Fitch Solutions

June 2019
Vol 24 Issue 6

Africa Monitor
North Africa

Egypt: Banks To Record Strong Loan Growth Over 2019 And Beyond

Key View

- We forecast Egyptian banks to record strong loan growth of 22.5% over 2019 as macroeconomic conditions improve and lower interest rates boost demand.
- The government's share of total loans will remain sizeable, but decline gradually in the medium term as its austerity drive progresses and private sector activity picks up.

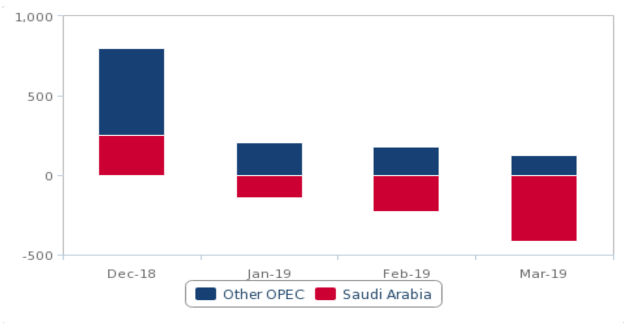
...continued on page 2

Libya: Haftar's Move On Tripoli Risks Conflict Escalation 5

Libyan National Army commander General Khalifa Haftar's advance towards Tripoli threatens to exacerbate the country's civil conflict and trigger further refugee outflows. Haftar, 75, has been the dominant military power in eastern Libya in the post-Qadhafi era,

Oil Outlook

Saudi Arabia Leading The Way
OPEC Production Cuts Versus November 2018 Reference Level ('000 b/d)



Source: OPEC, Fitch Solutions

Oil closed above USD70.0 per barrel (/bbl) in April for the first time since early December 2018, bringing its year-to-date gains to nearly 34%. Renewed concerns over supply disruption emerged in Libya as the Libya National Army moved to occupy Tripoli. Better numbers from China's leading indicators and no further escalation in trade tensions with the US have provided additional upside. However, the International Monetary Fund's downward revision of the global outlook has tempered gains. Overcompliance at 135% of OPEC+ production cut targets in March and continued impact on supply from sanctions in Iran and Venezuela have supported price appreciation. We at Fitch Solutions expect the overall demand growth to remain positive within emerging markets, excluding China. The US will boost overall demand as China and the eurozone will continue to drag on consumption. The supply-side constraint has tightened markets while outweighing concerns about the health of the global economy. We hold to our current forecast for Brent at an annual average of USD73.0/bbl for 2019 *(see 'Brent: Strong Fundamentals To Drive H2 Gains', April 2).*

ISSN: 1472-1791

Contents

Copy Deadline: 12 April 2019

Analysts: Andrine Skjelland, Axel Dalman, Matthew Searle, Selim Elbadri

Editor: Julie Beckenstein

Sub-Editor: Vida Jones

Subscriptions Manager: Lyan Chan

Marketing Manager: Julia Consuegra

Production: Vicky Naithani

Head Office
30 North Colonnade, London
E14 5GN, UK

Company Locations
London | New York | Singapore
Hong Kong | Dubai | Pretoria

Subscriptions Contact:

Tel: +44 (0)20 7248 0468

Fax: +44 (0)20 7248 0467

email: subs@fitchsolutions.com

NORTH AFRICA RISK INDEX

Our Country Risk Index scores countries on a 0-100 scale, evaluating short-term and long-term political stability, short-term economic outlook, long-term economic potential and operational barriers to doing business. For a detailed methodology, visit fitchsolutions.com or contact us using the details on page 1.

RISK INDEX TABLE

	Short Term		Long Term		Operational Risk	Country Risk
	Political	Economic	Political	Economic		
Morocco	70.6	48.8	69.2	53.0	54.1	57.8
Tunisia	56.9	34.6	68.6	44.3	47.1	50.0
Algeria	47.3	50.4	54.4	53.2	42.0	47.9
Egypt	53.3	53.3	54.0	50.4	45.2	50.3
Libya	26.7	35.2	20.2	31.4	28.0	28.7
Regional Average	**51.0**	**44.5**	**53.3**	**46.5**	**43.3**	**46.9**
Global Average	**63.1**	**52.8**	**62.0**	**54.2**	**49.8**	**55.1**

Note: Scores out of 100; higher scores indicate lower risk. Source: Fitch Solutions

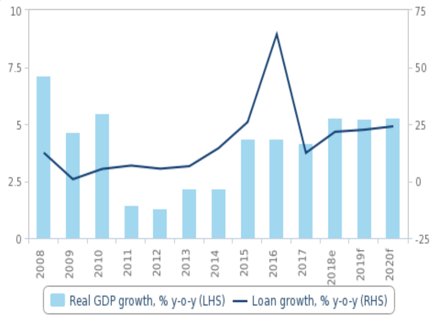
EGYPT – ECONOMIC OUTLOOK

...continued from front page

- Banks' deposits will expand at a slower pace than loans. The loan-to-deposit ratio remains low by EM standards, implying limited risks to liquidity and overall system stability.

Improving Macroeconomic Conditions To Fuel Credit Demand

Egypt – Real GDP & Banks' Loan Growth, % chg y-o-y



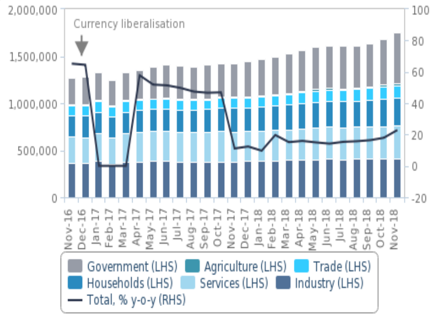
e/f = Fitch Solutions estimate/forecast. Source: CBE, Fitch Solutions

Egyptian banks look set to record strong loan growth over 2019. Egypt's macroeconomic conditions are improving, with declining inflation easing pressures on local households and businesses, and a more competitive exchange rate boosting exports (*see 'Egypt To Record Robust Growth Over 2019-2020,' February 11 2019*). The Central Bank of Egypt (CBE) has resumed its monetary easing cycle, cutting interest rates by 100 basis points at its latest policy meeting on February 14 2019 with the aim of boosting credit expansion to promote private sector activity. The cut came earlier than we had anticipated. While we still believe the CBE will pause its easing cycle around mid-2019 to allow for the inflationary impact of subsidy cuts to feed through, this has led us to **revise up our forecast for Egyptian banks' loan growth to 22.5% in 2019 from 18.1% previously.** This also reflects the steady acceleration in loan growth seen over H218, from 15.3% y-o-y in July to 22.8% at the latest reading in November. We nevertheless continue to highlight risks of global financial volatility returning and higher oil prices, which could yet return a hawkish bias to the CBE's policy trajectory (*see 'CBE Rate Cuts Positive For Growth, Though Downside Risks Persist,' February 15 2019*).

Over the medium term, we note that the government is looking to introduce a new tax law on sovereign debt holdings, which could weigh on banks' interest margins unless they divert a greater share of their liquidity towards loans. This may serve to encourage loan growth in the years ahead, should demand from high-quality borrowers pick up sufficiently to facilitate such a shift.

Steady Loan Growth Ahead Amid A More Stable Currency, Lower Inflation

Egypt – Banks' Extension Of Credit By Sector, EGP & Total % y-o-y



Source: CBE, Fitch Solutions

The government's share of total loans will remain sizeable, but decline gradually in the years ahead. Crowding out of the private sector remains an issue as credit demand from the government, which accounted for 30.9% of total loans in November, remains strong. The growth in loans to the government averaged 36.5% in the first 11 months of 2018. As the fiscal deficit looks set to narrow only gradually (*see 'Egypt To*

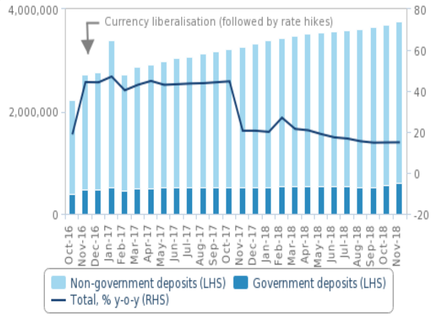
Record Further Progress On Fiscal Consolidation In 2019,' December 11 2019), we expect continued expansion in this segment over the next several years – albeit at a decelerating pace. Meanwhile, we believe private sector loan growth will pick up significantly as cost pressures ease, borrowing costs reduce, and the government continues to invest heavily in infrastructure. Credit extension to industry, trade, services and households rose by 8.0%, 27.4%, 9.7% and 18.6% respectively in November 2018, suggesting this dynamic is already playing out.

Deposits will also expand, albeit at a slower pace than loans. Strong economic activity and falling unemployment, coupled with lower inflation, will boost Egyptians' real incomes and likely raise savings rates. We highlight that much of the population still remains unbanked, which means there is substantial room for organic growth in lenders' deposit bases over the coming years. Egypt's banking penetration is estimated at only 10-15% (though, a higher rate in the range of 30-35% is estimated when taking into account individual savings at post offices). The CBE's easing cycle will cap gains to some extent, however, we expect the pace of cuts to be gradual, keeping real rates relatively attractive in the near-to-medium term. Overall, we forecast deposit growth at 15.0% in 2019, marking a slight increase from an estimated 14.5% in 2018.

This implies a gradual increase in Egypt's loan-to-deposit ratio, however, at an estimated 45.8% in Q318, this remains among the lowest levels regionally. Finally, we note that local households and the Egyptian diaspora account for the vast majority of banks' deposits, limiting the risk of global financial volatility affecting funding and system stability.

Deposits To Expand At A More Gradual Pace

Egypt – Banks' Deposits By Sector, EGP & Total % y-o-y



Source: CBE, Fitch Solutions

Banking Sector Structural Characteristics

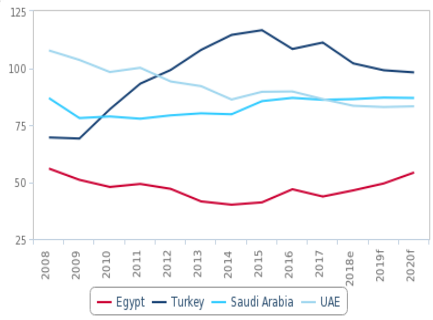
Asset Quality: Asset quality of Egyptian banks has remained relatively high, despite a challenging macroeconomic environment. NPLs stood at 4.4% of total loans as per CBE data from Q318, having fallen from 11.0% in 2011 (partly the result of NPL write-offs). Our expectation is for asset quality to remain broadly stable over the years ahead, supported by robust economic activity and job creation, and gradually reducing inflation and interest rates.

FX Exposure: Egyptian banks have limited exposure to currency risks, with foreign assets accounting for less than 10% of the total. Following the liberalisation of the pound in November 2016, we also expect the unit to remain largely stable in the years ahead, further lowering the likelihood that local banks experience any substantial FX-related instability.

Capital Adequacy: The overall capital adequacy ratio of Egyptian banks has improved from 14.0% in December 2016 to 15.6% in June 2018. According to the IMF, all of the country's largest banks remain fairly well capitalised, above the CBE's prudential requirement. Some smaller banks are reported to be less insulated against potential shocks; however, these are not believed to pose a threat to wider system stability.

Plenty Of Room For Growth

Selected MENA Countries – Loan-To-Deposit Ratio



e/f = Fitch Solutions estimate/forecast. Source: CBE, Fitch Solutions

EGYPT – ECONOMIC OUTLOOK

EGP: More Stability Ahead

Key View: *The Egyptian pound is likely to remain fairly stable in 2019 amid robust economic growth, an improving external position and still-attractive real interest rates.*

Short-Term Outlook (three-to-six months)

The Egyptian pound appears to have appreciated slightly against the US dollar in recent weeks as a result of reduced global financial volatility and renewed foreign interest in Egyptian debt. We expect the unit to remain fairly stable over the next few months amid slowing global financial tightening and reduced fears of a global growth correction. Robust economic growth and improving external dynamics will also provide support.

We do note, however, that the Central Bank of Egypt (CBE) has now phased out its repatriation mechanism, which previously had served to limit exchange rate volatility (as it guaranteed dollar returns on a share of portfolio inflows against a separate reserves account). Consequently, we could see somewhat greater movement in the pound moving forward.

Long-Term Outlook (six-to-24 months)

We retain our view for relative pound stability throughout the next six-to-24 months. While the CBE's likely resumption of its monetary easing cycle will put downside pressure on the unit, we highlight that the pace of cuts is likely to prove gradual (*see 'CBE Likely To Keep Rates On Hold In Near Term,' February 12 2019*), keeping real rates relatively attractive.

In addition, we expect real GDP growth to remain strong and the external position to continue to gradually improve (*see 'Egypt To Record Robust Growth Over 2019-2020,' February 11 2019*), underpinning support for the pound. Finally, we at Fitch Solutions are of the view that the CBE would likely step in to provide support for the exchange rate should it face risks of a sharper correction. This is consistent with recent statements by the central bank governor and the CBE's prioritisation of macroeconomic stability.

Risks To Outlook

Political instability remains a downside risk to Egypt's ongoing economic recovery, and by extension, the value of the pound. While not our core view, popular unrest could spread as a result of still-challenging conditions for Egyptian households and businesses and continued political repression (*see 'Egypt President May Look To Extend Rule Beyond 2022,' January 16 2019*). In turn, this could

EGYPT – DATA & FORECASTS

	2015	2016	2017	2018e	2019f	2020f	2021f
Population, mn	93.78	95.69	97.55	99.38	101.17	102.94	104.69
Nominal GDP, USDbn	317.3	269.4	194.4	249.0	296.8	345.0	398.3
GDP per capita, USD	3,725	3,257	2,429	2,845	3,268	3,667	4,108
Real GDP growth, % y-o-y	4.4	4.3	4.2	5.3	5.2	5.3	4.9
Consumer price inflation, % y-o-y, ave	10.4	13.7	29.6	14.4	12.7	10.2	9.5
Consumer price inflation, % y-o-y, eop	11.1	23.3	21.9	12.0	10.5	9.8	9.2
Central bank policy rate, % eop	10.25	15.75	19.75	17.75	15.75	13.75	12.00
Exchange rate EGP/USD, ave	7.70	10.06	17.85	17.82	18.01	18.30	18.53
Exchange rate EGP/USD, eop	7.83	18.14	17.78	17.92	18.10	18.50	19.00
Budget balance, EGPbn	-267.6	-326.4	-361.9	-420.0	-424.3	-416.0	-402.3
Budget balance, % of GDP	-10.9	-12.0	-10.4	-9.5	-7.9	-6.6	-5.5
Goods and services exports, USDbn	44.1	34.8	37.1	47.3	52.6	57.3	61.2
Goods and services imports, USDbn	72.4	66.9	68.8	73.5	77.6	82.5	87.7
Current account balance, USDbn	-12.1	-19.8	-14.4	-6.0	-5.9	-7.4	-8.3
Current account balance, % of GDP	-3.8	-7.4	-7.4	-2.4	-2.0	-2.2	-2.1
Foreign reserves ex gold, USDbn	17.7	15.0	28.7	41.6	41.7	41.7	41.6
Import cover, months	2.9	2.7	5.0	6.8	6.5	6.1	5.7
Total external debt stock, USDbn	48.3	67.6	82.9	75.6	75.7	77.1	78.4
Total external debt stock, % of GDP	15.2	25.1	42.6	30.4	25.5	22.4	19.7
Crude, NGPL & other liquids prod, '000b/d	718.0	684.0	657.0	672.2	687.8	695.5	699.3
Total net oil exports (crude & products), '000b/d	-108.1	-172.9	-159.1	-103.3	-64.6	-79.3	-90.9
Dry natural gas production, bcm	44.3	42.1	50.7	63.4	78.2	84.8	81.6
Dry natural gas consumption, bcm	47.8	51.3	56.4	59.8	64.0	67.4	70.8

e/f = Fitch Solutions estimate/forecast. Source: National sources, Fitch Solutions deter tourists from travelling to the country and also discourage the government from implementing further fiscal consolidation measures. The latter would weigh on business confidence, foreign investment and dollar inflows, and thus cause faster-than-expected depreciation of the pound. In addition, large-scale outflows of portfolio investments remain a concern in the event of a global growth correction and resultant 'risk-off' sentiment.

LIBYA – ECONOMIC OUTLOOK

Haftar's Move On Tripoli Risks Conflict Escalation

Key View

- Libyan National Army commander General Khalifa Haftar's advance towards Tripoli threatens to exacerbate the country's civil conflict and trigger further refugee outflows.
- Haftar appears to be either looking to expand and consolidate his territorial control, or pressure the rival Government of National Accord in Tripoli into political concessions.
- Should Haftar be aiming for sustained territorial expansion, then risks of conflict escalation would heighten dramatically – both in the capital and elsewhere, where Libyan National Army forces may now be stretched too thin to fight off rival militias.

Libyan National Army (LNA) commander General Khalifa Haftar's advance towards Tripoli in the first week of April threatens to exacerbate the country's civil conflict. Haftar, 75, has been the dominant military power in eastern Libya in the post-Qadhafi era, while the west of the country is nominally under the control of the internationally-backed Government of National Accord (GNA) in Tripoli. He is loosely aligned with the House of Representatives (HoR), a rival government to the GNA which is based in Tobruk. The GNA and HoR had officially split in 2014 and have since then been unable to agree on a power-sharing arrangement (*see 'Numerous Headwinds Persist To Libya's Stabilisation Process', February 5 2019*). Haftar's advance is likely to further fuel tensions between the main factions vying for power in Libya, as well as the patchwork of smaller militias and groups that operate on the ground throughout the country.

Haftar's overarching strategy appears to be to expand his influence across Libya at the expense of the GNA, in order to improve his chances of settling the conflict on his own terms (ie, ensure that he assumes political or military leadership). Haftar may have opted to move against the capital at this particular point in time as he has decided he has a unique opportunity to take and consolidate territorial control of the whole country. More likely, however, Haftar is looking to pressure the GNA and the wider international community to make concessions in order to improve his chances of assuming leadership via a political settlement. Iit is probably not a coincidence that the offensive is occurring just days ahead of a UN conference on Libya (scheduled for April 14-16), during which a timetable for long-delayed national elections is expected to be discussed. It also appears that the LNA's numbers are too small at present to sustain a prolonged campaign and takeover of Tripoli, while at the same time defending other strategically important areas already under the army's control against rival militias (including oil-producing regions). This would probably be the case even if several Tripoli-based militias switched to Haftar's side.

As such, **we still view it as possible that Haftar may agree to call off his offensive on Tripoli or hand back control over the capital after a short period of time** should the GNA make concessions. Risks of such concessions failing to materialise are considerable: indeed, the GNA has already warned it would counterattack Haftar's forces, which at the time of writing were on the outskirts of the city. In addition, **there is also a chance that clashes between the LNA and rival militias on the ground could spiral out of control.** This raises the spectre of urban warfare in a city of more than one million people, resulting in civilian casualties, and potentially a humanitarian crisis that triggers greater refugee flows across the Mediterranean towards southern Europe. We will closely be monitoring the LNA and rival militias' movements in Tripoli over the coming days and put out further research once the trajectory of Haftar's campaign becomes clearer.

LIBYA – ECONOMIC OUTLOOK

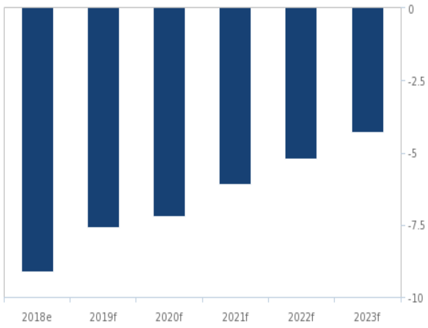
Fiscal Deficit To Narrow

Key View

- At Fitch Solutions, we believe Libya's fiscal deficit will narrow in the years ahead on the back of rising oil revenues. We forecast the fiscal deficit at 7.7% of GDP in 2019 and 7.3% in 2020.
- Political instability and lack of consensus between rival factions will keep government spending high, limiting the pace of deficit reduction.
- Despite large budget shortfalls, the public debt burden as a share of GDP will grow only gradually.

Deficit To Gradually Narrow

Libya – Budget Balance, % of GDP



e/f = Fitch Solutions estimate/forecast. Source: IMF, Fitch Solutions

Libya's fiscal deficit will gradually narrow over the coming quarters on the back of higher oil revenues (as recorded by the Tripoli-based authorities). The majority of Libya's tax revenue comes from oil and there is limited scope for any non-oil revenue increases. Libya's crude oil production has been climbing over the past couple of years, averaging 1.1mn barrels per day (b/d) in November 2018, its highest level since 2013. Our Oil & Gas team forecasts production to average 1.3mn b/d in 2019 and 1.35mn b/d day in 2020 – higher than the 1mn b/d-level recorded in 2018. At the same time, oil prices are set to continue heading higher. The decision by OPEC+ to cut 1.2mn b/d of supply as of January 1 2019 will help maintain a floor under Brent and set the stage for gains in the new year. As such, our Oil & Gas team forecasts Brent to average USD75.0 per barrel (/bbl) for 2019, implying significant gains from current spot price levels of around USD60.0/bbl.

Current spending looks set to remain high, weighing on the pace of deficit reduction. The Tripoli-based CBL and Government of National Accord (GNA) have agreed to implement reforms to restrict current spending, including cuts to fuel subsidies. As Libya suffers from an exceptionally bloated public sector and some of the highest subsidies relative to GDP in the world, this is ostensibly a positive step. However, amid the ongoing political conflict, we see limited scope for genuine progress, as the country's rival factions will be reluctant to

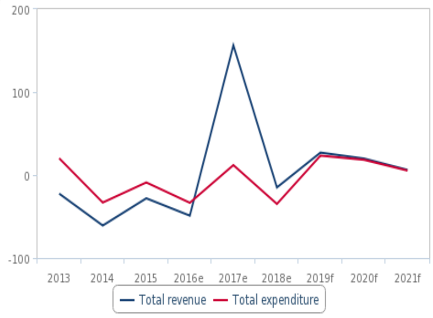
LIBYA – DATA & FORECASTS

	2015	2016	2017	2018e	2019f	2020f	2021f
Population, mn	6.23	6.29	6.37	6.47	6.57	6.66	6.75
Nominal GDP, USDbn	17.7	15.3	25.1	18.4	20.3	22.0	24.7
GDP per capita, USD	2,833	2,434	3,941	2,841	3,091	3,305	3,664
Real GDP growth, % y-o-y	-45.5	-16.1	64.0	10.3	10.1	9.9	9.5
Consumer price inflation, % y-o-y, ave	9.8	25.9	27.0	19.0	15.0	12.0	10.0
Consumer price inflation, % y-o-y, eop	15.7	25.2	25.0	18.0	14.0	11.0	9.0
Central bank policy rate, % eop	3.00	3.00	3.00	3.00	3.00	3.00	3.00
Exchange rate LYD/USD, ave	1.37	1.37	1.39	2.50	2.70	2.90	3.00
Exchange rate LYD/USD, eop	1.39	1.44	1.36	2.50	2.70	2.90	3.00
Budget balance, LYDbn	-26.4	-20.2	-10.4	-4.2	-4.2	-4.6	-4.5
Budget balance, % of GDP	-108.2	-94.8	-29.6	-9.1	-7.6	-7.2	-6.1
Goods and services exports, USDbn	15.7	9.5	13.2	16.8	18.0	19.5	20.8
Goods and services imports, USDbn	29.1	15.9	20.4	23.6	25.2	26.3	27.5
Current account balance, USDbn	-12.9	-5.7	-6.4	-6.0	-6.3	-5.9	-5.6
Current account balance, % of GDP	-73.1	-37.4	-25.5	-32.7	-31.0	-26.8	-22.8
Foreign reserves ex gold, USDbn	73.7	65.9	61.3	58.2	55.9	53.7	51.5
Import cover, months	30.4	49.8	36.1	29.6	26.6	24.5	22.5
Total external debt stock, USDbn	4.7	6.3	7.3	8.1	9.0	9.9	10.8
Total external debt stock, % of GDP	26.5	41.4	29.0	44.1	44.2	44.8	43.5
Crude, NGPL & other liquids prod, '000b/d	415.8	419.2	863.0	993.5	1,185.7	1,244.1	1,293.5
Total net oil exports (crude & products), '000b/d	203.2	210.1	653.3	752.6	908.8	939.8	974.0
Dry natural gas production, bcm	11.6	9.3	9.6	11.1	12.7	13.4	14.0
Dry natural gas consumption, bcm	4.5	4.5	4.7	5.4	5.7	6.1	6.4

e/f = Fitch Solutions estimate/forecast. Source:National sources, Fitch Solutions push through any reforms that risk eroding their popular and militia support. Any cuts to fuel subsidies will likely be limited in size, and compensated with increases in cash transfers to vulnerable households, meaning their overall impact on state spending will be minor. In turn, this leaves little room for increases in capital spending and improvements in public service delivery. In line with this, we forecast the fiscal deficit to narrow from 9.1% of GDP in 2018 to 7.7% of GDP and 7.3% of GDP in 2019 and 2020 respectively.

Slow Pace Of Consolidation

Libya – Government Revenue & Expenditure, % chg y-o-y



Note: Figures represent data from Tripoli-based authorities and likely underestimate the national total. e/f = Fitch Solutions estimate/forecast. Source: IMF, Fitch Solutions

Persistent deficits will primarily be funded through domestic borrowing. The official budget deficit will likely continue to be funded by borrowing from the Central Bank of Libya. In addition, western authorities are able to draw on foreign exchange reserves, which remain sizeable. Meanwhile, eastern-based authorities are also reported to be raising funds through the sale of treasury bills to local banks. A rival central bank has been set up in the east, though it is unclear to which extent it remains active. The Libyan National Army (LNA) sources funding directly from its LNA Authority for Investment and Public Works.

Overall, public debt levels (estimated by the IMF at around 100% of GDP in 2017) will continue to increase – albeit at a slowing pace, as higher oil revenue leads to gradually narrowing fiscal deficits. Furthermore, GDP is set to rise rapidly in the years ahead, limiting the rise in the debt ratio. Upon an eventual reconciliation between the country's rival political factions, we caution that any new governing body would likely have also to absorb any debt accumulated by the eastern-based authorities. We also highlight, however, that such a new body would also benefit from the unfreezing of Libya's sovereign wealth fund assets as a result of the lifting of UN sanctions.

MOROCCO – ECONOMIC OUTLOOK

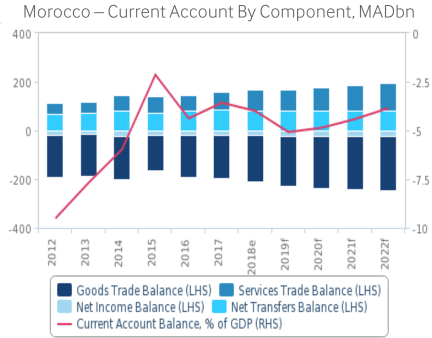
Current Account Deficit To Widen, But External Risks Remain Limited

Key View

- At Fitch Solutions, we believe Morocco's current account deficit will widen to 5.1% of GDP in 2019 from an estimated 4.0% of GDP in 2018.
- This will be primarily driven by a widening of the goods trade deficit on the back of weak external demand and a rising import bill.
- Furthermore, we expect tourism and remittances to mitigate the widening goods trade balance to a lesser extent.
- We expect investor sentiment to remain broadly positive on the back of robust external support and low short-term external debt obligations by regional standards.

Current Account Deficit To Widen On Weaker Terms Of Trade

Morocco – Current Account By Component, MADbn



e/f = Fitch Solutions estimate/forecast. Source: Office des Changes, Fitch Solutions

We forecast Morocco's current account deficit to grow in 2019 to 5.1% of GDP, mostly on the back of a widening goods trade deficit. This would be noticeably larger than our 2018 estimate of 4.0% of GDP but somewhat below the 10-year historical average of 5.6% of GDP.

We believe the larger current account deficit will be primarily driven by a widening goods trade deficit. High levels of government capital expenditure on energy and transportation infrastructure will keep demand for capital inputs elevated which will put upward pressure on the country's import bill (*see 'Morocco's Economic Growth To Accelerate Modestly', January 22 2019*). Figures in 2018 show that equipment (such as machinery) and intermediate goods together make up just under half of total imports. Furthermore, our Oil

& Gas team forecast oil prices to rise to USD75.0 per barrel (/bbl) in 2019 from USD71.7/bbl in 2018, suggesting that Morocco's energy import bill (17.2% of the total import bill in 2018) will also increase in 2019.

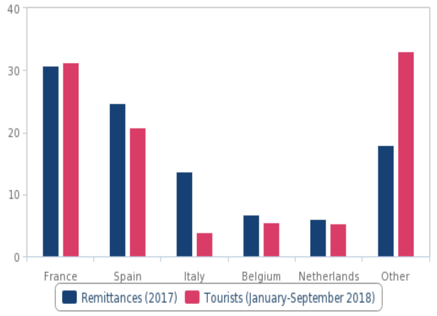
Simultaneously, exports are unlikely to grow fast enough to offset the higher import bill as, despite a robust outlook for autos and phosphates, weaker Eurozone growth will weigh on overall external demand (*see 'Eurozone Growth To Slow Even Further In 2019', November 27 2018*). Moroccan exports to the Eurozone represented 61.0% of total exports in 2017. As such, weak Eurozone private consumption growth in particular should weaken demand for key Moroccan exports such as textiles. Combined, this will enlarge the goods trade deficit by 7.6% in 2019.

Meanwhile, services and remittances will offer less support to hard currency inflows. Weaker Eurozone growth will also constrain inflows of remittances and tourism revenue, given that the region accounts for more than 70% of total tourist arrivals and more than 80% of all remittance inflows. We have already seen these flows perform poorly over 2018, with tourism receipts growing by a modest 1.4% in 2018 compared to 12.3% in 2017, while remittance inflows declined by -1.7% in 2018 from 6.0% growth in 2017. As such, these flows will mitigate Morocco's trade deficit to a lesser extent in 2019, weighing on the current account balance.

Despite a widening current account deficit, we believe risks to external stability will remain relatively low in the coming quarters. By end-September 2018, foreign direct investment (FDI) made up over 55.3% of Morocco's external liabilities, pointing to high levels of external stability since FDI tends to be less prone to capital flight than, for instance, portfolio investments. Net FDI inflows have also risen robustly in recent quarters, with growth hitting 28.6% in 2018. This should reduce the need to draw on foreign reserves and strongly mitigate risks stemming from Morocco's net debtor status. While the government has said it will resort to international bond markets in 2019, we do not expect this to markedly increase Morocco's relatively low external debt stock, which registered 45.4% of GDP at end-2017. Coupled with factors such as continued IMF support (the government secured a new USD2.7bn Precautionary Liquidity Line in December 2018) and a low short-term external debt-to-reserves ratio, borrowing costs should remain relatively subdued even amidst a more challenging global financial landscape in 2019.

Weak Eurozone Growth To Hit Tourism And Remittance Inflows

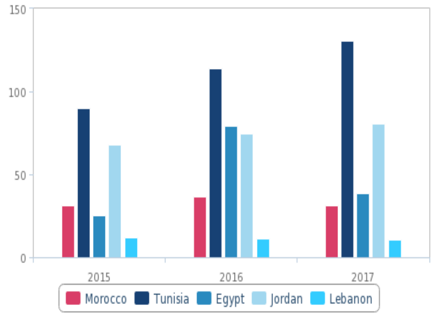
Morocco – Remittance Inflows & Tourist Arrivals By Country of Origin, % of total



Source: World Bank, Observatoire Du Tourisme, Fitch Solutions

Morocco's Short-Term External Debt Stock Small And Stable By Regional Standards

Selected MENA countries – Short-Term External Debt Obligations, % of Reserves



Source: World Bank, Fitch Solutions

MOROCCO – ECONOMIC OUTLOOK

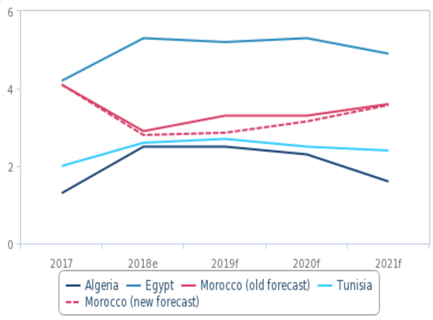
Growth Outlook To Deteriorate On Eurozone Weakness

Key View

- We at Fitch Solutions have revised down Morocco's 2019 and 2020 growth forecasts to 2.9% and 3.2% respectively, from 3.3% in both years, on the back of a deteriorating growth outlook for the Eurozone.
- We expect the fiscal stimulus to strengthen domestic demand, keeping household consumption growth elevated over the coming quarters.
- Fixed capital formation will provide further tailwinds to growth, largely owing to a boost in public capital spending and robust credit demand.
- Finally, we note that exogenous shocks to agricultural produce will continue to be a source of risk to the Kingdom's growth outlook.

Moroccan Growth To Converge To Regional Average

North Africa ex. Libya – Real GDP Growth, % y-o-y



Note: Dashed line = New forecasts, solid line = old forecasts. e/f = Fitch Solutions estimate/forecast. Source: National Sources, UN, Fitch Solutions

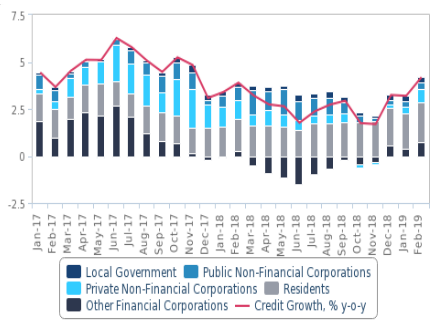
We have revised down Morocco's 2019 and 2020 growth forecasts to 2.9% and 3.2% respectively from 3.3% in both years previously. While this represents a modest uptick in growth relative to the 2018 estimate of 2.8%, we note that it compares poorly to the 2009-2018 average of 3.6%.

A troubled Eurozone will drag on Morocco's export growth. Our Europe team has revised down its 2019 and 2020 Eurozone growth forecasts from 1.6% to 1.5% (*see 'Downward Eurozone Growth Revision Highlights Challenging Outlook', March 19 2019*). Meanwhile, France and Italy, which together accounted for 26.1% of Morocco's goods exports and 35.0% of tourist arrivals in 2018, have both seen 0.8 percentage points stripped off their private consumption growth forecasts for 2019. While we have adjusted Morocco's export growth forecast to account for these reductions, we see scope for further cuts to headline growth down the line should downside risks highlighted by our Europe team – such as Eurozone recession – materialise in the coming quarters.

We expect government spending and subdued inflation to keep household consumption elevated. Privatisation revenues will enable the government to introduce fiscal stimulus in 2019, largely built around a boost in social spending. This includes a substantial increase in hiring in sectors such as healthcare and education, for example, coupled with plans to triple the number of beneficiaries of the 'Tayssir' cash transfer programme. Domestic demand will be further reinforced by an environment of low inflation, averaging 1.4% y-o-y in the last twelve months. We expect this modest price growth to extend into the next few quarters, in large part due to a relatively soft outlook for oil prices.

Credit Growth To Boost Private Investment Momentum

Morocco – PP Contribution to Credit Growth, % y-o-y



Source: BAM, Fitch Solutions

Moreover, increased public capital spending coupled with strong credit demand will provide tailwinds to growth in 2019. Public capital expenditure (capex) will increase in line with the government's commitment to support the country's numerous regional development projects. In 2019, capex will primarily be directed towards building new schools and reducing the housing deficit, but also towards major transport projects such as the new MAD10bn Nador West-Med port complex and its MAD4.5bn highway link. Furthermore, a pick-up in credit demand in both public and private non-financial corporations signals an increase in business activity, which in turn is likely to translate into more capital investments.

Finally, we stress that exogenous shocks to agriculture will continue to be a source of risk to economic growth. Preliminary data suggests that growth in agricultural output has slowed down in Q119 due to lacklustre rainfall. Despite occupying just a tenth of GDP, agriculture employs 36.5% of the total employment while food alone occupies 37.0% of the CPI basket. We therefore stress that any shocks to agricultural production – such as adverse weather conditions, especially during peak harvesting season (Q2 and Q3) – can potentially feed through to higher food prices, higher unemployment and lower wages, eroding household's purchasing power and hampering private consumption growth.

MOROCCO – DATA & FORECASTS

	2015	2016	2017	2018e	2019f	2020f	2021f
Population, mn	34.80	35.28	35.74	36.19	36.64	37.07	37.50
Nominal GDP, USDbn	101.3	103.6	109.5	119.3	123.3	124.8	127.3
GDP per capita, USD	2,911	2,936	3,065	3,295	3,365	3,366	3,394
Real GDP growth, % y-o-y	4.5	1.1	4.1	2.8	2.9	3.2	3.6
Industrial production, % y-o-y, ave	0.8	3.0	3.0	3.0	3.0	3.0	3.0
Consumer price inflation, % y-o-y, ave	1.6	1.6	0.8	1.8	1.3	1.5	1.5
Consumer price inflation, % y-o-y, eop	0.6	1.8	1.9	0.1	1.2	1.5	1.5
Central bank policy rate, % eop	2.50	2.25	2.25	2.25	2.50	2.75	3.00
Exchange rate MAD/USD, ave	9.75	10.13	9.33	9.20	9.60	10.00	10.30
Exchange rate MAD/USD, eop	9.93	10.13	9.33	9.20	9.60	10.00	10.30
Budget balance, MADbn	-41.2	-43.9	-37.8	-38.6	-39.0	-40.7	-42.5
Budget balance, % of GDP	-4.2	-4.3	-3.6	-3.5	-3.4	-3.3	-3.3
Goods and services exports, USDbn	33.3	34.3	38.6	44.2	45.8	47.4	49.2
Goods and services imports, USDbn	41.3	45.2	49.3	55.8	58.5	59.4	60.4
Current account balance, USDbn	-2.2	-4.5	-3.9	-4.7	-6.1	-5.9	-5.4
Current account balance, % of GDP	-2.1	-4.4	-3.6	-3.9	-5.0	-4.7	-4.3
Foreign reserves ex gold, USDbn	22.1	24.6	24.3	26.5	28.1	30.5	32.9
Import cover, months	6.8	7.0	6.7	6.0	6.1	6.4	6.7
Total external debt stock, USDbn	43.1	46.3	49.8	52.9	55.5	58.1	60.6
Total external debt stock, % of GDP	42.5	44.7	45.4	44.3	45.0	46.6	47.6
Crude, NGPL & other liquids prod, '000b/d	0.2	0.2	0.2	0.2	0.2	0.2	0.2
Total net oil exports (crude & products), '000b/d	-284.0	-288.1	-300.6	-311.3	-323.0	-334.4	-347.0
Dry natural gas production, bcm	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Dry natural gas consumption, bcm	1.1	1.1	1.1	1.1	1.1	1.1	1.1

e/f = Fitch Solutions estimate/forecast. SourceL National sources, Fitch Solutions

ALGERIA – POLITICAL OUTLOOK

Quick View: Ruling Elite To Steer Political Transition, Despite Bouteflika's Resignation

The Latest: On April 2 2019, Algeria's President Abdelaziz Bouteflika (82) announced his resignation after nearly two decades in power. The move follows over a month of widespread protests across the country, which began in response to the president's decision to run for a fifth term in office. Protests have since evolved into a wider expression of disapproval of the ruling elite, composed of an opaque mix of military and business leaders, as well as other people close to the president. Prior to April 2, Bouteflika had already delayed the presidential elections planned for April 29 and rescinded his bid, but stopped short of stepping down.

Implications: Bouteflika's accelerated exit may have been the result of growing pressure from the military leadership, with army chief of staff Ahmed Gaid Salah having repeatedly called for the president's resignation over the past week. Rather than signalling intensified rivalry between the military leadership and the executive branch of government, we believe the move points to continued relative cohesion within the political elite, who appears to be looking for a way to grant just enough concessions to placate protesters, while still maintaining control over the post-Bouteflika political transition.

In particular, the composition of the new caretaker cabinet – appointed by the president shortly before his resignation – suggests that the transition process will be managed by the ruling elite. Although some key appointments appear to be technocratic – for instance, the central bank governor has been named finance minister – there are also strong elements of the old regime. Bouteflika will remain as defence minister and Salah will stay on as deputy defence minister, while Prime Minister Noureddine Bedoui (a former interior minister) will also remain in his post.

Meanwhile, the opposition remains relatively poorly organised and without strong leadership, limiting its ability to bargain. Reports recently suggested that several opposition parties had come together to form a unified movement (named the 'National Coordination for Change'), but the existence of this organisation was later denied by the parties' respective leaders. Several figures, such as ex-Prime Minister Ali Benflis and lawyer Mustapha Bouchachi, have been highlighted as potential opposition leaders, but none have successfully rallied protesters under one banner. This could change as Bouteflika's exit leaves space for more substantive policy discussions, but we

ALGERIA – DATA & FORECASTS

	2015	2016	2017	2018e	2019f	2020f	2021f
Population, mn	39.87	40.61	41.32	42.01	42.68	43.33	43.97
Nominal GDP, USDbn	166.5	160.2	167.6	174.3	186.9	201.7	215.0
GDP per capita, USD	4,176	3,944	4,056	4,149	4,378	4,654	4,889
Real GDP growth, % y-o-y	3.7	3.3	1.3	2.5	2.5	2.3	1.6
Industrial production, % y-o-y, ave	1.5	1.5	1.5	1.5	1.5	1.5	1.5
Consumer price inflation, % y-o-y, ave	4.8	6.4	5.4	5.0	6.3	7.8	6.8
Consumer price inflation, % y-o-y, eop	4.4	7.0	4.9	5.0	7.5	8.0	5.5
Central bank policy rate, % eop	4.00	3.50	3.75	4.00	4.00	4.00	4.00
Exchange rate DZD/USD, ave	100.36	109.41	110.94	117.38	121.50	124.50	127.50
Exchange rate DZD/USD, eop	107.10	110.40	114.76	120.00	123.00	126.00	129.00
Budget balance, DZDbn	-2,551.0	-2,286.0	-1,207.0	-2,088.9	-2,249.2	-2,204.4	-2,148.8
Budget balance, % of GDP	-15.3	-13.0	-6.5	-10.2	-9.9	-8.8	-7.8
Goods and services exports, USDbn	38.1	32.7	37.6	48.0	52.7	53.9	55.0
Goods and services imports, USDbn	63.6	60.2	60.2	62.2	64.4	66.7	69.1
Current account balance, USDbn	-27.2	-26.2	-22.1	-13.5	-10.7	-11.7	-12.8
Current account balance, % of GDP	-16.3	-16.4	-13.2	-7.8	-5.7	-5.8	-5.9
Foreign reserves ex gold, USDbn	144.7	114.4	97.6	83.0	70.5	64.9	59.0
Import cover, months	33.0	27.8	23.9	19.6	16.1	14.3	12.6
Total external debt stock, USDbn	4.7	5.5	5.7	9.5	13.9	18.8	24.4
Total external debt stock, % of GDP	2.8	3.4	3.4	5.5	7.4	9.3	11.4
Crude, NGPL & other liquids prod, '000b/d	1,797.0	1,661.8	1,548.4	1,515.0	1,508.4	1,502.7	1,497.8
Total net oil exports (crude & products), '000b/d	1,419.9	1,260.2	1,148.2	1,112.7	1,085.8	1,067.9	1,053.7
Dry natural gas production, bcm	86.1	94.8	94.5	92.0	98.3	101.0	99.5
Dry natural gas consumption, bcm	39.5	36.0	37.4	38.6	38.7	39.7	40.8

e/f = Fitch Solutions estimate/forecast. Source: National sources, Fitch Solutions maintain that the fragmentation of the opposition – the parliament contains as many as 32 political parties outside the ruling two-party coalition – will complicate this process.

What's Next: Bouteflika will now hand over power to the Speaker of the Upper House, Abdelkader Bensalah, in line with the constitution. The Constitutional Council (which consists of nine appointed members, one of which is the president) will then be tasked with declaring elections in the next three months. More importantly, the ruling factions will now need to bring forward a mutually acceptable successor to Bouteflika to run in these elections. Although no such candidate has been forthcoming as of yet, it appears probable, in our view, that the heightened risks of political instability will push these factions, all of which benefit politically and financially from maintaining the status quo, to compromise.

Opposition figures have called for another round of large-scale protests on Friday April 5 and seem to maintain their calls for structural political reform. The size and scope of these protests will give an indication of whether the wider population feels that genuine progress has been made by the government in terms of addressing their political demands. Should protest action retain the same level of intensity over the next several weeks, then we would expect the political leadership to put forward further, albeit, still-limited concessions to appear inclusive and pro-reform. Our core view at Fitch Solutions remains for such concessions to eventually help quell the current wave of unrest. However, the longer the protests continue, the greater will be the risk of a more abrupt political transition in in the form of a popular overthrow or military coup.

Related Research:

- *'Algeria Crisis: Prospects For Political Change', March 19 2019*
- *'Sweeping Security Reforms Heighten Algeria's Succession Risks', January 14 2019*