



Egyptian eruptions

Omni Bridgeway examines the trade and economic implications of the recent protests in Egypt.

Just as the dust had settled and the debris had been cleared from Tahrir Square, the media's spotlight switched from Egypt to Libya. Despite ongoing protests in Libya, Yemen and elsewhere, there is a growing sense that the Arab world's spring of 2011 might turn out like the Prague Spring of 1968 – that this might not be the Arab world's 1989 but rather another 1848.

Nevertheless, having sat atop North Africa's largest economy for 30 years, the toppling of President Hosni Mubarak on 11 February was a seismic event that continues to cause shockwaves. Existing investors will be well aware of them, but what factors should prospective investors in Egypt consider? Trade disruption and its impact on economic and debt fundamentals will be considered, before an examination of the short-, medium- and long-term challenges.

In the short-term, trade has been significantly affected. One immediate consequence of the protests that started on 25 January was the sudden exodus of tourists. Companies such as Thomas Cook lost £15m from cancelled holidays and £5m as a result of repatriation costs – for Egypt and Tunisia combined. The Egyptian economy, meanwhile, itself lost between \$30m and \$40m in tourism revenues each day during the revolution. Western governments have lifted travel warnings, but the slow return of tourists will depend largely on continued stability.

Wider disruption

More significant than the dearth of tourists has been the general disruption to labour and trade infrastructure. With arson, curfews, demonstrations and looting, security concerns prompted many businesses to close including, for example, subsidiaries of Nestlé and Unilever, and several Indian multinationals such as IT services vendor Wipro and pharmaceuticals company Ranbaxy.

Some of these Indian-owned subsidiaries – for example, Tata Motors and Essar Global – acted as regional offices, so the impact on their business will be magnified. Although fears of a deepening descent into lawlessness have so far proved overblown, petty crime is on the increase, as is unemployment, as businesses cut payrolls in response to reduced demand.



While traffic through the Suez Canal – one of Egypt's key earners – was not affected, cargo operations at Egypt's Alexandria, Damietta, Ein Sokhna and Port Said container ports came to a standstill and are only now beginning to deal with the backlog. For example, shipping giants AP Møller-Maersk suspended some operations, while CMA CGM and Hanjin Shipping re-routed vessels, with ports like Malta benefitting temporarily.

Some traders took another approach – ordering vessels to circle close to port until the turmoil had passed in order to avoid non-payment risks. However, back on dry land, bank closures and communications outages thwarted both the aforementioned approach as well as most efforts to import or export. Egypt's woes have increased counterparty risk far and wide: For example, Egypt is the world's biggest wheat importer, and imports 74% of Lebanon's apple crop; Turkey, too, stands to lose in the short-term, as the biggest regional exporter to Egypt.

Also, many of Egypt's listed companies, such as Ezz Steel and Palm Hills Development, were not only affected economically but also politically: with close ties to Mubarak's regime, ongoing corruption investigations are partly to blame for the delay in re-opening the Egyptian Exchange. This has affected capital market fund-raising and trading alike. Counterparties involved with the estimated \$40bn-\$70bn of assets allegedly embezzled by the Mubarak regime will also be affected, and international efforts to identify and freeze Mubarak's properties and cash are afoot.

These short-term trade disruptions will also affect Egypt's macroeconomic outlook. Delaying the re-opening of banks may have averted bank runs and various measures, such as higher daily minimum cash withdrawal limits and longer clearance periods for bank transfers, may have ensured minimal capital flight. Nevertheless, currency, current account, fiscal, growth and inflationary concerns remain.

Exchange controls

Political turmoil has both weakened the Egyptian pound and stemmed capital inflows, the latter of which is reinforcing the former. The Central Bank of Egypt (CBE) may have to sell foreign reserves to support its currency,

but its likely imposition of controls on access to foreign exchange may also resuscitate the black market in foreign currency.

With a depreciating currency and increasing commodity prices, inflation is expected to accelerate. The CBE faces a significant challenge in balancing its fight against inflation and the government's desire for growth to not be stifled by excessive interest rate rises.

Growth, between 2005 and 2008, was driven by strong, investor-focused reforms and economic liberalisation – despite their unpopularity with the people at large. However, the ministers responsible for such reforms have now been tarred with the brush of the last regime. The current

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and any incoming government are likely to focus on stabilisation initially and only return to the liberalisation agenda gradually, from perhaps 2013 onwards. Even then, widespread non-patronage-based privatisation is unlikely.

The Economist Intelligence Unit expects the current account to remain in deficit until 2014 and the government's fiscal deficit – averaging 8% of GDP over the last decade – to deepen to 12.1% of GDP in the current fiscal year. This deficit will be exacerbated by increased spending on government wages, subsidies and public works projects.

External debt is estimated at \$30.8bn, or 14% of GDP. Yields have increased sharply: at a CBE auction of Treasury bills on 27 February, the average yield increased to 11.097% and 12.162% for three- and nine-month bills respectively. Recent studies suggest that the greater a sovereign's democratic credentials, the lower its yield. Egypt's debt sustainability could thus depend, in part, upon how successfully the military administers the new parliamentary and presidential elections. If the elections are held too early for opposition groups to mobilise, the existing, 'ancient regime' linked parties will benefit and voters will become dissatisfied. In light of this, Moody's recently cut Egypt's rating from Ba2 to Ba3, citing that

continuing anxiety about the transition was having an adverse impact on Egypt's fiscal position and general economic performance.

Egypt's debt situation also, in part, depends upon the charm of Samir Radwan. As the new finance minister, Radwan has asked the EU to write-off its loans and provide unconditional grants, and has asked others, such as Switzerland, to increase foreign direct investment. The African Development Bank, the EBRD, IMF and the US have all offered aid of varying levels of assistance and conditionality.

Again, how strongly the military and incoming government affirm their democratic credentials will affect how much debt relief and aid are provided. For example, if the army failed to deliver on its promises, the US might consider suspending its annual \$1.3bn grant to Egypt, which helps finance military procurement, and might even consider an arms embargo. Such arms might actually be needed. Although future conflict with Israel remains unlikely, potential geopolitical tensions could arise in the short-term from the growing humanitarian crisis on Egypt's border with Libya, and in the long-run from the incoming regional regime controlling use of the vital Nile River.

After the uncertainty and history-making of the last two months, one would hope systems would get back online, backlogs would clear and Egypt would return to business as usual. Irrespective of whether the forthcoming elections pass smoothly, an Egyptian sovereign default is highly unlikely, as is a recurrence of the trade disruptions of the type just experienced.

The incoming government must stabilise the economy swiftly and return – despite the population's wariness of economic pain – to a reform agenda of improving labour market participation and removing rigid economic structures that actually yields results. If the incoming government does not do this, then the same social and economic demands that underscored the Tahrir Square protests may well be heard again.

We invite holders of both defaulted trade debts and rendered arbitral awards relating to Egypt to contact us for advice.

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Emerging market debt pricing

Latin America & Caribbean Hyper-Exotics

Country / Issue	Price Range	
Cuba / Trade	2.000%	4.000%
Cuba / Loans	5.000%	10.000%
Suriname / Loans, Trade	14.000%	18.000%

Eastern Europe Hyper-Exotics

Country / Issue	Price Range	
Azerbaijan / Trade	18.000%	23.000%
Bosnia / Trade	36.000%	41.000%
Georgia / Trade	11.000%	15.000%
Serbia / Trade	44.000%	54.000%
Turkmenistan / Trade	23.000%	31.000%
Ukraine / Trade	20.000%	27.000%
Uzbekistan / Trade	20.000%	24.000%

Asia Hyper-Exotics

Country / Issue	Price Range	
Mongolia / Trade	22.000%	30.000%
North Korea / Loans, Certificates	9.000%	12.000%

Africa Hyper-Exotics

Country / Issue	Price Range	
Angola / Trade	50.000%	55.000%
Angola / Loans	55.000%	59.000%
Cameroon / Trade (non-HIPC)	14.000%	20.000%
Congo / Trade (non-HIPC)	22.000%	26.000%
DR Congo / Loans, Trade (non-HIPC)	16.000%	20.000%
Ghana / Trade (non-HIPC)	78.000%	82.000%
Kenya / Trade	39.000%	49.000%
Mozambique / Trade (non-HIPC)	20.000%	26.000%
Senegal / Loans, Trade (non-HIPC)	12.000%	16.000%
Sudan / Loans (non-HIPC)	11.000%	14.000%
Tanzania / Loans, Trade (non-HIPC)	10.000%	13.000%
Uganda / Trade (non-HIPC)	14.000%	16.000%
Zambia / Loans, Trade (non-HIPC)	13.000%	20.000%
Zimbabwe / Trade	1.000%	3.000%

Middle East Hyper-Exotics

Country / Issue	Price Range	
Egypt Trade	65.000%	75.000%
Iraq / Paris Club	85.000%	90.000%
Iraq / Bonds	92.000%	93.500% ↓
Libya / Trade	25.000%	35.000% ↓
Syria / Trade	6.000%	11.000% ↓

Trade : Trade Debt Instruments
 Loans: Loan Agreements
 PDI: Past Due Interest
 Pns: Promissory Notes
 Pars: Brady Par Bonds
 ↓↑: Changes compared to last edition

Prices are a percentage of principal only, however assuming inclusion of an average amount of PDI for the specific debt instrument and the specific debtor. Trade debts and their documentation differ from case to case and price ranges should therefore be considered as benchmark only.

Price ranges are based on a monthly compilation of sources and analytics. Liquidity on most instruments is very limited and trading may not have taken place for some time.

Prices of debts of other countries and/or other classes are available on request.

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