FUNDAMENTALS

EGYPT MPC UPDATE: HOLD AMIDST EMERGING CONCERNS

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IN BRIEF

- The Central Bank of Egypt retained the deposit rate at 19.25% in its November 2023 MPC meeting. The rate decision was in line with consensus amidst a slight uptick in September 2023 inflation print.
- Favourable base effects notwithstanding, recent price adjustments on fuel products and increased excise tax on tobacco implies sticky inflation in the near-term. The emergence of parallel FX rate and negative spillover effects from a prolonged Israeli-Gaza escalation tees up external sector risk, and inflation outlook.
- With the December 2023 polls on the horizon, the delayed combined first and second IMF reviews under the current USD 3.0bn programme are likely to be finalized in early 1Q2024, to enable the Fund and the authorities map out applicable quantitative performance criteria and indicative targets for the current FY24.
- The volatility in the USD-denominated Eurobond markets has seen Egypt raise USD 1.0bn-equivalent in non-USD denominated bonds. Egypt raised CNY 3.5bn (USD 500.0mn) in its debut 3.5% 2025 panda bond in October 2023 and followed up last week with JPY 75bn (USD 500.0mn) 1.5% 2027 samurai bond via private placement.
- Considering the emerging risks across its eastern border, the USD 3.0bn IMF financing seems inadequate to cover financing needs in the medium term. Given Egypt's programme financing size equivalent to 115.4% of its quota, there is a likelihood of upscaling against the backdrop of IMF's recent proposed across-the-board 50.0% increase in quota limit from next month.
- Since early October 2023, all the three major credit rating agencies downgraded Egypt's long-term ratings, with Moody's Caa1 a notch lower on comparable basis. Nevertheless, Moody's stable outlook reflects continued external financial support more so from the Gulf Cooperation Council (GCC) countries.

Hold, in line with expectations

The Central Bank of Egypt retained the deposit rate at 19.25% in its November 2023 MPC meeting. The rate decision was in line with consensus, amidst a slight uptick in the September 2023 inflation print. September inflation edged up 60bps to 38.0% y/y, in part by the flare up in food inflation (73.6% y/y). Despite the uptick in headline inflation, the moderation in core inflation for the third consecutive month assuaged the monetary authorities' inflation concern. Favourable base effects notwithstanding, recent price adjustments on fuel products and increased excise tax on tobacco implies sticky inflation in the near-term. The emergence of parallel FX rate and negative spillover effects from a prolonged Israeli-Gaza escalation tees up external sector risk, and inflation outlook.

Wider net foreign liabilities amplify parallel market risk

Net foreign liabilities in the banking system (CBE and banks) widened to USD 26.8bn in September 2023 (+USD 845.3mn m/m). Net foreign liabilities for banks at USD 16.4bn, although improving from recent lows of USD 17.2bn, has amplified concerns of parallel rate. The Egyptian Pound in the forward markets telegraphs a 7.8% premium over the current spot levels of (30.89/USD). With the upcoming presidential elections slated for 10 – 12 December 2023, we do not foresee currency adjustment before the elections. This is likely to exacerbate the non-clearance of FX backlog, prolonging the parallel market.

Delayed IMF reviews expected in 1Q2024; FY24 external financing on track

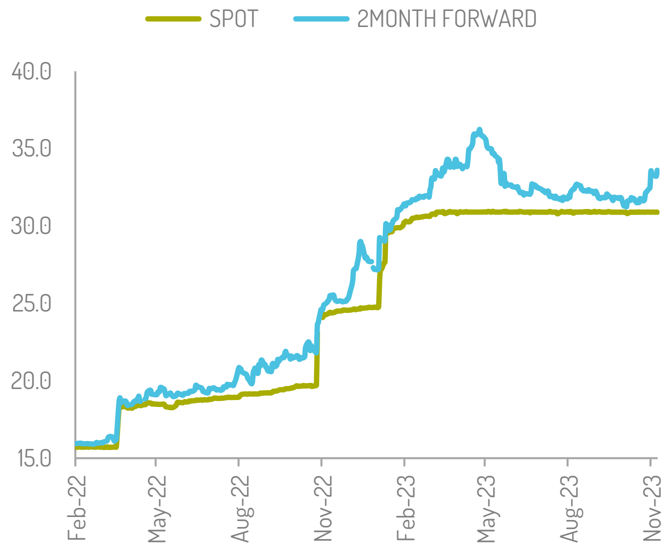
With the December 2023 polls on the horizon, the delayed combined first and second IMF reviews under the current USD 3.0bn program are likely to be finalized early 1Q2024, to enable the Fund and the authorities map out applicable quantitative performance criteria and indicative targets for the current FY24. The slow pace in the privatization process coupled with a less-credible exchange rate flexibility pose downside risks in the program outturn. Nonetheless, the FY23 budget shows a positive outturn for the quantitative performance criteria and indicative targets in the months of December 2022 and June 2023.

Notwithstanding the delayed IMF reviews, Egypt is on track to mobilize USD 1.5bn by the end of the year. The volatility in the USD-denominated Eurobond markets has seen Egypt raise USD 1.0bn-equivalent in non-USD denominated bonds. Egypt raised CNY 3.5bn (USD 500.0mn) in its debut 3.5% 2025 panda bond in October 2023 and followed up last week with JPY 75bn (USD 500.0mn) 1.5% 2027 samurai bond via private placement. With a rising risk premium attached on Egyptian assets, the success of the panda and samurai bonds was pegged on the guarantees given by multilateral lenders. Progress with the IMF program review should somewhat lower the risk premium, in our view. Considering the emerging risks across its eastern border, the USD 3.0bn IMF financing seems inadequate to cover financing needs in the medium term. Given Egypt's program financing size equivalent to 115.4% of its quota, there is a likelihood of upscaling against the backdrop of IMF's recent proposed across-the-board 50.0% increase in quota limit from next month.

Downgrades; Rating Agencies reading the same script

Since early October 2023, all the three major credit rating agencies downgraded Egypt's long-term ratings, with Moody's Caa1 a notch lower on comparable basis. Moody's flagged the nation's worsening debt affordability trend and constrained policy options as the negative catalysts underlying its downgrade. Nevertheless, Moody's stable outlook reflects continued external financial support more so from the Gulf Cooperation Council (GCC) countries. News flow suggests that Egypt will obtain new USD 5.0bn deposits from Saudi Arabia and the United Arab Emirates (UAE) to shore up its FX reserves.

EGYPTIAN POUND AGAINST THE US DOLLAR



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