04/04/2019

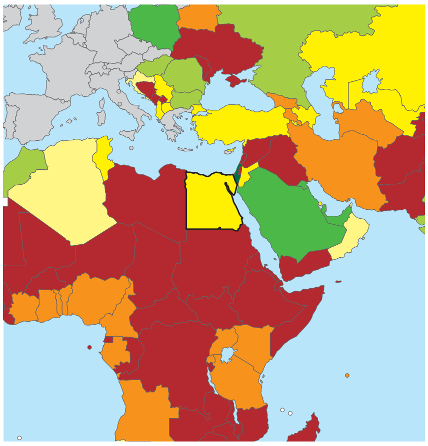
5/7 COUNTRY RISK CATEGORY

COUNTRY RISK ANALYSIS

Egypt

0 1 2 3 4 5 6 7

The country risk categories are arranged on a scale from 0 to 7.
The lower the figure, the better the country's creditworthiness.



CONTACT

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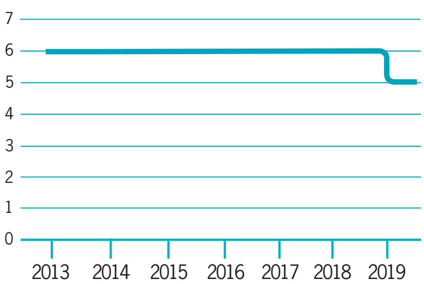
BASIC FACTS

Population:	95 million (2017)
GDP, nominally:	USD 237 billion (2017)
GDP/capita:	USD 2,495 (2017)

COUNTRY CLASSIFICATION HISTORY



Basic facts source: IMF WEO

Economic optimism thanks to reforms

Egypt's economic development has been positive over the past two years. Reforms implemented under the country's IMF programme have stabilised and boosted the economy, which was previously hampered by political uncertainty. A few years ago, Egypt suffered a shortage of foreign currency, while at the same time the central bank was forced to finance the state's record-high budget deficit. Today, most economic indicators point in the right direction. Growth is on the rise, the current account has been strengthened and inflation is on the way down.

The weaknesses in the economy is the public finances and the underdeveloped private sector. Fiscal policy austerity measures have been taken and the budget deficit and public debt are decreasing. The Government appears to be determined to continue strengthening state finances, also after the IMF programme expires in 2019. More uncertain is the Government's will and ability to strengthen the private sector. The economy is expected to continue to be dominated by the state and increasingly by the military.

EKN's guarantees include export transactions with Egypt within sectors such as transport, telecom and manufacturing. Payment experience has improved since 2017 due to increased access to foreign currency.

THE COUNTRY'S STRENGHTS AND WEAKNESSES

STRENGTHS

+ Financial support from multilateral lenders.
+ Low debt service ratio despite rising external debt.
+ EKN's good payment experience over the past decade.

WEAKNESSES

- Authoritarian leadership increases the risk of new violent events.
- Weak public finances.
- Weak business environment with a lack of financing and an unpredictable legal system.

SWEDISH EXPORT TO EGYPT, MSEK

	MSEK
2018	5 901
2017	6 297
2016	6 433
2015	6 153
2014	6 925

Source: The National Board of Trade

EKN:S EXPOSURE

	MSEK
Guarantees	2 874
Offers	1 674

EKN:S POLICY

EKN classifies Egypt in country risk class 5 out of 7, an assessment made in collaboration with the OECD. Egypt was upgraded in January 2019 as a result of favourable economic developments. EKN applies a normal risk assessment for sovereign risks as well as banking and corporate risks. Payment securities are a requirement for risks relating to other public purchasers, such as individual government ministries, municipalities and government agencies.

EKN:S EXPOSURE AND EXPERIENCE

During the period 2014-2018, EKN has issued guarantees in 280 transactions for Swedish companies that export to Egypt, totalling SEK 8 billion. EKN guarantees exports to Egypt within sectors such as transport, telecom and manufacturing. An investment guarantee dominates the commitment.

A shortage of hard currency led to arrears in several EKN-guaranteed transactions in 2015 and 2016. Payment experience has improved since 2017, thanks to the IMF programme and currency depreciation. Only a few arrears remain. The Paris Club claim, with renegotiated loans from the 1980s, will be fully repaid in 2021. Less than 1 SEK million remains to be paid.

EKN assesses the risk of negative impact on the environment and on human rights in all transactions. In some cases, information on environmental and social risks management indicates that local regulations on emissions to air and water are much less strict than international guidelines. The lack of free speech makes information gathering more difficult. Retaliation against dissidents and the authoritative leadership means that the actions of private actors is an important risk-reducing factor for transactions to the telecom sector.

WHAT MIGHT CAUSE A CHANGE IN THE COUTRY POLICY

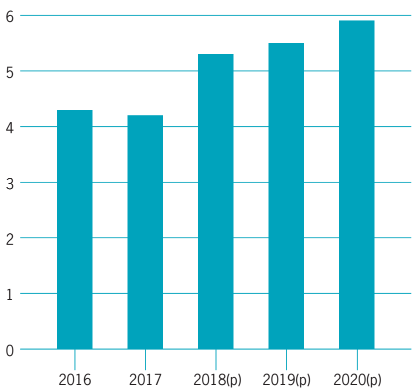
LESS RESTRICTIVE

- Structural reforms that strengthen the private sector.
- Fiscal policy reforms that further reduce the budget deficit.

MORE RESTRICTIVE

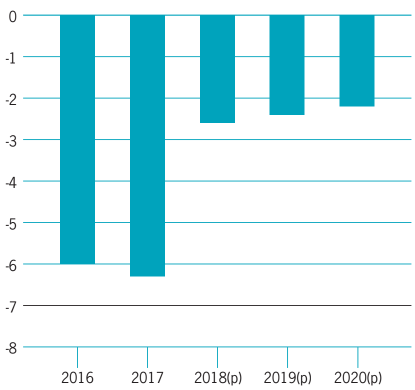
- New political instability would affect trade, investment and tourism.
- Non-existent reforms and a return to unsustainable fiscal policy after the IMF programme ends.

GDP-GROWTH (% PER ANNUM)



Source: IMF WEO 2019

CURRENT ACCOUNT (% OF GDP)



Source: IMF WEO 2019

COUNTRY ANALYSIS

BACKGROUND

With former army chief Abd al-Fattah al-Sisi as president, Egypt has regained the political stability and authoritarian rule that prevailed before the Arab Spring of 2011. The parliamentary election of 2015 was the last step in the military's surrender of power to a civilian government, even though the military retains great political and economic influence. As expected, Sisi won the 2018 presidential election, and without real competition. The challenger Moussa Mustafa Moussa had previously campaigned in support of Sisi. According to the National Election Commission, Sisi received 97 per cent of the votes. The lack of credible contenders and the low turnout created criticism from the opposition and human rights groups.

Political instability weakened the Egyptian economy in the years following the Arab Spring of 2011. Nine finance ministers came and went during this period. Flight of capital and the central bank's attempts to keep up the value of the Egyptian Pound eroded the international reserves between 2012 and 2016 and led to hard currency shortages in the economy. Payment delays occurred in several EKN-guaranteed transactions. Egypt was during this time dependent on financial support from individual Gulf countries.

After several years of speculation, Egypt entered into an IMF programme at the end of 2016. The Central Bank allowed the Egyptian Pound to float, which was a requirement from the IMF, and the currency depreciated by 50 per cent. The Pound has subsequently been stable due to the supply of foreign currency by the state-owned banks to the economy. The inflow of capital from the IMF and other multilateral lenders has increased the availability of hard currency and has created a functioning foreign exchange market. Remittances from Egyptians abroad have also increased since the depreciation.

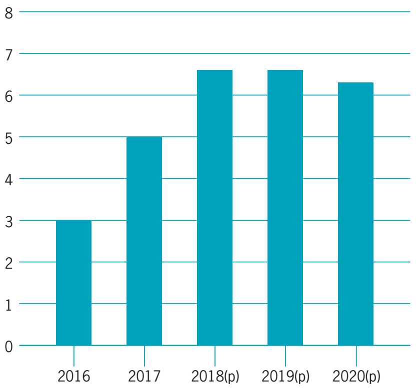
Inflation rose as a result of the weakened currency and reached a peak of 32 per cent in 2017. The weakening of the currency was accompanied by sharp interest rate hikes, which reduced inflation to below ten per cent at the beginning of 2019. Economic growth has remained between four and five per cent in recent years, somewhat subdued by a tighter fiscal and monetary policy.

RECENT DEVELOPMENTS

The Government's reform programme and the support from the IMF have led to macroeconomic stability and higher growth rates. Growth is expected to rise to 5.5 per cent in 2019. The main drivers are investments in the energy and construction sectors and favourable effects on export and tourism resulting from the devaluation. Private consumption has been hampered by high inflation, but is now expected to recover as inflation falls. Unemployment has fallen to less than ten per cent for the first time since 2011.

The Government has begun to take measures to address the weak public finances. Tax increases and reduced energy subsidies have

INTERNATIONAL RESERVES (MONTHS OF IMPORT)



Source: IMF Article IV 2019

yielded results and have led to the primary budget balance (the balance excluding public debt interest payments) being positive once again. The high public debt of 90 per cent of the GDP, and the interest costs it generates, mean that the budget deficit is still high at just over eight per cent of the GDP. A restrained fiscal policy is needed moving forward in order to make government finances sustainable in the long term.

The economic reforms that have been implemented have been well received by both the domestic industry and foreign investors. The capital inflow and foreign direct investment have increased significantly. Combined with multilateral support, the international reserves have doubled in two years and have risen to the highest level since 2011, corresponding to six months' import requirements. The current account deficit has fallen due to currency depreciation and an increased inflow of capital from tourism, remittances and exports.

Egypt has managed to attract foreign investment, but the government's international borrowing has accounted for a large part of the capital inflow. Bond loans and loans from the IMF and the World Bank have led to a doubling of the external debt over a couple of years, corresponding to 30 per cent of the GDP. The external debt service is still low as the loans are long-term and on favourable terms. Due to the reduction in the current account deficit and the fact that the state will make instalments on existing loans, the external debt is expected to slowly decrease in the future.

LONG-TERM DEVELOPMENT

Continued reforms are needed to make government finances sustainable in the long term. The IMF programme ends in 2019, but the Government appears to be determined to continue the reforms beyond this point, at least in terms of phasing out the energy subsidies. Tax increases and lower energy subsidies will improve government finances in the long term. Newly discovered gas deposits in the Mediterranean are being developed and will further strengthen government finances and the current account. The majority of public expenditure is interest payments, which account for 40 per cent of the total expenditure. With a falling government loan interest rate and an increased share of long-term external borrowing, interest costs are expected to decrease in the future.

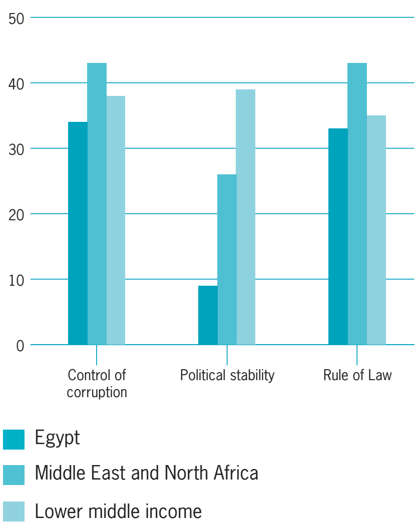
Significantly more uncertain is the Government's willingness and ability to proceed with structural reforms to strengthen the private sector. Egypt needs to attract foreign investment in sectors other than energy to strengthen the manufacturing industry and increase exports. Egypt's exports of goods in relation to the GDP have barely increased over the past 30 years, unlike most other emerging countries which have doubled their export share.

Structural reforms to improve competition, public procurement, governance of state-owned enterprises and land allocation are planned or have been implemented. However, this implementation has not been entirely successful. The privatisation of state-owned companies was announced in 2017, but was subsequently put on hold. The land reform that was implemented in 2016 with the purpose of making land available for industrial establishments has not been effective due to a lack of resources and instructions for how it should be realised. The challenges facing the private sector appear to persist. The economy is expected to continue to be dominated by the state and increasingly by the military.

The Egyptian Parliament is preparing a constitutional amendment that will allow Sisi to remain as president until 2030. With the current rules, Sisi's term will end in 2022. The constitutional amendment will by all accounts be voted through in Parliament and in the referendum which is then required. The power of the President, the military and the security service will then be strengthened at the expense of the judiciary and the Parliament. The constitutional amendment has received criticism from many quarters, but the military, allied Gulf countries and the United States are likely to support it, or at least not oppose it.

Although Sisi guarantees stability in the short term, there are significant social tensions that need to be dealt with to avoid new eruptions of unrest sooner or later. Poverty has increased since public austerity measures began in 2016. The middle class is also under pressure due to reduced purchasing power. Despite a forecast annual growth rate of around six per cent in the medium term, it will take many years before the majority of Egyptians experience a noticeable improvement in their standard of living.

BUSINESS ENVIRONMENT



Ranking from 0 (worst) to 100 (best)

Source: The World Bank

BUSINESS ENVIRONMENT

Reforms in the early 2000s have created a robust banking sector that has been able to withstand the difficult economic conditions following the 2011 revolution. The banks are expected to remain well-funded thanks to their large customer deposits and remittances from Egyptians working abroad. Capital adequacy is acceptable and provisions for non-performing loans are high. The Egyptian banking sector's lending to the private sector is minimal and most Egyptians do not have a bank account.

For many years, the banks' main function has been to finance the state's budget deficit instead of lending to the private sector. The exposure to the Egyptian state is the largest credit risk for the banking system and links the banks' creditworthiness to the state. Loan concentration is high, which reflects the banks' focus on well-established large companies. Small and medium-sized enterprises with a high demand for credit are instead referred to the informal credit market.

Egypt's economy is dominated by state-owned companies and the public sector. The military has significant financial interests and is expected to increase its influence further after the constitutional amendments have been voted through. The military's expansion is detrimental to the private sector, which cannot compete with military-owned companies that enjoy cheap or free energy, land and labour. The state's dependence on the banking sector to finance the budget deficit has superseded the private sector and has reduced its access to financing. The lack of financing has led to underinvestment, especially in infrastructure.

Bureaucracy and corruption cause difficulties for creditors in enforcing court judgments and recovery in the case of bankruptcies. The rule of law is inadequate, and the outcome of legal proceedings is unpredictable. However, some progress has been made in recent years on new legislation. A new investment law has been approved and a new bankruptcy law is expected to be approved shortly. According to the World Bank's classification, Egypt's business environment is ranked 120 out of 190 countries, which is after comparable countries in the region such as Tunisia, Morocco and Jordan.