EGYPT

Highlights

- **Macro and socio-economic conditions continued to improve.** The economy grew at 3.3 per cent in fiscal year 2020-21 (slightly below the previous year's growth rate), unemployment fell, inflation is low, a primary fiscal surplus was achieved and foreign exchange reserves are accumulating.
- **The government extended some Covid-19 response measures and provided support to certain sectors.** The initiative to support the tourism sector was extended for an additional year until the end of 2021 and the Central Bank of Egypt (CBE) directed commercial banks to increase their financing for micro, small and medium-sized enterprises (MSMEs) from 20 to 25 per cent of their credit facilities portfolio.
- **The government successfully completed the International Monetary Fund (IMF) programme and launched its National Structural Reform Programme.** The latest phase of reforms focuses on supporting private-sector-led growth and job creation and will capitalise on reforms implemented since late 2016 under successive IMF-supported programmes.

Key priorities for 2022

- **Implementing the recently adopted medium-term revenue and debt strategies is essential to put debt on a sustainable, declining path.** This would lower the risks arising from high financing needs, notably the external part, and would create space for more productive spending on health and education.
- **Reforms to the role of the state in the economy would support competition and create a level playing field for private enterprises.** There is a need to develop a transparent state ownership policy and governance framework, and the state's role as regulator needs to be separated from that of operator to resolve potential conflicts of interest.
- **Integration into global value chains should be stepped up.** There is a need for a master plan for logistics, as well as for upgrading infrastructure and transport for better integration with other African economies. Reforms to customs and ports, including the use of automation, would facilitate and expedite exports.

Main macroeconomic indicators %

	2017	2018	2019	2020	2021
GDP growth	4.1	5.3	5.6	3.6	3.3
Inflation (average)	23.5	20.9	13.9	5.7	4.5
Government balance/GDP	-10.4	-9.4	-8.0	-7.9	-7.3
Current account balance/GDP	-6.1	-2.4	-3.6	-3.1	-4.7
Net FDI/GDP [neg. sign = inflows]	-3.3	-3.0	-2.6	-2.0	-1.4
External debt/GDP	33.4	37.0	36.0	34.0	n.a.
Gross reserves/GDP	13.0	17.4	14.5	10.2	n.a.
Credit to private sector/GDP	28.3	24.4	22.9	24.9	n.a.

Note: Fiscal year is July-June.

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Covid-19: macroeconomic implications

Economic growth slowed in fiscal year 2020-21. Growth in fiscal year 2020-21 was 3.3 per cent, following 3.6 per cent in fiscal year 2019-20. There were improvements in the wholesale and retail trade, agriculture, telecommunications and construction, but sluggish manufacturing activity, coupled with weak tourism, slowed the recovery. Meanwhile, inflation slowed to 5.0 per cent year-on-year in the first nine months of 2021. This is at the lower end of the CBE's target of 7.0 per cent +/- 200 basis points, despite the cumulative 400 basis points cut in the CBE's policy rate to 8.75 per cent between March and November 2020. As a result, Egypt now has one of the world's highest real interest rates, which helped attract portfolio flows and stabilise foreign exchange reserves, as other traditional sources of foreign exchange (tourism and Suez Canal receipts) slowed because of the Covid-19 pandemic. At the same time, unemployment declined to 7.3 per cent in the second quarter of 2021 from a peak of 9.6 per cent in the second quarter of 2020, but the labour participation rate, at 41.9 per cent, remains below its pre-Covid-19 pandemic level of 42.7 per cent.

The fiscal position improved, but the current account deficit widened. Revenues rose, driven by an improvement in tax collection, partly thanks to new electronic systems being put in place, in addition to tax policy and revenue administration measures and the start of the recovery from the pandemic. Expenditures also increased, mainly investment and interest payments. As a result, the deficit narrowed to 7.3 per cent of gross domestic product (GDP) in fiscal year 2020-21 and the primary surplus remained at 1.3 per cent of GDP. Meanwhile, public debt increased to 91.4 per cent of GDP. On the external side, the current account balance widened sharply in fiscal year 2020-21, to 4.7 per cent of GDP from 3.1 per cent in fiscal 2019-20. Tourism revenues continued to underperform, imports increased and exports remained stagnant. Moreover, foreign direct investment (FDI) inflows declined to US$ 5.2 billion but portfolio flows recorded a strong US$ 18.7 billion inflow, against a US$ 7.3 billion outflow a year earlier, as foreign investors' confidence picked up, lured by the high real interest rates. International reserves increased to US$ 40.8 billion in September 2021 and continue to cover comfortably more than eight months of imports.

The government is actively looking to diversify its funding sources and lower its interest payment bill. In September 2020 the government issued its maiden green bond, raising US$ 750 million to fund climate-friendly projects. The government then sold US$ 3.75 billion in Eurobonds in February 2021 amid strong demand. Egypt's first issue of sukuks (Islamic financial certificates) is expected to take place in the first half of 2022, after the president ratified a law in August 2021 enabling the issue of sharia-compliant securities. Moreover, Egypt's public debt is expected to be Euroclearable in 2022, making the country more accessible to foreign investors.

The pace of GDP recovery is expected to pick up to 4.9 per cent in fiscal year 2021-22. The boom in the telecommunications sector will continue to sustain growth, the falling unemployment rates will support consumption, and private investment and FDI flows will pick up. However, risks include slow uptake of vaccination, the weak outlook in the tourism sector in view of a probable global delay in the recovery of tourism, as well as the slowing momentum of major projects implemented in different parts of the country.

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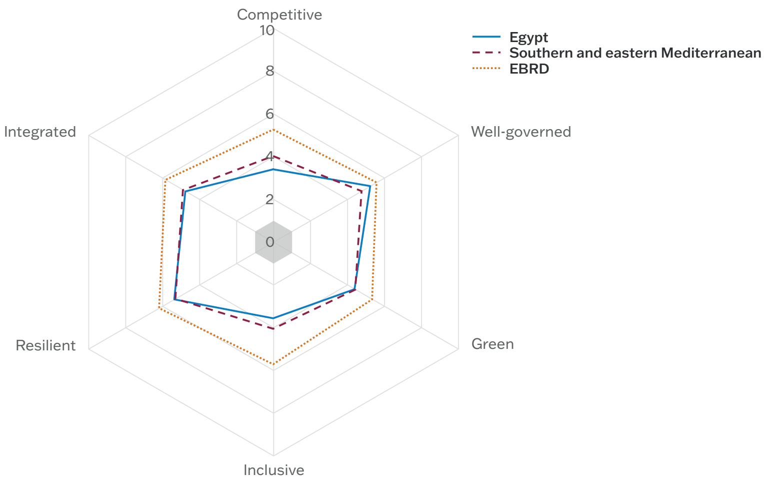
Policy response to Covid-19

Support for businesses affected by the Covid-19 pandemic has been maintained. The government decided to keep in place a package of financial support measures for businesses that were introduced in early 2020 in response to the Covid-19 pandemic. These include payments to cover the financing arrears of exporting companies, a scheme that is aimed at enabling such firms to continue meeting their current obligations. The government also extended its initiative to support the tourism sector for an additional year until the end of 2021. Banks are allowed to postpone dues and capitalise the interest rate on the principal without additional charges for a maximum period of three years. The government also extended the duration of the initiative for individuals working in the tourism sector, whereby banks can postpone their retail and mortgage loans due. Although the government's vaccination campaign was off to a slow start with only 3.7 per cent of the population fully vaccinated as of early September 2021, this had gone up to 10.5 per cent by early November 2021.

Assessment of transition qualities (1-10)



Structural reform developments

The government introduced a new phase of the National Structural Reform Programme. The new phase, announced in April 2021, focuses on structural reforms to support private-sector-led economic growth and capitalises on recent economic reforms. The three-year programme targets 6 reform pillars, 31 policies and objectives, and 100 procedural and legislative structural reforms. The authorities will continue to reform subsidies and move towards better-targeted social spending, increase investment in human capital, and focus on boosting certain sectors, including agriculture, manufacturing and information and communication technology (ICT). Other envisaged reforms include efforts to liberalise trade, improve competition and upgrade transport and logistics infrastructure.

Subsidy reforms have advanced. In July 2021 the government performed another round of electricity subsidy reforms, by hiking prices to consumers by 8 to 26 per cent, depending on consumption. Moreover, in August 2021 the president announced that the price of subsidised bread, fixed at 5 piasters (US$ 0.003) per loaf since 1988, would be increased and the savings directed to targeted social benefits, such as school meals. More details about the bread subsidy reform have yet to be announced. Meanwhile, Egypt remains the world's largest importer of wheat. Lastly, the government continued to rely on its automatic fuel indexation mechanism and fuel prices have increased three times in 2021, in line with global oil prices.

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The CBE has launched an EGP 100 billion (US$ 6.4 billion) mortgage finance initiative for low- and middle-income earners. Under the initiative, introduced in July 2021, banks and mortgage finance companies will offer loans at a declining interest rate of 3.0 per cent over a repayment period of up to 30 years. The programme aims to offer subsidised mortgages on houses valued at up to EGP 1.4 million (US$ 89,000), provided homebuyers make a 20 per cent down payment. Pensioners will also be eligible to take part in the programme.

Financing for small businesses is being expanded. In February 2021 the CBE directed commercial banks to raise financing for MSMEs to 25 per cent of their credit facilities portfolio, from 20 per cent previously. In particular, the central bank circular asked banks to direct 10 per cent of their net loan book to small enterprises. The CBE also allowed banks to finance micro and small-sized enterprises, with annual sales of less than EGP 20 million (US$ 1.3 million), without the requirement to submit their financial statements. This comes at a time when the government is increasing its focus on smaller firms and on the private sector to drive growth, create jobs and promote financial inclusion.

The government announced a minimum wage for workers in the private sector. The National Council for Wages confirmed in June 2021 that the minimum wage for private-sector employees would be set at EGP 2,400 (US$ 153) per month from January 2022. This is in line with the increase of 20 per cent in public-sector employees' wages that took effect in July 2021. This comes against a backdrop of low formal labour force participation (41.9 per cent in June 2021) and a significant portion of the private-sector workforce consisting of self-employed farmers, thus excluded from minimum wage rules. While this measure could increase purchasing power and boost private consumption, it could also force some smaller companies to lay off staff, further strengthening the informal sector. It is estimated that more than 95 per cent of companies in Egypt are MSMEs.

The Ministry of Finance continues to modernise and automate the tax management system. An electronic billing system was launched in November 2020 and, in January 2021, the ministry launched the first phase of the unified automated tax payment system for large and medium-sized companies and high-income self-employed taxpayers. It inaugurated taxpayer service offices, which provide businesses with a single online system for filing and paying taxes. The unified automated tax payment system will be implemented in four phases and is projected to be completed by the end of 2022.