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Not as Severe as Expected but All Eyes on the Scars

The economy battled COVID-19, backed by resilient remittances and lower global commodity prices: In line with our expectations, the effect of COVID-19 on Egypt's hydrocarbon-trade balance was relatively favorable given the significant fall in oil prices in Q4 FY20 and subdued import demand. Meanwhile, the service balance (mainly tourism) fell under the pressure of lockdown measures and travel ban, posting its worst performance since the terrorist attack on the Russian airplane in 2015. However, workers' remittances defied expectations and remained resilient.

CAD widened sharply as the significant fall in tourism was too large to be offset: Egypt's current account deficit (CAD) surged to USD3.8bn in Q4 FY20 from USD1.1bn a year earlier. Except for workers' remittances, Q4 FY20 figures reflected the impact of the economic fallout of COVID-19 on the external balance, as follows:

(1) **Trade deficit widened slightly** by 1.4% y/y on the back of a 28% y/y fall in exports that outpaced the 13% fall in imports.

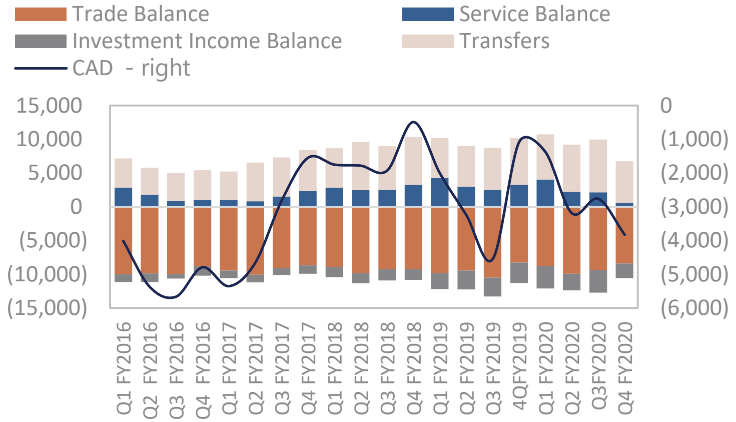
(2) **The effect of the crisis on the trade balance was mixed.** Hydrocarbon trade balance registered a slightly higher surplus of USD352mn vs. a surplus of USD303mn a year earlier. The improvement in hydrocarbon trade balance was mainly due to the fall in oil prices and lower demand for fuel imports due to the lockdown measures. The Egyptian government resumed fuel products imports in July 2020 after suspending imports during most of Q4 FY20 when Egypt became self-sufficient. Meanwhile, non-hydrocarbon trade deficit widened by 2% y/y due to an annual drop of 6% in exports and a slight fall in imports of only 0.8%.

(3) **Service surplus fell sharply** by 83% y/y to only USD550mn. This significant slippage was mainly driven by c.90% weaker tourism revenues which registered only USD305mn. This came as the country received no tourists at all in April, according to CAMPAS. Also, Suez Canal revenues declined by 7.7% y/y.

(4) **The effect on workers' remittances is still lagging.** Having grown by 4% y/y to USD6.2bn, workers' remittances are expected to slip in FY21.

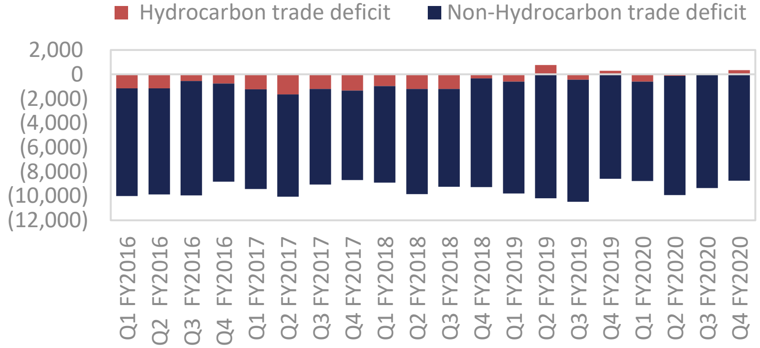
Despite the fall in net FDI and portfolio investment, the financial account net inflows increased, thanks to net borrowings: The financial account registered a net inflow of USD1.35bn, up from USD1.25bn a year earlier. However, foreign direct investment (FDI) dropped by 11 y/y to USD1.5bn in Q4 FY20, and foreign portfolio investment (PFI) fell sharply by 80% to just USD637mn. Egypt has faced a fierce capital outflow bout since mid-March, losing north of USD17bn from the local debt market. However, the rebound in carry trade inflows was faster than expected as the country started to receive capital inflows in June. The Egyptian government had to engage with the IMF through its rapid financing instrument (RFI) (USD2.8bn, disbursed in June 2020) to address the impact of the COVID-19 crisis on the country's external position. Moreover, Egypt was granted a USD5.2bn SBA credit facility in June 2020. Yet, the disbursement of the first tranche of USD2bn was only received in July 2020.

Figure 1: Transfer balance alleviated the effect of the COVID-19 on CAD (USDmn)



Source: CBE, Prime Research.

Figure 2: Hydrocarbon trade balance is in surplus for first time in 12 months (USDmn)



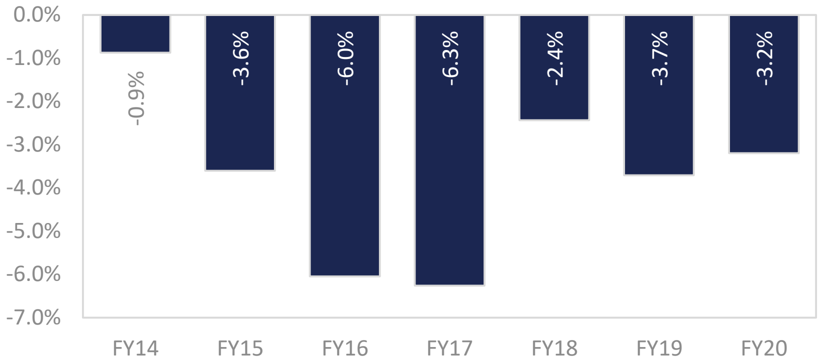
Source: CBE, Prime Research.

How Q4 FY20 affected the overall performance of CAD in FY20

CAD	• CAD ended the year at USD11.2bn (3.2% of GDP), slightly up from USD10.9bn (3.7% of GDP) in FY19. This came well below our expectations of USD15bn (3.9% of GDP). The larger-than-expected workers' remittances in Q4 FY20, coupled with a significant improvement in hydrocarbon trade balance and the performance of the first quarters of the year, eased the pressures of the COVID-19 turmoil on CAD. • Looking ahead, the unprecedented health crisis should leave a long-lasting effect on CAD, given the long road to recovery in the tourism sector and workers' remittances given that most GCC countries have been bracing for a slowdown, and they were speeding up their labor market nationalization policies.
Trade balance	• Trade deficit came in line with our expectations, falling by 4% y/y to USD36.5bn (vs. our projections of USD36.6bn) due to a 7.4% fall in exports and a 5.5% fall in imports. The fall in imports was triggered by a 23% drop in hydrocarbon imports, while non-hydrocarbon imports fell by only 2%. • The decline in exports was also triggered by the fall in hydrocarbon exports, which fell by 27% on the back of the slump in global natural gas prices. Meanwhile, the 6% annual growth in non-hydrocarbon export was not sufficient to offset the effect of the fall in hydrocarbon exports on overall exports.
Tourism	• The sudden halt in tourism in Q4 FY20 drove overall tourism revenues to fall by 22% in FY20, registering just USD9.86bn. • The robust performance, however, in the first two quarters of the year eased the effect of the pandemic crisis on the overall annual figure. • We expect tourism to rebound by H2 FY21 as the sentiment towards overseas travel remains weak until a vaccine is made available.
Workers' remittances	• Workers' remittances posted a historical record of USD27.8bn in FY20, up from USD25.2bn in FY19. • However, as the pandemic cast its shadows on global employment, we expect workers' remittances to witness a significant decline in the upcoming years due to increased employment nationalization efforts in GCC countries.
Investment income deficit	• Investment income deficit increased slightly in FY20 by 3% to USD11.4bn. • Looking ahead, we expect investment income deficit to accelerate further due to the increase in interest payment on external debt. The COVID-19 crisis has triggered a massive wave of external borrowing as the country managed to secure external financing needs. Such facilities were used to offset the effect of COVID-19 on FX liquidity, securing USD7.8bn from the IMF funding package (USD4.8bn of which has already been disbursed) in addition to USD5bn of Eurobonds by end of May 2020.

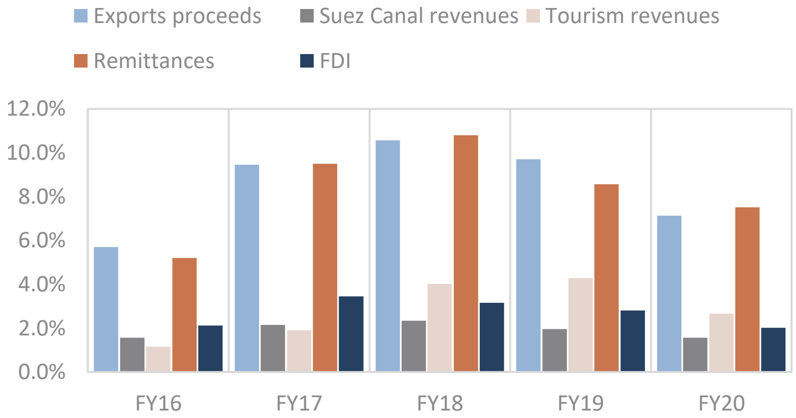
Source: Prime Research .

Figure 3: CAD as a percentage of GDP is still falling despite the crisis



Source: CBE, Prime Research.

Figure 4: FX revenues as a percentage of GDP shows the significant importance of workers' remittances



Source: CBE, Prime Research.

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