

AFRICA RISK CONSULTING

Egypt Monthly Briefing October 2017

Egypt Summary 3 October 2017

The government will issue up to \$8 billion in Eurobonds by the first quarter of 2018 in a mixture of euro and dollar-denominated issuances. The government is looking to international markets to bridge the 2017/2018 financing gap. The Central Bank of Egypt (CBE) notes that foreign debt increased 42% year-on-year to \$79 billion in the 2016/2017 financial year compared to \$55.8 billion in 2015/2016. The International Monetary Fund (IMF) praises reform programme progress under the \$12 billion extended fund facility (EFF) but ordinary Egyptians complain they are yet to see its benefits. The government is to list state-owned petroleum services company Engineering for the Petroleum & Process Industries (Enppi) in the first quarter of 2018, marking the beginning of an initial public offering (IPO) pipeline expected to last 18 – 24 months.

Government prepares international debt issuance

The finance minister, **Amr El Garhy**, said on 20 September that the government will confirm details of planned bond issuances in early October. The government plans to use foreign debt issuances, cheaper than domestic borrowing, to bridge a \$10-12 billion financing gap for the 2017/2018 financial year.¹ The government is looking to build on the success of its \$4 billion Eurobond issuance in January, when the government exceeded its original target of \$2–2.5 billion after receiving an order book of \$13.5 billion.² While the government is yet to publish details of the planned issuance, which the cabinet approved on 28 September, it is expected to issue a 1-2 billion euro (€) (\$1.2 billion - \$2.4 billion) bond in November, and launch a \$4-8 billion issuance in February 2018.³

“The terms and scope of the new round of offerings has not been finalised, as there is still ongoing debate on who will oversee the next round and what the terms will be. No date has been set as the cabinet is still in discussions, but we expect November.”⁴

The government reportedly wants to issue euro-denominated Eurobonds to diversify its basket of currencies.⁵ Local media, however, reported on 18 September that the government has abandoned its planned issuance of yuan-denominated panda bonds.⁶

“Estimates suggest there will be combined USD/euro offerings. But I think it’s not just about raising money. Yes, there is a lack of fiscal planning that is clearly evident and debt is an issue, but the issuances are also about generating interest and positioning the country as an appealing prospect in the emerging market.”⁷

The cabinet must still confirm the size and timing of the planned bond issues, which it is expected to do in early October. El Garhy said on 28 September that, as with previous issuances, it will take place on the **Luxembourg** and **London Stock Exchanges**.⁸ It is unclear if the government plans to retain the issuers and arrangers used during issuances in the last financial year: **France-based BNP Paribas**

¹ Al Borsa, 19 Sept 2017.

² Daily News Egypt, 27 Jan 2017.

³ Al Borsa, 19 Sept 2017.

⁴ Source, economic journalist, Cairo

⁵ Al Borsa, 19 Sept 2017.

⁶ Al Borsa, 18 Sept 2017.

⁷ Source, economic journalist, Cairo

⁸ Al Borsa, 28 Sept 2017.

and **Natixis SA**, and **United States (US)**-based **JPMorgan Chase & Co** and **Citigroup Inc.** International media reported on 2 October that the government may only use **Europe**-based banks as transaction advisers.⁹

Institutional investor appetite for Egyptian debt is unclear. International ratings agency **Moody's Investor Services** presented a mixed picture in its annual report published on 19 September.¹⁰ Moody's said that Egypt's B3 credit ratings with a stable outlook reflect its large and diversified economy and strong reform momentum.¹¹ However, according to Moody's, Egypt's main constraint is the government's "very weak" government finances.¹² Despite the positive assessment of Egypt's reform process, Moody's noted that any signs of reform slowdown would jeopardise Egypt's stable outlook, but it depends on the form and speed of reversals and the implications for government finances.¹³ Moody's also noted that any renewed social and political instability or a material deterioration in the security situation could also lead to a negative rating movement.¹⁴ Despite Moody's cautious stance, **Bloomberg** reported on 27 September that, for the first time in over a year, EGP-denominated Egyptian bonds are not the highest yielding among the major emerging markets that it tracks.¹⁵

*"The average rate on the nation's debt plummeted about 400 basis points since July, dragging the yield below that of **Nigeria**, whose multiple exchange rates have perturbed investors."*¹⁶

However, investors strike a note of caution that much will depend on the performance of the Egyptian pound.

*"The indicators have been tipped as positive. We keep hearing that Egypt is on the investment hot list. But there is also fear that the Egyptian pound will take further dives in 2018, as the government's reserves are not stable. On the bond issuances, there is a perception that this is a 'quick fix' measure that they are pursuing as part of complying with the **International Monetary Fund's (IMF)** terms to generate more cash. They are focusing on cash opportunities instead of trying to make conditions more favorable to encourage investors to put money into the country long term. They need to tackle legal reforms and finally face Egypt's image problem head on to have tangible impact."*¹⁷

The perception that the bond issuances are distracting the government from more substantive economic reforms is prevalent.

*"The first round was oversubscribed and well received so the government is hoping to capitalise on that demand to again raise cash. There has been some criticism of a potential new round of Euro offerings as another sign the government is not committed to long term reform, both political and economic, that is required to ignite and sustain interest from foreign investors. Instead they are using this to buy more time, using short term solutions to plug holes, while not doing enough to generate jobs and growth. Critics point to a lack of infrastructure projects beyond the new capital (which is widely considered to be a fiasco), and ongoing issues with regulation and arbitration that continue to put off efforts to encourage new investment."*¹⁸

However, **Central Bank of Egypt (CBE)** data may reassure investors about the sustainability of the government's international debt burden, if not the pace of reform. The CBE published its **2016**

⁹ Reuters, 2 Oct 2017.

¹⁰ Moody's Investor Services, 19 Sept 2017.

¹¹ Moody's Investor Services, 19 Sept 2017.

¹² Moody's Investor Services, 19 Sept 2017.

¹³ Moody's Investor Services, 19 Sept 2017.

¹⁴ Moody's Investor Services, 19 Sept 2017.

¹⁵ Bloomberg, 27 Sept 2017.

¹⁶ Bloomberg, 27 Sept 2017.

¹⁷ Source, private fund manager, Cairo

¹⁸ Source, policy analyst, Cairo

Financial Stability Report on 28 September.¹⁹ The report notes that foreign debt increased 42% year-on-year to \$79 billion in the 2016/2017 financial year compared to \$55.8 billion in 2015/2016.²⁰ Institutional loans from international and regional lenders increased \$7.7 billion, treasuries and bonds \$5.5 billion, and short-term loans \$5.3 billion.²¹ The CBE says the total foreign debt figure “remains within safe levels by international standards, as it’s still below global net foreign reserves”.²²

The success of the January issuance meant that a return to the international markets this financial year was always likely. Investors have a long-term positive view of Egypt. Much, however, will depend on the government’s continued political will and capacity to deliver on sensitive economic restructuring.

IMF praises economic reform progress

The IMF published the first review of Egypt’s IMF-backed economic reform programme under the \$12 billion extended fund facility (EFF) on 26 September.²³ The IMF is broadly positive about Egypt’s progress, describing

“a good start at reining in public spending, boosting investor confidence, and addressing the surging inflation generated by the new policies.”²⁴

The IMF praised the transition to the flexible exchange rate, saying it has significantly curbed the parallel market and increased CBE reserves since its introduction in November 2016.²⁵

The IMF acknowledged that Egypt had missed primary fiscal balance and fuel subsidy targets at the end of June.²⁶ However, the IMF granted waivers for these missed targets “because of planned strong fiscal adjustments in the next two years.”²⁷ The IMF also backed the proposed amendment of the **Central Banking Act**, despite this remaining contentious in the banking sector (see *ARC Briefing Egypt July 2017*). The IMF noted that,

“Among other provisions the amendments envisage strengthening its governance structure, improving the recapitalisation and profit distribution rules, normalising the financial relationship with the government and commercial banks, enhancing transparency, and separating the emergency liquidity assistance and bank resolution frameworks.”²⁸

The IMF also praised the 2017/2018 budget as consistent both with the government’s medium-term objectives and the reform programme.²⁹ The IMF noted that,

“energy subsidy reform, wage restraint, and a new value-added tax have all contributed to reducing the fiscal deficit and helped free up space for social spending to support the poor.”³⁰

The IMF projects that, under the programme, the overall deficit will decrease to 1.8% of gross domestic product (GDP) in 2016/2017 and 0.4% in 2017/2018, compared to 3.4% in 2015/2016.³¹ In the current financial year, tax revenue will increase to 0.7% of GDP, the public-sector wage bill will decrease by 1% of GDP, and energy subsidies will decrease by 0.8% of GDP.³²

¹⁹ CBE 2016 Financial Stability Report, 28 Sept 2017.

²⁰ CBE 2016 Financial Stability Report, 28 Sept 2017.

²¹ CBE 2016 Financial Stability Report, 28 Sept 2017.

²² CBE 2016 Financial Stability Report, 28 Sept 2017.

²³ IMF Country Report No. 17/290, 26 Sept 2017.

²⁴ IMF Country Report No. 17/290, 26 Sept 2017.

²⁵ IMF Country Report No. 17/290, 26 Sept 2017.

²⁶ IMF Country Report No. 17/290, 26 Sept 2017.

²⁷ IMF Country Report No. 17/290, 26 Sept 2017.

²⁸ IMF Country Report No. 17/290, 26 Sept 2017.

²⁹ IMF Country Report No. 17/290, 26 Sept 2017.

³⁰ IMF Country Report No. 17/290, 26 Sept 2017.

³¹ IMF Country Report No. 17/290, 26 Sept 2017.

³² IMF Country Report No. 17/290, 26 Sept 2017.

The IMF warns that “*entrenched, high and persistent inflation*”³³ is the main economic headwind. This comes despite the **Central Agency for Public Mobilization and Statistics (CAPMAS)** publishing data on 10 September showing that annual urban headline inflation declined from 33% in July to 31.9% in August and the core inflation rate declined from 35.26% in July to 34.86% in August.³⁴ This led to suggestions by analysts that inflation may have peaked, and will continue to decline before the end of the calendar year if the appreciation of the Egyptian pound continues.³⁵ The CBE kept interest rates unchanged on 28 September.³⁶ Inflation has not yet reached a level that would encourage the CBE to decrease borrowing and lending costs. The CBE kept its overnight deposit rate at 18.75%, its overnight lending rate at 19.75%, and its discount rate at 19.25%.³⁷ The CBE monetary policy committee noted that economic conditions had improved in recent months, citing in particular the tourism, trade, natural gas, construction, and non-petroleum manufacturing sectors.³⁸ However, the CBE warned that “*the inflation outlook remains in line with achieving the inflation target.*”³⁹ The IMF expects inflation to decrease to “*slightly above*” 10% by the end of the 2017/2018 fiscal year, and then to single digits in 2019.⁴⁰ This compares to the finance ministry’s most recent projection of below 15% inflation by end of the current fiscal year.⁴¹ The IMF says the CBE will continue to closely monitor inflation rates and that monetary policy adjustments will depend on its assessment.⁴²

There is, however, popular concern that the public is not seeing the tangible benefits of the economic reform programme in their everyday lives.

*“Overall, the deficit is seeing movement, but there remain real questions about the competency of the current government to steer Egypt through these volatile times. President **Abdel Fattah Al-Sisi** [2014-present] has been repeatedly critiqued for his failure to retain the kind of people that could steer Egypt toward the right track and for instead hiring ‘yes men’... There is still not enough centered effort going into creating jobs, inflation is high, tourism is slumped, poverty is increasing and foreign investment is not where it should be.”⁴³*

The IMF’s praise for Egypt’s economic reform programme will facilitate the release of future financial support under the EFF. The IMF will probably disburse a third tranche, of \$2 billion, after a second programmatic review at the end of the year. However, the disconnect between Egypt’s macroeconomic performance, and the economic position and confidence of ordinary households is concerning. Tension over the issue will become increasingly acute as the May 2018 presidential election approaches. The government’s commitment to fiscal discipline may slide as it looks to shore up support for Sisi.

Enppi liberalisation to mark start of IPO pipeline

The investment minister, **Sahar Nasr**, confirmed on 25 September that the government plans to list state-owned petroleum services company **Engineering for the Petroleum & Process Industries (Enppi)** on the **Egyptian Exchange (EGX)** in the first quarter of 2018.⁴⁴ The government had originally hoped to list Enppi before the end of the year.⁴⁵ The listing of Enppi is particularly significant as it will provide a model that the government will look to replicate during its pipeline of initial public offerings (IPOs) of state-owned enterprises. The government aims to raise \$213m-267m

³³ IMF Country Report No. 17/290, , 26 Sept 2017.

³⁴ www.campas.gov.eg

³⁵ Enterprise, 10 Sept 2017.

³⁶ CBE statement, 28 Sept 2017.

³⁷ CBE statement, 28 Sept 2017.

³⁸ CBE statement, 28 Sept 2017.

³⁹ CBE statement, 28 Sept 2017.

⁴⁰ Reuters, 26 Sept 2017.

⁴¹ Reuters, 26 Sept 2017.

⁴² IMF Country Report No. 17/290, 26 Sept 2017.

⁴³ Source, policy analyst, Cairo

⁴⁴ Daily News Egypt, 25 Sept 2017.

⁴⁵ Zawya, 29 Mar 2017.

from the sale of a 24% stake in Enppi.⁴⁶ **CI Capital, Emirates NBD, and Jefferies International** are transaction advisers.⁴⁷ Nasr made the comment at a meeting of the government committee with oversight of the IPO pipeline. The committee includes chairman Nasr, El Garhy, the petroleum minister, **Tarek al-Molla**, and the public enterprise minister, **Ashraf El-Sharkawy**.⁴⁸ The prime minister, **Sherif Ismail**, established the committee on 14 September with the mandate to determine the schedule and pricing for the IPOs on the EGX, and ensure that government ministries are both prepared for the listing and the subsequent corporate restructuring and management of the companies.⁴⁹ The government plans to retain majority stakes in liberalised companies.⁵⁰ The committee committed to accelerating the listing of Enppi to expedite the remaining pipeline. After Enppi, the government will liberalise state-owned banks, starting with **Banque du Caire**. However, the other entities involved are less certain. Local media quoted anonymous officials on 18 September as saying that the government has abandoned the planned listing of the **Alexandria and Damietta Container and Cargo Handling Companies**.⁵¹ El Garhy said on 25 September that the first phase of the IPO programme will last between 18 and 24 months.⁵²

Egypt's oil and gas sectors are subject to payment arrears, policy delays, and political interference, all of which may deter investor response to the Enppi liberalisation. The IPO progress, and investor appetite, will provide a bellwether for the rest of the pipeline which is central to government efforts at economic streamlining.

Planner

May 2018 **Cairo (Egypt)** *Al Ahram*. Presidential election;

Early 2018 **Cairo (Egypt)** *Enterprise*. **El Garhy Steel Group** plans to offer 25% of its shares on the **Egyptian Exchange (EGX)**;

First Quarter 2018 **Cairo (Egypt)** *Reuters*. **Engineering for the Petroleum & Process Industries (Enppi)** IPO expected to begin 18-24 month government liberalisation pipeline;

Early 2018 **Cairo (Egypt)** *Reuters*. Proposed \$2-4 billion Eurobond issue;

End 2017 **(Egypt)** *World Oil*. **BP** expects offshore **Zohr** gas field to begin production;

Dec 2017 **(Egypt)** *IMF*. **Central Bank of Egypt (CBE)** expected to remove \$50,000 cash deposit cap on non-priority goods;

Dec 2017 **(Egypt)** *Youm7*. Investment ministry to publish investment map of 600 projects open to investment;

Nov 2017 **(Egypt)** *Al Borsa*. The **Egyptian-American Business Council** will meet delegation of **United States**-based companies;

9-15 Oct 2017 **(Egypt)** *Youm7*. Finance minister **Amr El Garhy** and deputy minister **Ahmed Kouchouk** to attend **World Bank** and **International Monetary Fund** fall meetings

Oct 2017 **Cairo (Egypt)** *Al Borsa*. Parliament to discuss revised **Capital Markets Act**;

⁴⁶ Zawya, 29 Mar 2017.

⁴⁷ Reuters, 25 Sept 2017.

⁴⁸ Daily News Egypt, 25 Sept 2017.

⁴⁹ Al Borsa, 14 Sept 2017.

⁵⁰ Daily News Egypt, 25 Sept 2017.

⁵¹ Al Mal, 18 Sept 2017.

⁵² Al Masry Al Youm, 25 Sept 2017.

Chronology

2 Oct 2017 **Cairo (Egypt)** *Press release*. The prime minister, **Sherif Ismail**, set out his government's legislative priorities as house of representatives begins third session;

1 Oct 2017 **(Egypt)** *Washington Post*. **United Nations** investigation reportedly concludes that **Egypt** purchased weapons from the **Democratic People's Republic of Korea**;

28 Sept 2017 **Cairo (Egypt)** *Reuters*. Cabinet approves planned \$7 billion Eurobond programme for the 2017/2018 financial year;

28 Sept 2017 **Cairo (Egypt)** *Press release*. The **Central Bank of Egypt (CBE)** keeps interest rates unchanged, holding its overnight deposit rate at 18.75%, its overnight lending rate at 19.75%, and its discount rate at 19.25%;

28 Sept 2017 **Cairo (Egypt)** *Press release*. CBE **2016 Financial Stability Report** shows that foreign debt increased 42% to \$79 billion in 2016/2017 financial year compared to \$55.8 billion in 2015/2016;

26 Sept 2017 **Cairo (Egypt)** *Press release*. The **International Monetary Fund (IMF)** is broadly positive about progress as it publishes first review of economic reform programme;

25 Sept 2017 **Cairo (Egypt)** *Daily News Egypt*. The investment minister, **Sahar Nasr**, confirms that the government plans to list state-owned petroleum services company **Engineering for the Petroleum & Process Industries (Enppi)** in the first quarter of 2018;

24 Sept 2017 **Cairo (Egypt)** *Al Mal*. Investment firm **BPE Partners** is looking for new investments in finance, energy and food manufacturing ahead of planned initial public offering;

20 Sept 2017 **Cairo (Egypt)** *Reuters*. **United States (US)** president **Donald Trump** (2017-present) says US is willing to reconsider cancelled or withheld aid;

20 Sept 2017 **Cairo (Egypt)** *Fin 24*. Egypt tops **Rand Merchant Bank's "Where to Invest in Africa"** report for 2018, for first time ever;

19 Sept 2017 **Cairo (Egypt)** *Al Borsa*. The government is expected to issue a 1- 2 billion euro (€) (\$1.2 billion - \$2.4 billion) bond in November, and a \$4 - \$8 billion issuance in February 2018;

19 Sept 2017 **(Egypt)** *Reuters*. President **Abdel Fattah Al-Sisi** (2014-present) criticises international states that fuel terrorism, in apparent reference to **Qatar**, in address to **United Nations General Assembly**;

17 Sept 2017 **Cairo (Egypt)** *Reuters*. Sisi says budget deficit was 9.5% of GDP in 2016/2017 financial year compared to 11.5% in 2015/2016;

16 Sept 2017 **Suez (Egypt)** *Al Shorouk*. The **Suez Canal Development Authority** says **Mercedes Benz** has agreed to resume car assembly, after suspension in 2015 due to foreign exchange crunch;

16 Sept 2017 **Cairo (Egypt)** *Reuters*. **BP** expects production from **Zohr** field to begin before end of year;

14 Sept 2017 **Cairo (Egypt)** *Bloomberg*. The finance minister, **Amr el Garhy**, says Egypt is

considering \$1.5 billion Eurobond in November;

14 Sept 2017 **Cairo (Egypt)** *Enterprise*. CBE governor **Tarek Amer** says the CBE will renew \$2.7 billion currency swap agreement with **China**, signed in October 2016, at end of the year;

14 Sept 2017 **Cairo (Egypt)** *Enterprise*. Amer says the CBE will send amended **Central Bank and Banking Act** to government for approval in October;

12 Sept 2017 **(Egypt)** *Enterprise*. **Government Accountability Office** criticises **Telecom Egypt** corporate governance in limited audit;

11 Sept 2017 **(Egypt)** *Press release*. **Central Agency for Public Mobilization and Statistics (CAPMAS)** data shows that urban headline inflation decreased from 33.0% in July to 31.9% in August;

11 Sept 2017 **Sinai (Egypt)** *Al Jazeera*. **Islamic State**-affiliated militants ambush security convoy, killing 18 police officers about 30km west of **El-Arish**;

9 Sept 2017 **(Egypt)** *Press release*. US senate foreign aid appropriations committee approves withholding 25% of \$1 billion military and economic aid to Egypt in 2018 financial year;

6-9 Sept 2017 **(Egypt)** *Al Masry Al Youm*. Egypt and **China** sign series of agreements during **2017 China-Arab States Expo**;

6 Sept 2017 **Cairo (Egypt)** *Al Mal*. Garhy says Egypt exceeded annual tax revenue target in 2016/2017 financial year by 33%, the first time it has ever done so;

6 Sept 2017 **Cairo (Egypt)** *Al Borsa*. CBE data shows international reserves reached \$36.1 billion in August;