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FOREIGN AFFAIRS & TRADE
Manatū Aorere

Egypt Economic Update

Market Report

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Prepared by the Embassy in Cairo.

Summary

1 Several negative factors are currently impacting Egypt's economy include low foreign currency reserves, high interest payments, the Russia-Ukraine war; reduced tourism; food insecurity; and high inflation. As a result, the Egyptian Government is taking steps to curb inflation, increase local production and exports, reduce reliance on imports, and bolster both foreign investment and foreign exchange reserves.

2 Mitigating measures such as a possible International Monetary Fund (IMF) loan, high Gulf investment and implementation of Egypt's localisation and privatisation programmes may aide Egypt's balance of payments.

3 New Zealand exporters can expect ongoing measures aimed at increasing local production and exports, and reducing imports. There are exemptions to these policies for the import of essential commodities and goods for Egyptian local production, such as in the production of basic foodstuffs.

Report

Egypt's economic outlook

- A World Bank report released in July indicated Egypt held foreign debt of nearly USD$158 billion at the end of March. Egypt had committed to repaying USD$33 billion over March 2022-March 2023. The country's foreign currency reserves were estimated at USD$33.3 billion.
- In May, credit rating agency Moody's lowered its future projections for Egypt from stable to negative.
- There are calls by analysts for further devaluation of the Egyptian pound (EGP) and markets are pricing in anticipation of further depreciation. Investment research company Tellimer Research forecasts that the Egyptian pound could slide an additional 10 percent over the coming three months and 22 percent over the next year (this follows a previous depreciation of 14 percent in March 2022).
- Inflation hit a three-year high in July, according to Egyptian state statistics agency Capmas. Core inflation, which excludes volatile items like food and fuel, increased to 15.6 percent nationwide in July, up from 14.6 percent in May. Inflation in Cairo is estimated to be around 25 percent. The decision to raise fuel prices and reduce government subsidies in July has increased transport costs by 17 percent from July 2021.
- The Central Bank of Egypt (CBE) has increased interest rates by 300 basis points since March in a bid to curb inflation. The CBE has indicated it is aiming for 7 percent (±2 percent) inflation by the end of 2022 but will "temporarily tolerate" an elevated inflation rate until 2023. On 18 August, Egypt's Monetary Policy Committee (MPC) committed to retaining the current interest rates, with the overnight lending and deposit rates steady for now at 12.25 percent and 11.25 percent respectively.

State Ownership Policy: a new "economic constitution"

- The Egyptian Government is currently leading consultations on a new state ownership policy. It proposes the privatisation of public assets and seeks increased private-sector participation from the current levels of 30 percent up to 65 percent over the coming three years.

- According to the proposed policy, Egypt will exit within three years a number of activities in the agricultural sector and grains, with the exception of wheat; drinking and waste water; communications and information technology; accommodation services; and food and beverage services. The Government may maintain or reduce its presence in the transportation sector; education; water sector; mining; power; real estate; mobile phone services; and sports.
- Egypt will maintain or increase investments in some activities in education; water; the Suez Canal; healthcare; social work; wholesale trade; and power transmission.

Push to increase exports and decrease imports

- Egypt continues its push to maintain levels of foreign currency by cutting imports. The most significant measure has been the CBE's requirement, introduced in February 2022, for importers to use a letters of credit (LC) to finance imports instead of 'cash-against-documents' system which enabled traders to make a lower payment in advance and the rest at a later date. Importers have been required to pay the full amount to banks in advance of shipment. This has allowed the CBE to control the influx of imports and the resulting exit of foreign currency. There have been exceptions, including for essential commodities and raw materials for local production.
- The above policies to reduce imports are impacting the availability of consumer goods and the ability of factories to access raw materials. This has flow on impacts for local supply and Egypt's exports.
- Egypt has taken steps to encourage domestic production. Earlier in 2022, the Government announced nine priority investment industries to promote localisation of manufacturing to help raise exports to USD$100 billion per annum by 2025. Priority industries include wood and furniture; engineering; food and agriculture; chemicals; textiles; pharma and medical; printing and packaging; building materials; and metallurgical industries. These sectors comprised 23 percent of Egypt's 2019 import costs.
- Many of these industries continue to rely on imports of raw materials which could represent an opportunity for New Zealand exporters.
- Generally exports are holding strong. Egyptian government data indicate non-oil exports increased 20 percent to USD$19.35 billion in the period January-June 2022. This was comprised of chemical and fertiliser (22 percent of export revenues); building materials (19 percent); the food industry (11 percent); engineering industries and agricultural crop (each 10 percent); and ready-made garments (7 percent).

Foreign investment welcome

- Pushing for foreign investment continues to be an important tool in Egypt's efforts to promote growth. The General Authority for Investment and Free Zones (GAFI) has stated that Egypt is ranked first in Africa for Foreign Direct Investment (FDI) and second in the Arab World in 2020 (behind the United Arab Emirates).
- The Finance Ministry is increasing its export subsidy programme in its 2022-23 financial year budget to EGP6 billion, up from EGP4.2 billion in the previous budget.
- GAFI seeks to attract more FDI through two pillars:
  - Establishment of a nation-wide promotional strategy to attract investments; and
  - Removing challenges facing investors and enhancing coordination between ministries and automation of processes.
- Egypt's target sectors for investments are industry; agriculture; construction and building; transport and logistics; communications and information; education; healthcare; and tourism.
- GAFI's website provides an investment map that displays all available investment opportunities in the country.
- GAFI has provided the following guarantees investors, including:
  - Equal treatment of foreign and national investors;
  - Protection of the project against nationalisation, guardianship and seizure;
  - Right to transfer profit dividends and liquidation output; and
  - Exemption from registration in the importers register for importation of equipment, raw materials, machinery required for establishing expanding or operating the project.

- In an effort to attract international investment, other incentives include:
    - Tax incentives: Egypt provided tax exemptions amounting to 50 percent of investment costs in areas of Egypt designated as ‘A’ (areas in need of development) and 30 percent tax exemption on areas in area ‘B’ (areas GAFI considered did not need development). These tax exemptions applied against net profits made for the first seven years;
    - Customs incentives: including a 2 percent reduction in fixed customs fees on machinery and equipment required for the set up; and
    - Golden Licences: where foreign entities were investing in nationally strategic priority areas with high added value to the Egyptian economy, the Egyptian Cabinet could issue a ‘Golden Licence’. Applying for a golden licence needed to be arranged through the local Egyptian Embassy. Once a request was made a response was provided within 20 working days, if which a response was not received, the approval would be deemed automatic.
- Thirteen Investor Service Centres had been established around the country to act as a ‘one stop shop’ for investment services regarding company incorporation as well as during the business lifetime.
- GAFI is also responsible for the administration of free zones within Egypt to attract international FDI. These included Free Zones; Investment Zones and the Suez Canal Economic Zone:
    - Free Zones: were investment areas, managed by GAFI where investors are provided a full exemption from taxes and customs and can use Egyptian workers. Investors in Free Zones are required to export at least 80 percent of their production from Egypt. The Free Zones provide employment for 200,000 Egyptians and produce approximately USD $13.4b in capital per annum.
    - Investment Zones: are “integrated business clusters” allowing for simplified procedures and are already equipped with utilities that companies investing in Egypt can utilise. Developers in the clusters provide land and industrial units to the investor either through rent or sale.
    - Suez Canal Economic Zone: provides a full exemption from customs duties. As this Zone falls under Investment area A, it also provide a 50 percent tax deduction. The Suez Canal Economic Zone operated in an area of strategic importance for global trade routes, with more than 8% of global trade passing through the Suez. 18,000 container ships used the Canal last year alone.
- Additional incentives for investment in Egypt include human capital (with 60 percent of the population under the age of 30 and an unemployment rate in 2020 of 7.9 percent), strong infrastructure and network of roads and transportation (with an additional 7,000km of roading due to be completed in 2022 and a total of 11,530km of rail networks due for completion by 2030).
- Regional investment in Egypt is on the rise. Saudi Arabia announced in March it will purchase USD$10 billion in state assets from Egypt, and in June confirmed its intention to “lead” USD$30 billion worth of investments to Egypt. Several Saudi companies signed agreements that month to invest USD$7.7 billion in fields varying from renewables to pharmaceuticals. In August, Saudi Arabia bought USD$1.3 billion in shares in four Egyptian state-owned companies via the Saudi-Egyptian Industrial Investment Company which is wholly owned by the Saudi Sovereign Wealth Fund. Saudi Arabia’s Gulf neighbours have also pledged more than USD$22 billion of investment. There is speculation a Qatari investment worth USD$20 billion will soon be announced. This is in addition to the USD$5 billion Qatari investment confirmed in March.
- In the Suez Canal Economic Zone, Denmark’s AP Moller-Maersk, the world’s largest container line, will invest USD$500 million in the Suez Canal Container Terminal in the East Port Said Port to operate a new 1km container berth to raise the port’s capacity.

<u>A possible International Monetary Fund loan</u>

- Egypt is in the final stages of negotiating a loan from the International Monetary Fund (IMF) under the Extended Fund Facility. While it is unlikely to replenish Egypt's foreign reserves, it may generate investor confidence. IMF loans are not contingent on credit ratings and can be considered a ‘certificate of trust’ which could encourage foreign investors to invest in debt.
- A higher amount may require austerity measures, such as reducing subsidies, adopting a flexible exchange rate policy and letting the value of the Egyptian pound slide against the US dollar.

Russia-Ukraine war impact on Egypt

- Egypt's engagement with Russia and Ukraine for its food security and tourism has meant the Egyptian economy been impacted by the war. Egypt imports more wheat than any other country and prior to Russia's invasion Egypt secured 80 percent of its wheat imports from Ukraine and Russia. The recent limited resumption of Ukrainian grain exports has driven wheat prices down.
- In addition, Russia and Ukraine previously accounted for 30 percent of Egyptian tourism but this has been deflated by the conflict and sanctions. Tourism revenues decreased to USD$2.4 billion in January-March, down from almost USD$3 billion in the same period the year prior.

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