FX) inflows to **USD 300 billion by 2030**. The strategy, outlined in an IDSC report, focuses on increasing exports, boosting tourism, raising remittances, attracting foreign direct investments (FDI), optimizing Suez Canal revenues, and implementing strategic securitization plans.

Key Elements of the 2030 Strategy

Export

Targeting annual export growth of at least 20% to reach USD 145 billion.

20%

Tourism Revenues

20% annual increase in tourism revenues to USD 45 billion.

FDI Increase

10% annual increase in FDI, including real estate investments, to USD 19 billion.

10%

Suez Canal

Striving for a 10% annual boost in Suez Canal revenues to USD 26 billion.

Remittances

Seeking a 10% annual rise in remittances from Egyptians abroad to USD 53 billion.

10%

Outsourcing Revenues

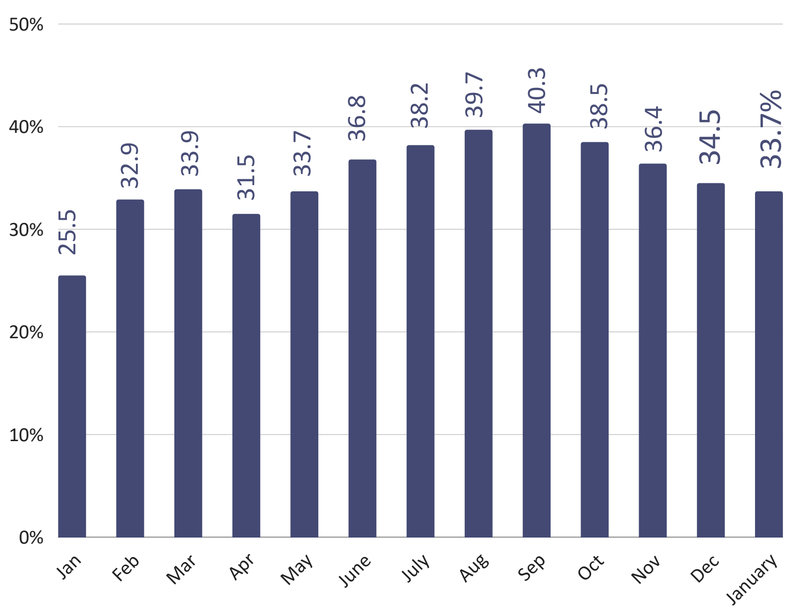
Targeting a 10% annual increase in outsourcing revenues to USD 13 billion.

MONETARY POLICIES

Inflation

In December 2023, the monthly inflation rate increased to 1.2% from 0.9% the month before. Furthermore, from its highest level ever recorded in September 2023 at 38%, the consumer price inflation rate dropped to **33.7%** in December 2023 from 34.6% in November 2023 and 21.3% in December 2022. The annual inflation rate in Egypt was 34.2% in December 2023 as opposed to 35.9% in November 2023, according to data from the Central Bank of Egypt.

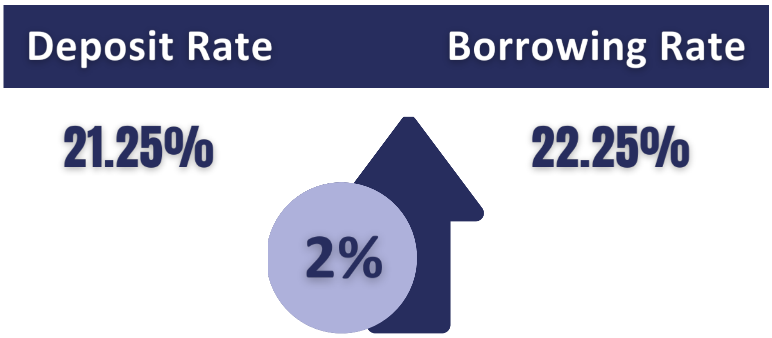
The Monthly Inflation Rate on an annual basis



Source: CAPMAS

Interest Rate

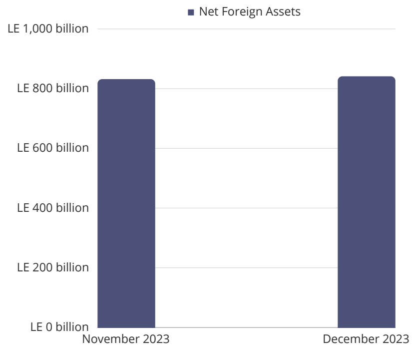
In its recent meeting, the Monetary Policy Committee (MPC) opted for a decisive move, choosing to raise key policy rates by **200 basis points**. The Central Bank of Egypt's (CBE) overnight deposit rate, overnight lending rate, and the main operation rate were all elevated to **21.25 percent**, **22.25 percent**, and 21.75 percent, respectively. Concurrently, the discount rate saw an increase of 200 basis points, reaching 21.75 percent.



MONETARY POLICIES

Net Foreign Assets

The Central Bank of Egypt (CBE) revealed a slight decline in Egypt's net foreign assets (NFAs), reporting a negative **LE 841.391 billion** in December 2023, compared to a negative **LE 831.924 billion** in November.

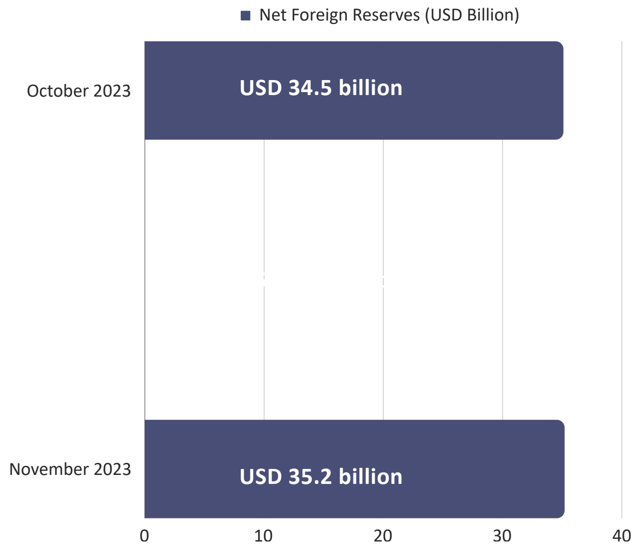


Source: CBE

The net foreign assets deficit rose to **$27.2 billion** in December 2023, a slight uptick from November's **$27 billion**, according to the latest CBE data. The CBE's NFAs saw a slight bump to LE 1.058 trillion during the final month of 2023, compared to LE 1.056 trillion, pulling its **net foreign asset deficit** to negative **$11 billion** in December, up from negative **$11.2 billion** reported the month prior.

Egypt's Foreign Reserves

International reserves experienced a noteworthy boost, surging by **USD 548 million** in April 2023 and reaching a total of USD **34.5 billion.** This positive trajectory continued through November, marking the fifteenth consecutive monthly increase. At the close of November, net foreign reserves climbed to **USD 35.2 billion**, showcasing the Central Bank of Egypt's steadfast efforts in rebuilding financial stability.



Source: CBE

January

SCENARIOS

Given the prevailing economic conditions in Egypt, our team of experts has crafted the following scenarios. These scenarios do not rely on concrete data but rather on market sentiments and forecasts, especially regarding the potential devaluation of the Egyptian pound against the dollar in the near term. It's crucial to emphasize that these scenarios are speculative in nature and do not represent factual data; instead, they aim to contemplate various potential outcomes for future developments.

SCENARIO 1

Devaluation to Achieve a Range of 40-45 EGP against USD

In this scenario, there is a deliberate effort to decrease the value of the Egyptian pound within a specified range of **40 to 45 against the US dollar.** The main aim is to better synchronize the official exchange rate with the rates observed in the parallel market. This strategy involves a carefully orchestrated devaluation approach, enabling a controlled adaptation to the economic environment.

SCENARIO 2

Dual Pricing System

The suggested scenario proposes implementing a dual pricing system for the US dollar. Within this framework, a set exchange rate, such as around the thirties, **would be designated for essential goods and raw materials, while a distinct rate would apply to non-essential or luxury items,** possibly around the forties.

SCENARIO 3

Gradual Liberalization

The phased approach to gradual liberalization would involve the central bank periodically adjusting the exchange rate in incremental phases, approximately 10% for each phase. This strategy enables the market to react naturally to economic conditions while mitigating the potential for sudden shocks.

In 2015, Influence Public Affairs (IPA) is a key subsidiary of Influence Communications Group, a prominent marketing communications consultancy in Egypt since 2007, with a diverse clientele of over 90 local and regional clients.

As a leading public policy and public affairs firm, IPA is committed to creating a positive societal impact. Our seasoned professionals bring extensive expertise, actively shaping government policies, and facilitating effective stakeholder communication. With a deep understanding of Egypt's political landscape, regulatory frameworks, and socioeconomic dynamics, we transcend the traditional role of a public affairs firm, assuming the mantle of a distinguished think tank and research institute.

Dedicated to the economic and public policy landscape of Egypt and the Middle East, IPA provides invaluable insights and strategic guidance. Our expertise serves as a beacon of knowledge, guiding you through the evolving business environment, ensuring your endeavors are rooted in wisdom and poised for success.

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