Euler Hermes Economic Research

Country Risk Analysis

Egypt

Political transition takes another turn

General Information

GDP	USD229.5bn (World ranking 43, World Bank)
Population	82.54 million (World ranking 15, World Bank 2011)
Form of state	Republic
Head of government	Adli Mansour (interim President)
Next elections	Undergoing political transition, fluid electoral timetable

Strengths

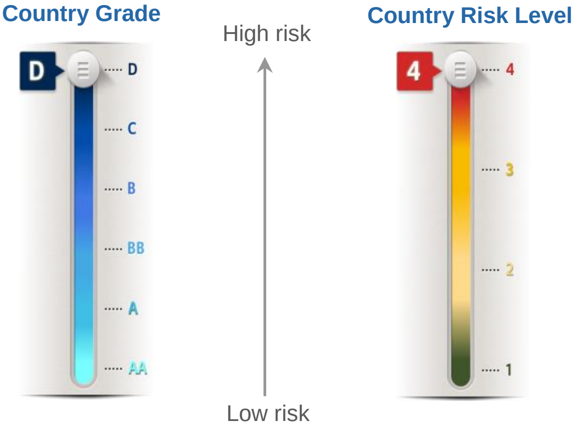
- Large domestic market and strategic position between the regional Middle Eastern and African markets.
- Relatively diversified economy and sources of FX generation: including oil and gas, tourism, Suez Canal and a manufacturing base.
- Although an IMF facility is proving time consuming, financial assistance from the US and the region (particularly the GCC) remains supportive.
- External debt repayments are comfortable.

Weaknesses

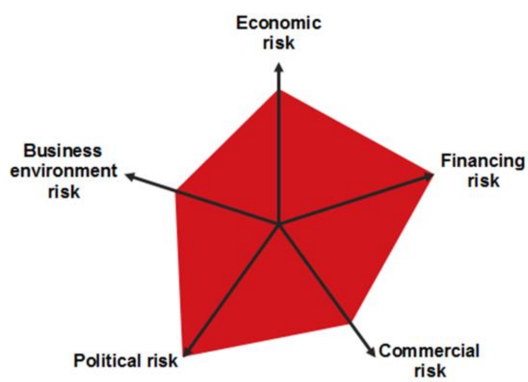
- Nascent political system, with untested abilities of new government to implement policies and retain support within the country. Recently unseated elected head of state and uncertain political transition.
- Regional uncertainties (relationship with Israel, contagion risk from Syria and Iran's nuclear programme).
- Poverty and lack of job prospects, two underlying reasons behind pressures for regime change, have not been tackled effectively.
- The difficult and protracted political transition has slowed the rebound in economic performance, with consumption and investment (domestic and foreign) awaiting clarity of policies.

Country Rating

D4

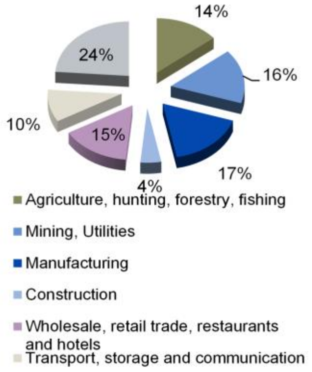


Risk Dimensions



Economic Structure

GDP breakdown (% of total, 2011)



Trade structure (% of total, 2011)

By destination/origin

Exports		Rank		Imports
Italy	8%	1	12%	United States
Non-OPEC Middle East	8%	2	8%	China
United States	7%	3	7%	Germany
Other Gulf	6%	4	7%	Italy
Spain	6%	5	4%	Other Gulf

By product

Exports		Rank		Imports
Crude Oil	13%	1	7%	Refined Petroleum Products
Natural Gas	12%	2	6%	Cereals
Refined Petroleum Products	12%	3	5%	Engines
Other Edible Agricultural Proc	6%	4	4%	Iron Steel
Non Ferrous Metals	4%	5	4%	Plastic Articles

Sources: Chelem, UnctadStat, IHS Global Insight, Euler Hermes

Economic Forecast

	2009	2010	2011	2012	2013f	2014f
GDP growth (% change)	4.7	5.1	1.8	2.2	2.0	3.0
Inflation (%, end-year)	13.2	10.6	9.5	4.7	13.5	8.0
Fiscal balance (% of GDP)	-6.6	-7.7	-10.1	-10.9	-13.5	-11.5
Public debt (% of GDP)	61.8	61.7	64.6	68.1	74.5	78.0
Current account (% of GDP)	-1.8	-2.1	-2.4	-2.8	-2.2	-2.0
External debt (% of GDP)	18.6	17.0	15.2	14.8	16.0	14.0

Source: IHS Global Insight, national sources, Euler Hermes

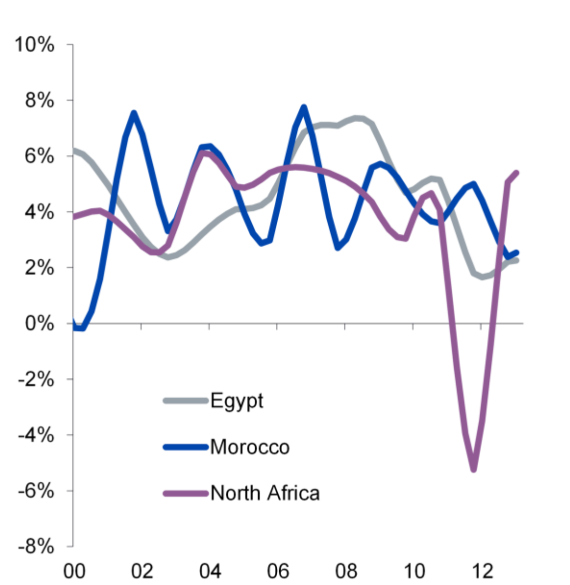
Economic Growth

Growth momentum depends on the political transition

Growth of GDP in North Africa fell markedly in 2011 (see chart), particularly in Libya, and registered only +1.8% in Egypt, after over +5% the year before. All sectors of the economy were adversely affected by the period of demonstrations, strikes and regime change and by the uncertainties that followed. In particular, tourism was badly affected, with visitor numbers and sector earnings down sharply. Widespread demonstrations have dwindled in intensity and levels of activity have therefore increased, but only moderately. Uncertain governance (changes to the electoral timetable) and policies (with several key reversals) continued into 2012, so that domestic consumption and investment were constrained and foreign investment very limited. GDP growth in that year is estimated at just over +2%.

Most of the factors impeding higher growth in 2011-12 were evident in H1 2013 but the unseating of the elected government of Mohamed Morsi in July engendered even more uncertainty and GDP is now forecast to expand by (below potential) +2% this year. With a new election timetable to be worked through and prospect of an IMF facility now more distant, growth is unlikely to exceed +3% in 2014. GDP forecasts are dependent on stability being maintained and are therefore tentative.

GDP growth (%)

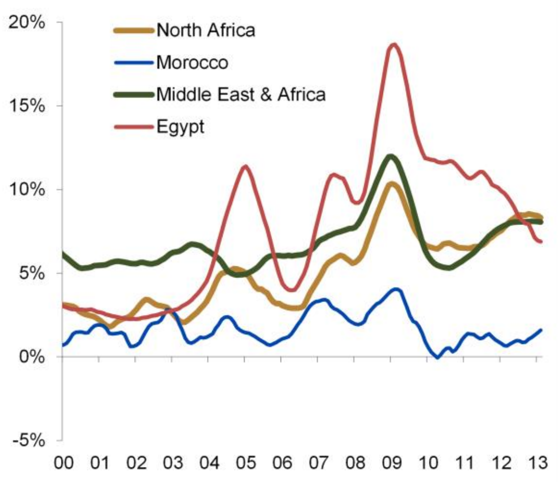


Sources: IHS Global Insight, Euler Hermes

Economic Policies

Since the fall of the Mubarak regime in 2011, economic policies have been uncertain, reflecting the inexperience of a new leadership and an inability to counter the economic deterioration while meeting expectations of the population. With the fall of the Morsi government in July 2013, further uncertainty in relation to the overall direction of economic policies is now prevalent.

Inflation rate (%)



Sources: IHS Global Insight, national sources, Euler Hermes

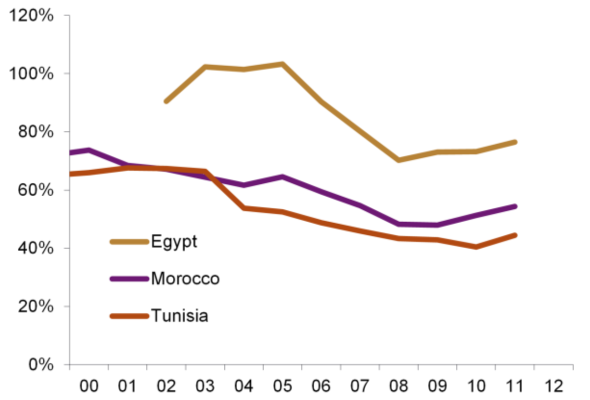
High inflationary pressures set to continue

Average annual inflation was over 7% in 2000-08 and remained elevated through to the time of the political transition, ending 2011 at 9.5%. The social impact of high prices will remain a key concern of the government as it attempts to limit further protests. A policy of subsidy reduction is difficult to implement against such a background. Moreover, EGP depreciation and a high import propensity (Egypt is an exporter of crude oil and gas but requires inflows of refined energy products and it is the world's largest wheat importer) will keep inflationary pressures high in 2013 and 2014. The central bank will remain cautious in relation to monetary policy, balancing the inflation/growth dynamics and social imperatives.

The fiscal deficit has widened

Traditionally high fiscal deficits (with subsidy provision a leading cause) have been heightened because of the current political and economic environment. Annual average fiscal deficit-GDP ratios are likely to register double digits in the period 2011-14. Deficits of this magnitude are not sustainable and the IMF is likely to want strong evidence that whatever government is in place can implement some austerity measures in this regard. EH believes that only limited progress will be achievable in relation to fiscal deficits, given the social imperatives of maintaining cheap foodstuffs and overall stability.

General government debt (% GDP)



Sources: IHS, Euler Hermes

And public debt is increasing

The public debt-GDP ratio had been declining pre-crisis compared with a ten-year average trend and is estimated to have remained below 70% in 2012. However, with revenue streams limited but spending needs remaining high, public borrowings will increase and debt is set to rise, perhaps to around 78% of GDP by 2014.

External Sector

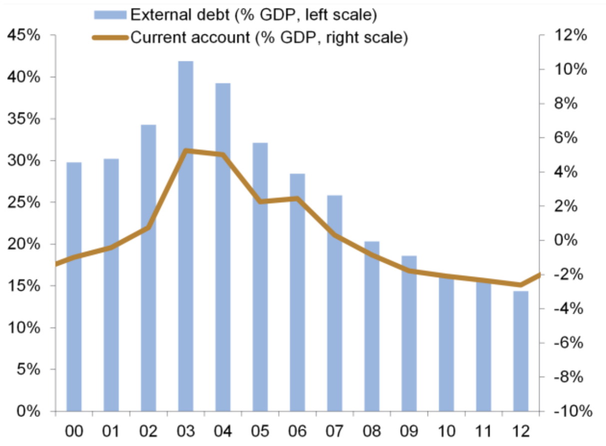
Current account deficits, weak FDI but low foreign debt ratios

The current account balance registered an annual average surplus of 1.5% of GDP in 2000-08 but deficits began to be registered even before the Mubarak regime change and accompanying economic slowdown from 2011. As with the fiscal accounts and other economic indicators, current account deficits increased with the onset of political change, reflecting a combination of disruption to the domestic economy, high propensity to import and reduced tourism earnings.

Foreign direct investment (FDI) is unlikely to recover to inflow levels seen pre-regime change (Mubarak's fall) until stability and security and a track record of political consolidation are observable.

External debt ratios and servicing of existing obligations were relatively low going into the crisis period. Inevitably, these ratios will also deteriorate as financial assistance will involve extending foreign obligations at a time when GDP and export receipts are constrained.

External Debt and current account balance (% of GDP)



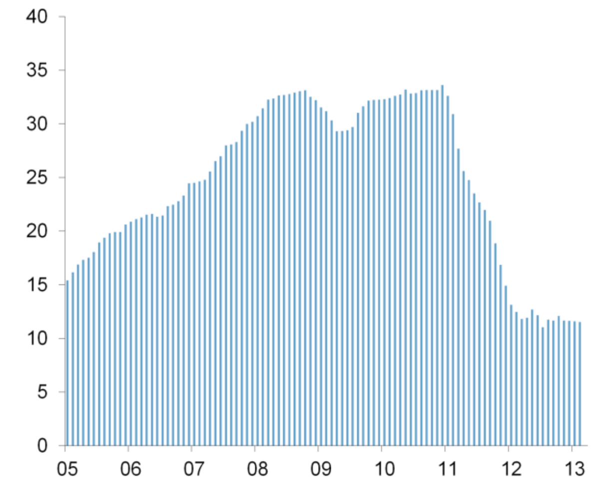
Sources: IHS Global Insight, national sources, Euler Hermes

Foreign exchange reserves have fallen markedly

Official foreign exchange reserves (excluding gold) have fallen sharply and now (USD15 billion at end-June 2013) only cover around three months of imports of goods and services, which is the international benchmark minimum comfort level. However, this level of reserves is almost wholly because of aid inflows from countries such as Qatar (USD3 billion in May). In contrast, the domestic economic activities that should be responsible for reserve accumulation (including the tourist sector, associated and other service sectors and the manufacturing industry) remain weak.

Since the fall of the Morsi government, other GCC states, including Saudi Arabia, have pledged a further USD12 billion in loans, grants and oil concessions but increasing FX organically from net economic transactions will be difficult, placing more emphasis on support from external sources.

FX reserves USD bn



Sources: IHS, Euler Hermes

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