

AFRICA RISK CONSULTING

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Egypt Summary 19 January 2023

The Egyptian pound plunges to its lowest level in recorded history on 11 January, reaching 30 pounds to the dollar as the Central Bank of Egypt (CBE) is forced to aggressively devalue the currency on the back of a loan agreement with the International Monetary Fund (IMF). Egypt's Sovereign Fund adds five military and state-owned companies to its pre-initial public offering (IPO) fund as the government renews efforts toward privatisation amid a financial crisis. The terms of the new bailout plan with the IMF also require the government to demonstrate a commitment to reducing the footprint of the military in the economy. Italy-based energy group Eni and United States-based energy company Chevron announce a large discovery in an offshore field of Egypt in the Eastern Mediterranean Sea on 15 January, as Egypt moves in to capitalise on the European Union's plans to reduce dependence on Russian energy.

Egyptian pound drops to record low as IMF imposes discipline

The **Egyptian** pound plunged to its lowest level in recorded history on 11 January, reaching 30 pounds to the dollar as the **Central Bank of Egypt** (CBE) was forced to aggressively devalue the currency on the back of a loan agreement with the **International Monetary Fund (IMF)**.¹ Egypt reached a staff-level \$3 billion funding deal with the lender on 27 October that would run over four years after months of protracted negotiations (*see ARC Briefing Nov 2022*).²

The sharp decline in the pound came a day after the IMF released a detailed breakdown of conditions tied to the extended credit facility arrangement.³ Chief among these was a commitment to a flexible exchange rate which was a point of contention throughout the negotiations as it would contribute to further inflation on food staples. This added to current levels of inflation would place further pressure on millions of Egyptians who are already below the poverty line and potentially lead to social unrest.⁴ The lender hinted at its scepticism regarding Egypt's ability to maintain the flexible exchange rate, noting it as a risk given the country's historical reluctance to cede control over the currency:

"Risks to the programme stem from the need to stay the course on difficult policy adjustments amidst heightened uncertainty and challenging headwinds in the outlook. The durability of the shift to a flexible exchange rate remains to be proven and the CBE may face political and social pressure to reverse course."⁵

Other key policy conditions specified in the arrangement include spending cuts in various areas. The government announced spending cuts for ministries on 10 January.⁶ As part of these cuts,

¹ Financial Times, 11 Jan 2023

² AFP, 27 Oct 2022.

³ IMF Country report, 10 Jan 2023

⁴ IMF Country report, 10 Jan 2023

⁵ IMF Country report, 10 Jan 2023

⁶ Reuters, 10 Jan 2023.

there will also be a pause on new national projects that require foreign currency, a key aspect given that Egypt has been criticised for incurring massive debt on national infrastructure projects including the **New Administrative Capital**, the **Dabaa** nuclear plant, and the world's longest monorail line.⁷ The sidelining of public sector investment, to reduce the government's participation in the economy via state-owned enterprises to "*level the playing field between public and private institutions*", was also a major sticking point in the agreement. The private sector has long complained that they are shut out given the unfair advantages afforded to state-run enterprises, which include a lack of tax oversight and free labour.⁸ There was also a series of overnight measures that will see detailed reporting on state budgets including those of state-owned companies. This will also apply to military-owned companies, who will be required to publish annual tax expenditures. Ending fuel subsidies to be in line with global markets will also be a priority, as will further reforms to the tax code.⁹

President **Abdel Fattah Al-Sisi** (2014-present) noted growing concern about the state of the economy in a public address on 6 January, but did little to allay fears of an all-out economic collapse, instead invoking the divine:

"I can see that people are worried and afraid. I won't say that this isn't justified ... we [the government] don't hide anything from you. Don't be afraid. God is with us. Do you think he will abandon us?"¹⁰

His comments come as Egyptians are facing skyrocketing inflation, with a 37.2% year-on-year rise in food alone, prompting the government to call for citizens to eat chicken feet instead of meat.¹¹ This promoted an outpouring of public anger on social media as the cost of poultry and eggs have soared in recent months after a halt on import financing caused huge backlogs of goods at ports, which meant animal feed producers have been unable to import soybeans which have forced prices up for poultry farmers, many of whom have either closed down or scaled their back their operations.¹²

Egypt watchers have suggested that official inflation figures should not be taken at face value as they do not accurately reflect the situation on the ground. **Steven Hanke**, a professor of applied economics at **United States (US)-based Johns Hopkins University** has suggested that the 21% inflation figure given by the **Central Agency for Public Mobilization and Statistics (CAPMAS)** the government statistics agency, was not accurate and was likely to be closer to 88%.¹³ Local sources agree that the government numbers do not reflect current prices in volatile staples like food.

⁷ Reuters, 10 Jan 2023.

⁸ IMF Country report, 10 Jan 2023.

⁹ Al Masry Al Youm, 12 Jan 2023.

¹⁰ Al Ahram, 7 Jan 2023.

¹¹ Daily News Egypt, 17 Jan 2023.

¹² The National, 11 Jan 2023.

¹³ Steven Hanke, Via Twitter, Jan 2023.



Multiple sources in **Cairo** agreed that inflation was set to continue to rise given that the adjustment of the Egyptian pound is not yet complete. **Farouk Soussa**, an economist with US-headquartered **Goldman Sachs** wrote to clients on 10 January that he expects further depreciation “to run before the supply-demand equilibrium in the FX market is restored”.¹⁴ Soussa further noted that the currency depreciation is a positive step given that the status of the currency has been a barrier to investors who were reluctant to invest while they saw the pound overvalued. Soussa believes that “the absence of large capital inflows from the **Gulf** and the central banks’ limited ability to provide foreign currency liquidity will lead to further depreciation of the pound”.¹⁵

For the business community, the measures imposed by the IMF are viewed as both positive and negative - on the one hand, there is a belief that fiscal discipline being imposed by the lender is important given that mega projects have drained Egypt’s cash reserves. There is also collective relief that curbs on imports have been lifted under the terms of the loan as these restrictions were causing pain for numerous industries that require imported goods, particularly manufacturing. However, there remains scepticism about the ability of the current leadership to create a viable model for growth going forward, considering the consistent failure of the government to achieve job creation or encourage foreign investment outside oil and gas. A chief executive officer (CEO) of a local company in Cairo told **Africa Risk Consulting Briefing (ARC Briefing)** that it is a precarious time for Egypt and that he believes the current government is ill-equipped to engage with Egypt’s challenges including the cost-of-living crisis and soaring debt levels.

¹⁴ Goldman Sachs, 10 Jan 2023.

¹⁵ Goldman Sachs, 10 Jan 2023.

"It's very difficult to impose further austerity on an already poor population. Meanwhile, Egypt's debt exposure is huge and at the same time the pound has lost half its value, which means the cost of imported items has become hugely difficult for businesses reliant on foreign inputs, such as the industrial sector, while a global downturn makes it harder for Egyptian business seeking global clients."¹⁶

It is the fourth time Egypt has sought the fund's help since 2013 with the country being the second biggest debtor to the IMF after Argentina.¹⁷ In total, it owes multilateral institutions \$52 billion.¹⁸ Negotiations with the IMF began in March, following **Russia's** invasion of **Ukraine**, which pushed Egypt's already fraught finances into further chaos.

State and military-owned companies added to initial public offering fund

Egypt's sovereign fund has added five military and state-owned companies to its pre-initial public offering (IPO) fund as the government moves to restart its IPO programme which has been repeatedly delayed.¹⁹ The renewed efforts toward privatisation come as the country is going through severe financial turmoil. Privatisation also formed a vital part of Egypt's arrangement with the IMF, requiring the government to demonstrate a commitment to reducing the footprint of the military in the economy which has grown sizably since the former defence minister assumed the presidency in 2014.

The military-owned bottled water company **Safi** and fuel retailer **Wataniya** are set to be included with **Misr Insurance**, Banque du Caire, and chemical company **Elab** in the IPO.²⁰ The fund will offer initial stake sales of 20-30% in these companies to investors, with full IPOs expected to take place in the years to come as market conditions improve.²¹

Several **Middle East North Africa (MENA)**-based sovereign wealth funds have expressed interest in acquiring shares in the military firms. **Ayman Soliman**, the head of the fund has said that the government plans to raise around \$6 billion through strategic stake sales via the pre-IPO fund.²² The government initially announced plans to sell state assets in 2018 saying that it would offer minority stakes in 23 state-owned companies, however, the programme has been repeatedly delayed due to weak markets and legal issues.²³ The government aimed to sell shares in up to 10 companies in 2022 after the instability of the **Covid-19** pandemic seemed to be passing, but the war in **Ukraine** then upended global markets. Thus far, they have managed to successfully sell stakes in the fintech company **e-market**, as well as secondary stakes in tobacco producer **Eastern Company** and **Abu Qir Fertilizers** since 2018.²⁴

Prime minister **Moustafa Madbouly** announced in May 2022 that government plans to more than double the private sector's contribution to the country's economy from 30% currently to 65% within the next three years. For business, pressure from the IMF as well as the urgency of the current crisis is positive in that it is expected to force some movement in reducing state participation in business but there is also recognition that this is a very precarious territory for the current president given his former position within the military. A former government official told ARC Briefing that Sisi has not only spent his entire life in the military but that the military is his only constituency given that he has eliminated all other centres of power in

¹⁶ Source, Company CEO, Cairo.

¹⁷ The Financial Times, 31 Oct 2022.

¹⁸ Middle East Eye, 26 Oct 2022.

¹⁹ Al Mal, 11 Jan 2023.

²⁰ Enterprise, 15 Jan 2023.

²¹ Al Mal, 11 Jan 2023.

²² Bloomberg Asharq, 5 June 2022.

²³ Al Arabiya, 8 May 2022.

²⁴ Enterprise, 8 May 2022.

Egyptian society. The official believes that while the military has always been a powerful force in Egypt, under Sisi's government it has become the only institution:

*"This presents a huge problem, given his spending habits and his penchant for very expensive homes and planes, the idea that he will then try to take away companies that the generals have created and profit from, or try to impose taxation on them is extremely problematic for the viability of his presidency."*²⁵

The official added that given that Sisi has also alienated the citizenry, unlike previous presidents who all maintained a clear social contract with citizens –which was bread and affordable living costs in return for silence:

*"Sisi's predecessor was ousted when that same contract began to erode. Fast forward to where we are now and you have unaffordable transport costs, electricity and fuel, food costs and the currency has fallen out of the sky. I can't see this lasting, someone will prevail, but will that be the generals or the president?"*²⁶

ENI and Chevron make large gas discovery off North Sinai coast

Italy-based energy group, **Eni**, and US-based energy company **Chevron** announced on 15 January a large discovery in an offshore field in the **Eastern Mediterranean Sea** which is estimated to hold 3.5 trillion cubic feet of resources.²⁷ The find was made at the **Nargis** offshore block off the coast of **North Sinai**, in which both companies hold a 45% stake, while state-owned **Tharwa Petroleum** holds a 10% interest.²⁸

This is Chevron's first discovery since it entered the Egyptian market in 2020. The energy giant has become significant in the region after it acquired fellow US company **Noble Energy** in 2020.²⁹ Noble, under Chevron, operates **Israel's** two biggest gas fields: **Tamar** and **Leviathan** and are developing the **Aphrodite field** in **Cyprus**.

Eni's most notable previous discovery in Egypt was the **Zohr** field in 2015, which allowed Egypt to become a net gas exporter.³⁰ The find comes as state-controlled Eni is looking for new energy sources to meet domestic demand as it aims to phase out dependence on imports from **Russia** by 2025.³¹ This was the second major gas discovery in Egypt in one week. **German**-based company **Wintershall Dea** and **Chevron** announced on 11 January a gas field discovery in Eastern **Damanhur** in the **Nile Delta**.³²

These discoveries come as Egypt is moving in to capitalise on European demand for gas to replace domestic supply after **European Union (EU)** nations pledged to move away from Russian hydrocarbons. Egypt's natural and liquefied gas exports increased to 7.8 billion between January and October 2022, ranking Egypt as the first gas exporter in the **Arab** world. Ninety percent of those exports went to markets in the EU.³³ Cementing its aspirations to be a regional energy hub, Egypt signed a nine-year agreement with the EU and Israel in mid-2022 to increase gas exports to Europe.³⁴

²⁵ Source, former government official, Cairo.

²⁶ Source, former government official, Cairo.

²⁷ Press release, 15 Jan 2023.

²⁸ Al Masry Al Youm, 16 Jan 2023.

²⁹ Enterprise, 5 Dec 2022.

³⁰ Al Ahram, 17 Jan 2023.

³¹ Al Ahram, 17 Jan 2023.

³² Reuters, 15 Jan 2023.

³³ Press statement, 11 Jan 2023.

³⁴ Al Aaswat, 28 Nov 2022.

³⁴ France24, 22 Jun 2022.

Planner

1 Feb 2023 **Cairo (Egypt)** *Enterprise*. **Capricorn Energy** will hold a vote on its merger with **Israel's NewMed**;

2 Feb 2023 **Al Mal (Egypt)** **Central Bank of Egypt's** Monetary Policy Committee to meet;

Chronology

17 Jan 2023 **Cairo (Egypt)** *Press release*. **Hassan Allam Holding** and the **United Kingdom's** export credit agency, **UK Export Finance**, have signed a memorandum of understanding (MoU) to increase cooperation in several projects across **Africa**;

17 Jan 2023 **Cairo (Egypt)** *Press release*. **Cairo** hosts the **Egyptian-Jordanian-Palestinian** summit;

16 Jan 2023 **Cairo (Egypt)** *Reuters*. Foreign investors transfer more than \$925m into the foreign exchange market in the three days after Egypt's currency sharply depreciated last week;

15 Jan 2023 **Cairo (Egypt)** *Al Mal*. **Italy** submits a proposal to the **Egyptian Electricity Transmission Company** to work on a joint \$ 2.8 billion electricity interconnection project with a capacity of 2.5-3 gigawatts (GW);

15 Jan 2023 **Cairo (Egypt)** *Reuters*. Foreign minister **Sameh Shoukry** meets with **Chinese** foreign minister **Qin Gang**;

15 Jan 2023 **Cairo (Egypt)** *The Washington Post*. Egyptian court hands down a life prison sentence to 38 people, including a self-exiled businessman, **Mahmoud Ali**, whose social media posts helped to spark anti-government protests;

15 Jan 2023 **Cairo (Egypt)** *Egypt Independent*. President **Abdel Fattah al-Sisi** directs the implementation of comprehensive development plans in the **Sinai Peninsula**, especially regarding land reclamation;

11 Jan 2023 **Cairo (Egypt)** *CAPMAS*. Figures released by state statistics agency **CAPMAS** showed annual urban inflation jumped to 21.3% in December, up from 18.7% the month before, driven by surging food costs;

11 Jan 2023 **Cairo (Egypt)** *World Bank*. **World Bank** revises its growth forecast for Egypt to 4.5% from a previous forecast of 4.8%;

11 Jan 2023 **Cairo (Egypt)** *Enterprise*. Government clears imports worth \$1.5 billion from ports in the first 10 days of January, putting the total value of goods cleared since 1 Dec at \$8.5 billion;

10 Jan 2023 **Cairo (Egypt)** *Press statement*. **United States** oil giant **ExxonMobil** acquires two offshore blocks in the **Nile Delta** and through its subsidiary, **ExxonMobil Egypt**, will operate both blocks and hold 100% interest;

8 Jan 2023 **Cairo (Egypt)** *Al Arabiya*. **National Bank of Egypt (NBE)** and **Banque Misr** secure loans worth a combined \$705m from global lenders to meet the local demand for hard currency as the government looks to clear a backlog of imports at ports;

27 Dec 2022 **Cairo (Egypt)** *Al Mal*. The price of gold soars to unprecedented highs as nervous savers seek refuge from a weakening currency and some companies export bullion to raise scarce dollars to fund imports;

22 Dec 2022 **Cairo (Egypt)** *Press statement*. **Central Bank of Egypt** hikes overnight interest rates by a greater-than-expected 300 basis points in a bid to defuse inflationary pressure;

16 Dec 2022 **Cairo (Egypt)** *IMF*. **International Monetary Fund** executive board approves a \$3 billion 46-month arrangement under the Extended Fund Facility;

15 Dec 2022 **Suez (Egypt)** *Xinhua*. **China**-based giant fibreglass producer **Jushi** inaugurates a new production line at its Egyptian factory;

13 Dec 2022 **Cairo (Egypt)** *Arab Finance*. **Central Agency for Public Mobilisation and Statistics** says the value of Egypt's exports to **East Asian** countries grew by 62.8% to \$6.6 billion in 2021, versus \$4.1 billion in 2020;

12 Dec 2022 **Cairo (Egypt)** *Arab Finance*. Telecommunications and information technology ministry signs a memorandum of understanding (MoU) with its **Zambian** counterpart for cooperation in several telecommunications and information technology fields.

About Africa Risk Consulting:

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Getting in touch

Please contact us by email info@africariskconsulting.com or call + 44 (0) 20 7078 4080

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