EGYPT

Highlights

- **Growth has slowed in the fiscal year 2019-20.** The Covid-19 crisis has contributed to a sharp rise in unemployment, but inflation has slowed, a primary surplus was achieved, and the current account deficit narrowed.
- **In response to the Covid-19 crisis, the authorities took a range of measures.** The government introduced a stimulus package and fast-tracked the release of overdue payments to contractors and export subsidies. The Central Bank of Egypt (CBE) announced a new debt relief initiative for those at risk of default, and issued loan guarantees to banks to on-lend to private sector companies active in the manufacturing, agriculture and contracting sectors.
- **Structural reforms advanced.** The government continued with subsidy reform through increases to electricity and public transport prices, and a series of laws were passed, including the new Banking and Central Bank Act, the SME law, the Unified Economic Operators Registry Act, and amendments to the Sovereign Fund Law and the Public Enterprises Act.

Key priorities for 2021

- **The authorities should step up measures to promote alternative water solutions.** Water security is at the forefront of Egypt's national security. To stem the worsening of its water shortage, systematic investments are required to promote efficient water utilisation in agriculture, industry and beyond.
- **Further steps to strengthen competition and promote a level playing field are needed.** Approving the revised Competition Law would ensure the institutional independence of the Egyptian Competition Authority and empower it to regulate mergers and acquisitions that meet certain thresholds.
- **Upgrading digital infrastructure and advancing digitisation would create much-needed job opportunities in a post-Covid-19 world.** The Covid-19 crisis has accelerated the move to remote working, online education and e-government services, and there is now an urgent need to upgrade available platforms.

Main macroeconomic indicators %

	2016	2017	2018	2019	2020
GDP growth	4.3	4.1	5.3	5.6	3.6
Inflation (average)	10.2	23.5	20.9	13.9	5.7
Government balance/GDP	-12.5	-10.4	-9.4	-7.4	-7.5
Current account balance/GDP	-6.0	-6.1	-2.4	-3.6	-3.2
Net FDI/GDP [neg. sign = inflows]	-2.0	-3.3	-3.0	-2.6	-1.7
External debt/GDP	16.8	33.4	37.0	36.0	34.4
Gross reserves/GDP	5.1	13.0	17.4	14.5	10.3
Credit to private sector/GDP	26.3	28.3	24.4	22.9	25.0

* Fiscal year is July-June.

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Covid-19: macroeconomic implications

GDP growth slowed in the fiscal year 2019-20. The economy grew by 3.6 per cent, versus 5.6 per cent in the previous fiscal year and well below the initial target of 6.0 per cent. Growth in the first half of the fiscal year, before the Covid-19 crisis, was 5.6 per cent year-on-year, declining slightly to 5.0 per cent in the third quarter. In the last quarter (April to June 2020), GDP contracted by 1.7 per cent year-on-year, when a lockdown was imposed, thus negatively affecting both private consumption and investment. Unemployment rose sharply to 9.6 per cent in this quarter, reflecting the economic impact from the Covid-19 crisis on labour-intensive sectors, such as tourism. Inflation slowed to 3.7 per cent year-on-year in September 2020, reflecting a decrease in food prices and lower housing costs and utilities inflation. In a pre-emptive move to support the economy in the face of the Covid-19 crisis, the CBE cut its policy rate by 300 basis points in March 2020 and another 50 basis points in September 2020, the lowest level since early 2015.

The fiscal position continued to improve, despite the Covid-19 crisis. The budget deficit remained around 7.5 per cent of GDP in fiscal year 2019-20, slightly above the initial target of 7.2 per cent of GDP. The crisis saw tax revenues fall because of exemptions provided to businesses as part of the pandemic mitigation measures, but this was partly offset by strong revenues from state-owned enterprises (SOEs) and banks. Spending on subsidies declined, as most petroleum products have been indexed to actual procurement costs since April 2019, resulting in a sharp fall in energy subsidies. Overall, a primary surplus was achieved in the fiscal year 2019-20, amounting to 1.8 per cent of GDP. The latter, coupled with robust growth, led to a decline in the public debt-to-GDP ratio to 86.1 per cent.

External imbalances have fallen, but reserves declined. The current account deficit narrowed to 2.6 per cent of GDP in the first three quarters of fiscal year 2019-20 as imports fell due to weak commodity prices, the impact of Covid-19 and related measures on incomes and consumption, and supply disruptions. Exports also declined, as well as tourism revenues. Inflows of foreign direct investment to Egypt declined to US$ 2.1 billion in the same period. International reserves have dropped to US$ 38.4 billion in September 2020, but continue to comfortably cover over six months of imports.

Covid-19-related measures will hold back growth in the first half of the fiscal year 2020-21. GDP growth is projected at 3.5 per cent in the fiscal year 2020-21, due mainly to the weak outlook in the tourism sector, disruptions in global value chains, weaker demand from trading partners and the slowdown in foreign direct investment. However, large public construction projects and the boom in the telecommunications sector have so far sustained growth. The main risks to the outlook arise from the need for a tougher lockdown should the spread of Covid-19 accelerate, and from the negative outlook in Egypt's main trading partners.

Policy response to Covid-19

In response to the Covid-19 crisis, the government undertook a range of measures. A stimulus package of EGP 100 billion (US$ 6.4 billion) was announced in March 2020, of which EGP 50 billion (US$ 3.2 billion) was dedicated to the tourism sector. The petroleum and tourism ministries gave airlines a US$ 0.10-per-gallon discount on fuel, and several airlines were reportedly in negotiations with the government in pursuit of measures to mitigate the economic repercussions of the pandemic, including talks with banks and Egypt's Sovereign Wealth Fund over potential stake sales and zero-interest loans. Fiscal measures introduced by the government included: lower energy costs for the industrial sector; real estate tax relief for the industry and tourism sectors; an extended moratorium on agricultural land tax for two years; reduced stamp duty on transactions and dividend tax; postponed capital gains tax; and deferred utility payments for tourism and airline companies. On the social front, the government expanded Takaful and Karama (the national social protection programmes) to reach more families; and implemented a targeted support initiative for irregular workers (EGP 500, or US$ 32, in monthly grants for three months).

The CBE has also intervened with crisis-mitigation measures. In March 2020, the CBE increased the limit for electronic payments via mobile phones, announced a new debt relief initiative for those at risk of default, implemented an EGP 20 billion (US$ 1.3 billion) stock-purchase

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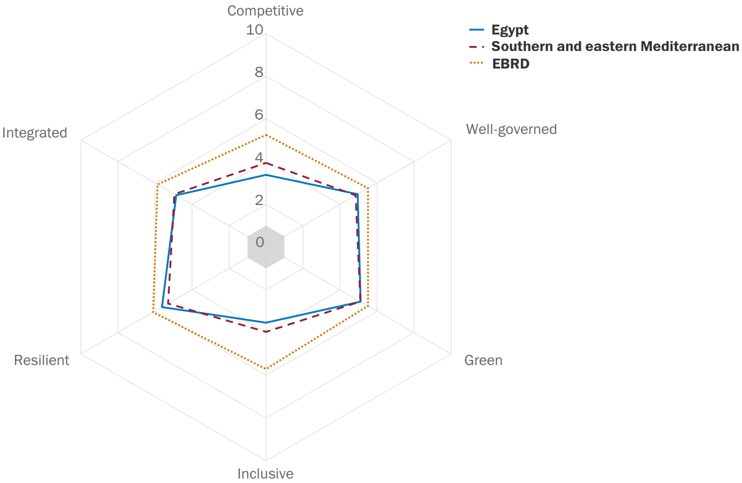
programme, suspended blacklists of loan defaulters, and provided loans with two-year grace periods to the aviation sector. The CBE also issued EGP 100 billion (US$ 6.4 billion) in loan guarantees to banks to on-lend to private sector companies active in the manufacturing, agriculture and contracting sectors, in addition to a EGP 3 billion (US$ 190 million) guarantee on three-year loans to tourism companies and hotels at a subsidised rate of 5 per cent with a one-year grace period.

Assessment of transition qualities (1-10)



Structural reform developments

A new International Monetary Fund (IMF) programme is in place. The programme, a US$ 5.2 billion one-year standby arrangement, was signed in June 2020. Coupled with a US$ 2.8 billion rapid financing instrument approved by the IMF in early May, this will help the government tackle the economic impact of the Covid-19 crisis and reinforce the progress on macroeconomic stabilisation and structural reforms carried out under the previous US$ 12 billion extended fund facility (EFF), which ended in 2019. The new programme's primary focus will be on enabling the government to finance spending on health services and social protection by bolstering the balance of payments and the state budget. Among the other pertinent features of the IMF programme is reforming the National Investment Bank, the state development bank, through the hiring of an international auditor to evaluate its financial position.

The parliament approved a new Banking and Central Bank Act. The legislation, approved in May 2020, gives the CBE increased discretionary powers to regulate the banking sector. Another provision of the law puts the CBE in charge of licensing companies that want to offer credit risk guarantees. The law will also allow the CBE to provide short-term bailout funding to struggling banks. Under the legislation, future boards and chairpersons of state-owned banks will be appointed by the prime minister and will be subject to some form of competency approval from the CBE.

Reforms to subsidies have advanced. In June 2020, the government announced increases in electricity prices, which went into effect in July. Residential users will face an average increase of 19.1 per cent, following a 21.2 per cent rise in July 2019. Electricity prices remain subsidised, and the plan for abolishing electricity subsidies completely was extended from 2021 until 2025. In August 2020, the metro fares on all lines in Cairo were increased by 50 per cent on average, following a previous increase in May 2018. The fuel indexation mechanism that was introduced in 2019 ensures that retail fuel prices remain at cost recovery and that the budget is unaffected through regular quarterly adjustments to reflect changes in world oil prices and movements in the exchange rate.

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The long-awaited SME (small and medium-sized enterprise) law was approved. Under the new law, approved in August 2020, the government will grant tax and custom incentives to the micro, small and medium-sized enterprises (MSMEs) sector. MSMEs will be given preferential tax rates ranging from 0.5 to 1.0 per cent according to the volume of their revenues, and will be excluded from stamp duty taxes and fees for registration of articles of association for five years. The law includes a range of tax exemptions for MSMEs, and provides support in securing land and credit, and in marketing their goods and services. Companies will be entitled to exemptions from stamp duty and fees for company registration, land contracts and credit agreements for five years from the date of their registration and will not be liable for capital gains tax. The law will also create a special income tax regime for MSMEs. One of the key advantages cited for the new law is that it would help MSMEs to gain better access to credit, as the process of formally registering these businesses for tax purposes would make it easier for banks to make risk assessments.

The Sovereign Fund Law and the Public Enterprises Act have been amended. The amendments, approved by parliament in June 2020, provide value-added tax refunds to any company that is more than 50 per cent owned by the Sovereign Fund of Egypt (SFE) and its sub-funds, and limits the scope of legal action that can be taken against the fund, shielding the SFE and its co-investors from third-party lawsuits. The Public Enterprises Act amendments reclassify listed companies in which the government holds up to a 75 per cent stake and brings them within the scope of the Companies Act, introduces a cap on board compensation, and puts in place new regulations requiring SOEs to provide evidence that their subsidiaries are economically viable.

JORDAN

Highlights

- **The economy is being impacted by the Covid-19 crisis.** The pandemic and related containment measures have led to a deteriorating fiscal balance, rising public debt and a further increase in the already-high rate of unemployment.
- **The authorities have implemented a range of fiscal, social and monetary measures to combat the crisis.** The Central Bank of Jordan (CBJ) increased liquidity and lowered interest rates, while the government postponed tax and other contributions, and allocated support to those sectors and segments of the economy most in need.
- **The authorities have agreed a new programme with the International Monetary Fund (IMF).** The third consecutive IMF-supported programme since 2012 will help the authorities build on the implementation of the authorities' five-year matrix, launched at the 2019 London Initiative.

Key priorities for 2021

- **Swift implementation of key reforms envisaged under the IMF-supported programme are necessary.** These include electricity tariff reform, labour market reforms and improvements in governance to strengthen public sector transparency and accountability.
- **Improving the fiscal situation is needed to stabilise public debt and bring it towards more sustainable levels.** Broadening the tax base, reducing tax exemptions, overhauling investment incentives and reforming the governance of tax and customs administrations should be complemented by spending containment and subsidy reforms, in addition to improving the targeting of social safety nets.
- **Implementation of the government's anti-corruption campaign should be prioritised.** The newly empowered Integrity and Anti-Corruption Commission (JIACC) should pursue corruption-related issues, especially those related to tax evasion, money laundering, abuse of power and embezzlement.

Main macroeconomic indicators %

	2016	2017	2018	2019	2020 proj.
GDP growth	2.0	2.1	1.9	2.0	-6.0
Inflation (average)	-0.6	3.6	4.5	0.8	0.5
Government balance/GDP	-3.7	-3.6	-4.7	-6.0	-9.1
Current account balance/GDP	-9.7	-10.6	-6.9	-2.3	-6.8
Net FDI/GDP [neg. sign = inflows]	-3.9	-4.9	-2.2	-1.8	-1.7
External debt/GDP	65.1	68.4	67.9	68.0	n.a.
Gross reserves/GDP	38.9	37.6	33.9	34.6	n.a.
Credit to private sector/GDP	75.2	79.3	80.9	81.4	n.a.

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Covid-19: macroeconomic implications

The economy is being hit by the crisis. After just 2.0 per cent growth in 2019, GDP decelerated further to 1.3 per cent year-on-year in the first quarter of 2020 and contracted by 3.6 per cent in the second quarter. Tourism, usually a major driver of growth, declined by 62 per cent in the first half of 2020, directly impacted by the Covid-19 crisis. The unemployment rate increased to 22.9 per cent in the second quarter of 2020, but annual inflation has remained low in the first eight months of 2020, at an average of 0.5 per cent.

The fiscal balance deteriorated, and debt is approaching 100 per cent of GDP. The overall fiscal deficit (excluding foreign grants) widened to 7.3 per cent of GDP in the first quarter of 2020, from 5.0 per cent in the same period of 2019, reflecting the drop in non-tax revenues and higher current expenditure (and despite the increase in tax revenues and lower capital expenditures). Public debt remains elevated at 95.4 per cent of GDP. Meanwhile, the current account deficit narrowed to 4.2 per cent of GDP in the first quarter of 2020, down from 4.6 per cent a year earlier. The reduction was driven by the decrease in imports of goods, which more than compensated for the decline in exports. Gross official reserves increased in September 2020 after the issuance of the US$ 1.75 billion Eurobonds and reached US$ 17.9 billion, covering more than 10 months of imports.

Monetary policy has been accommodative. The CBJ continued to lower interest rates in 2020, following three cuts in 2019. The two cuts to the main policy rate in March, by a cumulative 150 basis points, were a response to the growing Covid-19 crisis, and in line with interest rate changes in the United States of America and in regional markets, given the Jordanian dinar peg to the US dollar and the comfortable level of reserves.

Negative growth in 2020 should be followed by a recovery in 2021. We currently project that GDP will fall by 6.0 per cent in 2020, due mainly to the contraction in tourism and cross-border trade. Growth is expected to pick up again in 2021 to 4.0 per cent, sustained by the lower cost of imported energy, increased finance provided to small and medium-sized enterprises (SMEs) under various schemes from the CBJ, and reforms anchored in the new IMF-supported programme. Risks to the outlook include an erosion of real competitiveness stemming from the strengthening of the dinar (in light of the peg to the US dollar). Regional instability, delays in reforms in the run-up to the parliamentary elections in November, and the possibility of slower-than-expected recovery of partner economies also pose risks to the outlook.

Policy response to Covid-19

In response to the Covid-19 crisis, the authorities implemented a range of fiscal, social and monetary measures. In March 2020, the CBJ introduced several measures. It allowed banks to postpone the credit facilities instalments granted to clients of sectors affected by the virus, waived penalties on bounced cheques and pumped JOD 550 million (US$ 776 million) in additional liquidity to the banks by reducing the compulsory reserve ratio on deposits with banks from 7 per cent to 5 per cent. At the same time, the government postponed until the end of 2020 the collection of sales tax on all domestic sectors, imports related to health, and the supply of medicines. It also allocated 50 per cent of the maternity insurance revenues (JOD 16 million or US$ 23 million equivalent) to material assistance for the elderly and the sick, introduced price ceilings on essential products, postponed 70 per cent of the value of customs duties for selected companies, and reduced social security contributions from private sector establishments. In addition, it allocated up to JOD 30 million (US$ 42 million) to the tourism sector and JOD 150 million (US$ 212 million) in liquidity to enable the private sector to continue the production process with efficiency and revitalise the economy.

Support to SMEs has been stepped up during the crisis. The Jordan Loan Guarantee Corporation guaranteed JOD 500 million (US$ 705 million) under a Finance Facilitation Programme for SMEs, which was later expanded to include larger firms. Moreover, the Jordan Enterprise Development Corporation launched two programmes aimed at providing small and medium-sized and industrial enterprises in sectors directly affected by, or involved in responding to, the epidemic with a total of JOD 680,000 (US$ 960,000) in funding.

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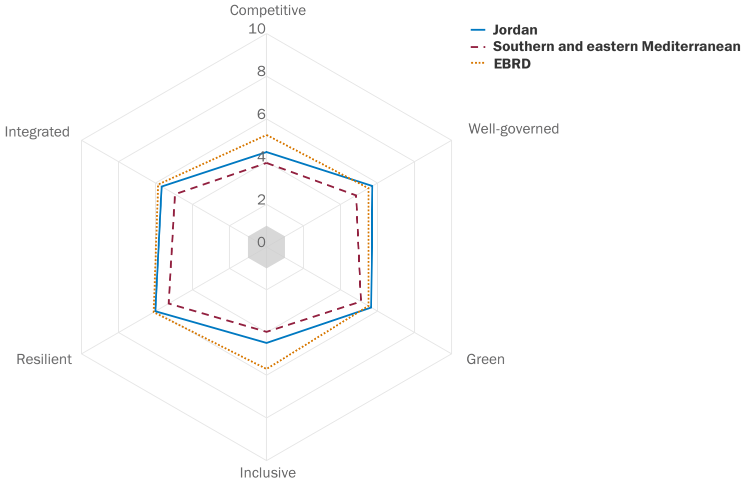
Assessment of transition qualities (1-10)



Structural reform developments

A new IMF programme has been signed. The new programme, approved by the IMF board in March 2020, is a four-year US$ 1.3 billion Extended Fund Facility. This is the third consecutive IMF-supported programme since 2012. The new programme aims at achieving stronger and more inclusive growth and creating jobs, with implementation centred on growth-enhancing structural reforms and a gradual reduction in the budget deficit. Key reforms envisaged under the programme include electricity tariff reform, labour market reforms to promote greater employment opportunities for women and young people, and the swift implementation of the authorities' five-year matrix, launched at the 2019 London Initiative, to improve the business climate, boost competitiveness, and attract foreign investment. These efforts are supported by governance reforms to strengthen public-sector transparency and accountability. The IMF also approved in May 2020 Jordan's request for emergency financial assistance under the Rapid Financing Instrument, equivalent to US$ 396 million, to cover about a quarter of Jordan's external financing needs stemming from the Covid-19 shock.

An ambitious green growth plan has been launched. The National Green Growth Plan 2021-25, launched in July 2020, is part of a broader national drive towards a green economy and sustainable development. It comprises executive plans targeting the key sectors of water, waste management, energy, agriculture, tourism and transport. In part, the blueprint is intended to help build sustainable sectors that are more resilient and adaptive to adverse phenomena, including climate change and the fallout of emergencies, such as the coronavirus pandemic. It was drawn up in collaboration with the Global Green Growth Institute. Already, the government has cut taxes on cars imported into Jordan's free zones, including eliminating a weight tax on vehicles and lowering customs duties on electric vehicles.

A new legislative framework for public-private partnerships (PPPs) is in place. The new legislation, which came into effect in August 2020, strengthens the identification, approval, implementation and evaluation process of PPPs in several ways. Under the new rules, the PPP unit is moved to the prime minister's office, a new ministerial committee will select suitable projects and refer them to cabinet, and another committee will assess contingent liabilities and thereby financial risk to the government. The new legislation also ends the exemption under the previous law of the water and energy sectors, which had hindered sound project selection and risk analysis.

The government has launched an anti-corruption campaign. As part of the campaign, the government approved in June 2020 a draft law amending the Integrity and Anti-Corruption Law of 2020. The campaign is targeted against former officials, businesspeople and companies

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suspected of tax evasion, money laundering, abuse of power and embezzlement. The government also announced that tax evasion would be treated as money laundering, which carries a harsher sentence. The amendments to the law give the Integrity and Anti-Corruption Commission (JIACC) more financial and administrative independence to enable it to perform its duties and enhance its capabilities in pursuing corruption-related issues. They also give the JIACC the right to conduct investigations related to money-laundering crimes resulting from corruption cases and to reconcile with those who commit these crimes if they return the money they obtained.

A new agricultural strategy has been announced. The Ministry of Agriculture announced the 2020-25 National Agricultural Development Strategy in August 2020. The strategy focuses on the restructuring and digitisation of the agricultural sector, the utilisation of modern technology, enhancing production and productivity, focusing on strategic crops, and developing the logistics chain of operations. It also prioritises uplifting the agro-processing chain, developing the export chain, and expanding forest and pasture areas.

LEBANON

Highlights

- **Lebanon has entered a deep economic crisis.** The pound is depreciating sharply, the government is struggling to manage the parallel foreign exchange market, inflation continues to spiral, and current economic trends point to hyperinflation and further economic decline.
- **A default on external debt occurred in March 2020, and all credit rating agencies downgraded Lebanon's sovereign ratings.** Major sources of external funding have dried up, including non-resident deposits, remittances and foreign direct investment, and all major ratings agencies have downgraded the sovereign rating.
- **Some reforms have advanced, but progress has been slow.** Several reforms requested by the International Monetary Fund (IMF), as part of their discussions with the government, have started, including auditing the central bank and embarking on subsidy reforms. Other reforms have stalled, notably the passage of a capital control law and the reform of the ailing electricity sector.

Key priorities for 2021

- **Agreeing on an IMF-supported stabilisation and structural reform programme is essential.** The priority should be to rebuild credibility though implementing concrete actions to reach an agreement with the IMF. This will need to include banking sector restructuring and restructuring of the government's debt obligations following its default on Eurobond payments in March. The reform programme should also involve other international financial institutions to ensure complementarity and coordination and help unlock around US$ 11 billion in commitments pledged during the CEDRE conference in 2018.
- **A social safety net needs to accompany the reform programme.** The sharp drop in economic activity, coupled with the exchange rate depreciation, record inflation and the Covid-19 crisis, have led to a surge in unemployment and poverty. There is a need to set-up a targeted social safety net to provide support for the most vulnerable segments during the painful reform process.
- **The campaign to combat corruption needs to take place, and a programme to recover stolen assets is essential.** Protests in October 2019 were triggered by discontent towards corruption in the ruling parties. Combating corruption needs to happen at all levels, starting from tax and revenue collection and procurement.

Main macroeconomic indicators %

	2016	2017	2018	2019	2020 proj.
GDP growth	1.5	0.9	-1.9	-6.7	-22.0
Inflation (average)	-0.8	4.5	4.6	2.9	80.0
Government balance/GDP	-8.9	-8.6	-11.3	-10.5	-16.5
Current account balance/GDP	-23.5	-26.3	-28.2	-27.4	-16.3
Net FDI/GDP [neg. sign = inflows]	-3.1	-2.3	-3.7	-3.6	0.5
External debt/GDP	182.1	190.3	192.8	197.8	n.a.
Gross reserves/GDP	78.6	76.5	66.4	45.7	n.a.
Credit to private sector/GDP	103.8	107.4	100.3	89.4	n.a.

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Covid-19: macroeconomic implications

Lebanon is embroiled in multi-dimensional economic crises. The economy is estimated to have fallen into a recession of -6.7 per cent in 2019, reflecting regional and domestic political uncertainties, social unrest, slow implementation of reforms and lower capital inflows. Expectations for 2020 are even worse, as a deeper recession is exacerbating unemployment and poverty. The unemployment rate is estimated to be above 40 per cent, and 75 per cent of the population could be living below the poverty line by the end of 2020. The pound has continued to depreciate and the central bank is struggling to manage the parallel foreign exchange market. The official pegged exchange rate (of 1,507.5 Lebanese pounds per US dollar) is being used only for vital imports, while the rest of the economy is subject to multiple exchange rates in the parallel market, often reaching 9,000 Lebanese pounds per US dollar.

Inflation continues to spiral. Annual inflation reached record levels of 120 per cent in August 2020 year-on-year, as the pound continued to depreciate. Given Lebanon's import dependence, the depreciation, coupled with dollar shortages, is making imports more expensive and difficult to get. Food and non-alcoholic beverages were the main drivers of inflation, in addition to rising prices of clothing and footwear, furniture, household equipment and transport. Following the August 2020 explosion, imported building materials are in high demand requiring fresh dollars thus putting pressure on those imports. At the same time, purchasing power is quickly evaporating, notably for the many Lebanese earning in local currency and spending in US dollars on imported goods.

Lebanon has ceased servicing all of its external debt. This decision in March 2020, together with the ongoing political, economic and social crisis, contributed to a narrowing in the fiscal deficit. Revenues declined, with both non-tax and tax revenues dropping significantly due to a worsening economic crisis. Expenditures also fell, mainly owing to lower debt service costs, traditionally the main expenditure component; and to a decline in transfers to Electricité du Liban (EdL), usually around 4 per cent of GDP. The debt-to-GDP ratio reached 175 per cent at the end of 2019, and is rising further as the economy is collapsing. Meanwhile, Lebanon is struggling to access capital markets and is opting for domestic borrowing, with domestic debt accounting for approximately two-thirds of total debt (evaluated using the official exchange rate).

External imbalances remain wide. The current account deficit was over 20 per cent of GDP in 2019, one of the highest in the world. This was due to the continued appreciation of the real effective exchange rate (5.5 per cent year-on-year in December 2019) and a large import bill (59.3 per cent of GDP), which was only partially compensated for by exports of services (25.5 per cent of GDP) – mainly tourism and financial services. The external situation deteriorated further in the first half of 2020, with an additional 77 per cent appreciation in the real effective exchange rate and a 13 per cent decline in non-resident deposits compared with the end of 2019. The foreign currency reserves of Banque du Liban (BdL) dropped by 26 per cent year-on-year in August 2020 to US$ 22.8 billion, as the foreign currency was used to subsidise a basket of essential imports. The actual net assets of the BdL are estimated to be negative.

The outlook remains uncertain and the recovery depends on the speed of implementation of reforms. A further contraction of 22 per cent is expected in 2020 - the result of the ongoing economic crisis, the default on debt repayments, the Covid-19 crisis and the associated containment measures, in addition to the August 2020 warehouse explosion, which caused enormous damage. A recovery in 2021 is contingent on the government embarking on a comprehensive economic reform programme in collaboration with the IMF and in the context of an IMF programme, including debt restructuring, which would lead to increased international support and follow-up on the CEDRE commitments. However, any delay in the implementation of reforms will lead to a fourth successive year of deep GDP contraction.

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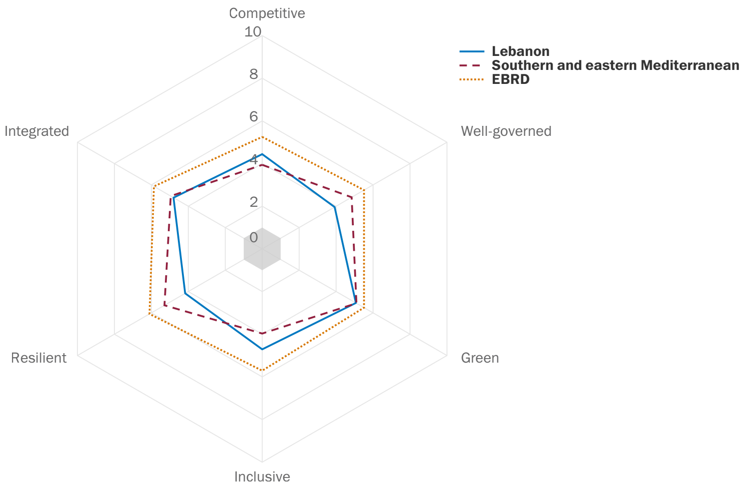
Policy response to Covid-19

In response to the Covid-19 crisis, the authorities undertook a variety of measures. In March 2020, the government established a national solidarity fund, accepting in-kind and monetary donations. It also allocated LBP 1.2 trillion (US$ 796 million at the official rate) for social support, extended all deadlines related to payment of taxes and fees, and provided a solidarity basket of food, sanitisers and financial assistance of LBP 400,000 (US$ 265 at the current official rate) to families most in need. Some of the announced measures were likely not implemented, attracting criticism. A BdL circular in March 2020 allowed banks and financial institutions to extend exceptional five-year zero per cent interest rate loans in Lebanese pounds or US dollars to customers that already have credit facilities but were unable to meet their obligations, operating expenses, or pay salaries to their employees during March, April and May 2020. The BdL also reduced the Beirut Reference Rate in April 2020 to 5.75 per cent for US dollars and 7.75 per cent for Lebanese pounds, and suspended US dollar withdrawals until the airport reopens.

Assessment of transition qualities (1-10)



Structural reform developments

Lebanon has entered discussions for an IMF-supported programme. The discussions began in April 2020. However, progress has been slow and did not progress to negotiations, with almost none of the reforms requested by the IMF fully implemented. The discussions were placed on hold subsequently in July 2020 and the IMF has made it clear it is ready to resume discussions once the government agrees on a common approach towards – and starts implementing – reforms in key sectors. Without the IMF's backing, Lebanon will likely be unable to gain access to external financing, as creditors will want to see a firm commitment to reforms.

The authorities have made progress on some of the reforms urged by the IMF in advance of a programme and major international counterparts. Audits of BdL have been launched, while a capital control law was drafted awaiting parliamentary approval. In July 2020, the cabinet chose a US-based company for the forensic audit of BdL, while two other companies were selected to carry out the accounting audits. In early July 2020, a capital control draft law was introduced in parliament after taking into account comments from various parties. Formal capital controls could help Lebanon curb currency depreciation and rapidly decreasing foreign reserves which follows *de facto* capital controls by the banking sector starting in late 2019. Given the fiscal constraints, the government needs to reform the electricity sector. Some progress was recently made with the appointment of a new board of directors of EdL,

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the state-owned utility, but the appointments were criticised by several groups who viewed these as still reflective of sectarian affiliations. Subsidy reforms continued, with the increase in the price of subsidised bread in June 2020. For the first time since October 2019, bread prices increased by 33 per cent, after previous weeks saw long lines in front of bakeries as some owners had decreased production due to the rising costs of imports. Meanwhile, reforming the electricity sector and subsidies will require a concerted effort by the government.

A new trade finance fund has been launched. Cedar Oxygen, a US$ 175 million independent Trade Finance Impact Fund supported by BdL, was launched in July 2020 to provide trade finance solutions to manufacturing companies. The support of the industrial sector through Cedar Oxygen aims to stabilise the economy and the banking sector, and ultimately attract foreign capital investments to Lebanon. Cedar Oxygen will be working in partnership with selected Lebanese banks, which will identify those eligible for financing.

MOROCCO

Highlights

- **The economy is contracting in 2020 as a result of the Covid-19 crisis and related containment measures.** Unemployment is growing, the fiscal deficit is widening and public debt is increasing, but inflation has remained low.
- **To combat the Covid-19 crisis, the authorities implemented a range of response measures.** A US$ 1 billion special fund was established, the government announced a programme to support micro, small and medium-sized enterprises (MSMEs) in certain sectors, and Bank Al-Maghrib extended credit lines guaranteed by the Central Guarantee Fund.
- **The government has advanced structural reforms.** A draft law on crowdfunding was submitted to parliament, a national programme for water was signed, a new strategy for the agricultural sector was launched and the government announced a fiscal stimulus package.

Key priorities for 2021

- **Reforms to achieve digital transformation are urgent in light of the Covid-19 crisis.** Measures are needed to promote the universal access to telecommunications and broadband networks and provide opportunities for the digital transformation of enterprises and administration. The focus should also be on e-government and digital and financial services access for small and medium-sized enterprises (SMEs) and entrepreneurs.
- **Measures to improve the banks' lending portfolios need to be prioritised.** The value of outstanding bank loans is rising, reflecting the government's efforts to ensure continued bank credit availability for borrowers and avert repayment difficulties during the Covid-19 crisis. The quality of banks' lending portfolios appears to be deteriorating, and, coupled with the rising cost of risk for banks, this suggests that systemic stresses in the banking sector need to be mitigated.
- **There is a need to promote trade integration and global value chains.** This would be achieved through removing current impediments to trade integration, boosting trade agreements with the European Union, sub-Saharan Africa and the Arab Maghreb Union, and defining appropriate policies and support to global value chains.

Main macroeconomic indicators %

	2016	2017	2018	2019	2020 proj.
GDP growth	1.0	4.2	3.0	2.2	-5.0
Inflation (average)	1.5	0.7	1.8	0.2	0.7
Government balance/GDP	-4.5	-3.5	-3.7	-4.1	-7.8
Current account balance/GDP	-4.1	-3.4	-5.3	-4.1	-7.3
Net FDI/GDP [neg. sign = inflows]	-1.5	-1.5	-2.4	-0.5	-0.1
External debt/GDP	33.7	35.0	32.1	33.1	n.a.
Gross reserves/GDP	24.3	23.9	20.7	22.3	n.a.
Credit to private sector/GDP	62.5	61.6	60.9	62.4	n.a.

CONTINUES

Covid-19: macroeconomic implications

The economy is contracting as a result of the Covid-19 crisis and related containment measures. Stagnant growth in the first quarter of 2020 was followed by a 13.8 per cent contraction year-on-year in the second quarter. The main sectors affected by the lockdown were retail, tourism, restaurants and construction. The agriculture sector continued to contract because of a drought during the early planting season. Unemployment increased substantially to 12.3 per cent in the second quarter of 2020, but annual inflation remained low at 0.6 per cent on average in the first nine months of 2020, due to a drop in the prices of food and transport.

The fiscal deficit is widening, reflecting the fallout from the Covid-19 crisis. The deficit is expected to reach 7.8 per cent of GDP in 2020, compared with 4.1 per cent in 2019. Both tax and non-tax revenues are decreasing, the result of the disruption of economic activity from the lockdown in key sectors. Meanwhile, fiscal stimulus packages are increasing expenditures, although many of the measures were financed by voluntary donations. Moreover, public debt is expected to increase to 75 per cent of GDP at the end of 2020, and to account for 90 per cent of GDP when including guaranteed debt for public economic agents.

Both imports and exports have fallen, and tourism and remittances are also down. Lower demand for consumption and investment reduced imports in the first half of the year (except food products, which increased because of the drought). Exports also declined, mainly those from the agricultural, agribusiness and automotive sectors, which in recent years were Morocco's largest exports. The most negative economic effects of Covid-19 are the decline in tourism receipts and the fall in remittances. Nevertheless, international reserves increased to US$ 32.0 billion in October 2020, covering over 10 months of imports. Relying on its large reserves, which provide stability to the exchange rate, Bank Al-Maghrib (the central bank) broadened the dirham's fluctuation band in March 2020 to +/- 5 per cent (from +/- 2.5 per cent), and cut interest rates by a cumulative 75 basis points in March and June 2020 in response to the Covid-19 crisis.

The contraction in GDP in 2020 will likely be followed by a robust recovery in 2021. We expect GDP to contract by 5.0 per cent in 2020, before rebounding to 3.5 per cent growth in 2021. The recovery in 2021 may be helped by an expansion in mining, as the decline in China's production of phosphate may benefit Morocco, the world's second-largest producer of this substance. Downside risks include rising social discontent, a slower-than-expected recovery in the main trading partners in Europe, and the continued vulnerability of agricultural production to adverse weather and fluctuations in agricultural commodity prices.

Policy response to Covid-19

To combat the Covid-19 crisis, the authorities implemented a range of response measures. A US$1 billion special fund, financed by the government and by tax-deductible voluntary contributions from public and private entities, was established in March 2020 to cover the costs of upgrading medical facilities and support businesses and households. The government also announced a programme to support MSMEs who manufacture medical products and equipment with up to 30 per cent refunds. Meanwhile, to reduce volatility on the market, the Bank Al-Maghrib called on credit institutions to suspend all distribution of dividends or shareholder profits for the 2019 financial year and reduced the maximum variation thresholds applicable to financial instruments listed on the Casablanca Stock Exchange. Moreover, it created a banking credit line to finance businesses' operational expenses, guaranteed by the Central Guarantee Fund, and tripled the refinancing capacity of banks with Bank Al-Maghrib by providing dirham and foreign exchange liquidity, widening the scope of securities accepted for bank refinancing and extending the duration of loans.

A new fiscal stimulus package is in place. In July 2020 the government announced a MAD 120 billion (US$ 13 billion, 11 per cent of GDP) fiscal stimulus package. The bulk of the package will consist of state-guaranteed bank loans to businesses, including public-sector enterprises. The remaining part will take the form of a strategic investment fund that will finance public-private partnership infrastructure projects. One-third of the total value of the fund will be financed directly from the state budget, while the remaining amount is to be raised from domestic and international institutional investors.

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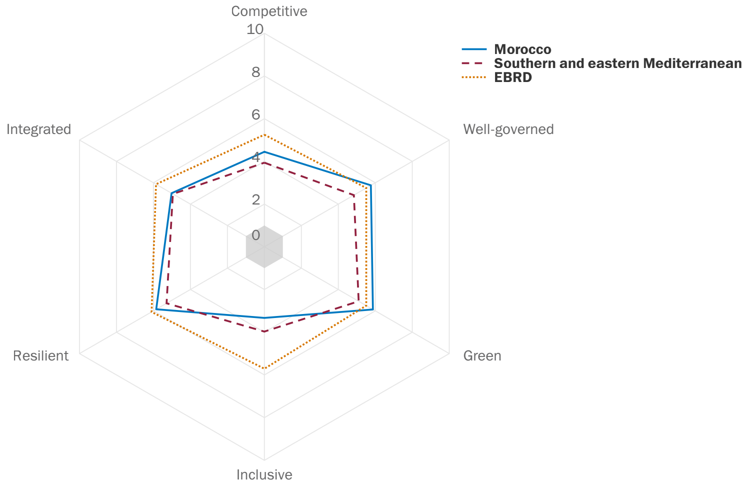
Assessment of transition qualities (1-10)



Structural reform developments

A draft law on the establishment of electronic crowdfunding platforms has been prepared. The new law was submitted to parliament in November 2019. The law, which has been in development since 2017, would allow large numbers of people to finance projects in small increments and allows platform operators to facilitate three different types of crowdfunding transactions: loans, equity investments and donations. The legislation would bolster the availability of financing for micro and small businesses in particular, as well as helping to bring funds from Moroccans living abroad into the national economy. Moreover, this move to introduce crowdfunding comes against a backdrop of wider efforts to boost financial inclusion.

The government fully drew down the US$ 3 billion IMF Precautionary and Liquidity Line (PLL) in April 2020. This is the first time the authorities are drawing on funds available under their fourth consecutive two-year PLL since 2012. The funds were used to maintain an adequate level of official reserves and mitigate pressures on the balance of payments stemming from the economic impact of the Covid-19 crisis.

The preparation of a new development model has been delayed. In December 2019, the King formed a commission, headed by a former interior minister and ambassador to France and comprising 35 members, responsible for designing a new model of socioeconomic development. It consists of a combination of senior political figures, business and public-sector representatives, economists and other specialists and academics, members of civil society organisations, public intellectuals and journalists. Recent signs of socioeconomic and political discontent, as well as the anaemic medium-term economic performance, spurred the need for a new development model. Given the Covid-19 crisis and related measures, the commission has yet to deliver its conclusions and recommendations.

The Green Generation 2020-2030 strategy was launched in February 2020. The new strategy for the agricultural sector aims to create jobs, promote income-generating activities in rural areas, support the agricultural middle class and bolster farming exports and agricultural production, and is based on two pillars. First, it aims to enhance the human element, by promoting the emergence of a new generation of agricultural middle class (some 400,000 households). Second, it encourages young entrepreneurs, through the development of one million hectares of collective land and the creation of 350,000 jobs for the benefit of young people. The new strategy builds on achievements accomplished by the Green Morocco Plan (Plan Maroc Vert), which was launched in 2008 and boosted agricultural exports and investments, created jobs, improved the resilience of agriculture against droughts and contributed to the expansion of SMEs in the agribusiness sector.

TUNISIA

Highlights

- **The economy is contracting significantly in 2020.** The Covid-19 crisis and related containment measures are leading to higher unemployment and rising fiscal deficits, but inflation is lower, foreign exchange reserves are up and the exchange rate is stable.
- **The authorities have responded to the crisis with a wide range of measures.** The government executed an emergency plan, created a fund for health and social spending, and disbursed cash transfers for the most vulnerable segments of the population. The Central Bank of Tunisia (CBT) reduced the policy interest rate by 150 basis points.
- **There has been some progress in structural reforms.** The CBT raised the limits on overseas borrowing by local firms, the interbank guarantee fund for bank deposits started operating, and a new law regulating crowdfunding was approved.

Key priorities for 2021

- **Digitisation of government services should continue.** During the Covid-19 crisis, several digital applications were developed to meet the needs of the administration with a large number of ministries and several online services, such as tax regulation. Increased literacy of the population alongside upgraded digital infrastructure in southern and interior regions will allow digital technology and electronic payments to be applied more widely.
- **Tunisia could benefit from the relocation of European and Asian industry to the southern Mediterranean post-Covid-19.** Tunisia should develop its international positioning to benefit from a wide range of business opportunities. Essential reforms include improving the competitiveness of economic sectors such as health and education, agricultural and agro-food, automotive and textiles.
- **The authorities should commit to further reforms in the energy sector and public administration.** Key reforms on the agenda include a reduction in energy subsidies and streamlining of the civil service wage structure.

Main macroeconomic indicators %

	2016	2017	2018	2019	2020 proj.
GDP growth	1.2	1.9	2.7	1.0	-8.0
Inflation (average)	3.6	5.3	7.3	6.8	5.8
Government balance/GDP	-6.2	-5.9	-4.6	-3.9	-8.1
Current account balance/GDP	-9.3	-10.2	-11.2	-8.5	-8.3
Net FDI/GDP [neg. sign = inflows]	-1.7	-2.0	-2.5	-2.1	-0.6
External debt/GDP	66.9	82.0	86.1	99.4	n.a.
Gross reserves/GDP	14.2	14.1	13.1	19.1	n.a.
Credit to private sector/GDP	76.8	80.3	80.4	77.4	n.a.

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Covid-19: macroeconomic implications

The economy is undergoing a severe contraction. GDP fell by 11.4 per cent year-on-year during the first half of 2020 because of the Covid-19 crisis and related containment measures. The largest contractions were in the tourism, transport, public administration, manufacturing, construction, textiles and trade sectors. Meanwhile, the agricultural and agro-food sectors posted strong positive growth, thanks to a record-breaking olive oil harvest in 2019-20. Unemployment increased to 18 per cent in the second quarter of 2020, the highest rate reported since 2011. Inflation is also quite elevated by regional standards at 5.4 per cent in September 2020, although it is slowing down. The CBT implemented a rate cut of 100 basis points (to 6.75 per cent) in March 2020 in response to the Covid-19 crisis, and by another 50 basis points in October, reversing a trend of monetary tightening to contain inflation.

The fiscal deficit widened and debt increased. The original budget targeted a deficit of 3.0 per cent of GDP for 2020, but the complementary budget forecasts a much higher deficit because the implications of the Covid-19 crisis emerged. In the first eight months of 2020, revenues shrank while expenditures stagnated, as the drop in capital spending offset the increase in interest payments and administrative spending, mainly the public sector wage bill, although an increase in expenditures is projected for the end of the year. Meanwhile, the government's public debt stock increased to 71.4 per cent of GDP at the end of June 2020, and is likely to be higher by the end of the year, given the contraction in GDP and a larger fiscal deficit.

The external accounts have been supported by record olive oil exports and by a lower imports bill due to declining crude oil prices. The current account deficit narrowed to 4.0 per cent of GDP in the first half of 2020, reflecting a larger contraction in imports than in exports. Exports started to rebound in June and July, as did imports in July. Meanwhile, tourism declined by 61 per cent year-on-year in the first eight months of 2020 because of the Covid-19 crisis, and foreign direct investment flows dropped 14.2 per cent year-on-year during the first half of 2020. However, reserves actually increased to US$ 7.6 billion in October 2020, covering 4.7 months of imports.

Negative growth in 2020 should be followed by a recovery in 2021. We forecast GDP growth at -8.0 per cent in 2020 before picking up to 4.0 per cent in 2021. Lower global oil prices and reforms anchored within a new IMF-supported programme are expected to support the economy next year, but risks remain with slow policy reforms and a possible resurgence of the pandemic globally.

Policy response to Covid-19

The authorities responded to the Covid-19 crisis with a range of measures. The government implemented an emergency plan, to which it allocated TD 2.5 billion (US$ 0.9 billion), including value-added tax (VAT) exemptions, VAT refund procedures and reimbursement acceleration, the creation of a TD 100 million (US$ 36 million) fund for the acquisition of equipment for public hospitals, the purchase of emergency medical equipment and medicine, and increasing the strategic food reserve. On the social side, the government disbursed cash transfers for low income households, disabled and homeless people (TD 150 million, US$ 55 million) and support for those in temporary unemployment (TD 300 million, US$ 109 million). It also created investment funds (worth TD 600 million, US$ 219 million) and a state guarantee for new credits (TD 500 million, US$ 182 million). The CBT asked banks to suspend fees for electronic payments and withdrawals, and initiated a mechanism to cover the difference between the policy rate and the effective interest rate on investment loans within a 3 per cent cap.

The CBT is also supporting the recovery. In June 2020 the CBT raised the limits on overseas borrowing by local firms to help them tap other sources of finance and support the recovery from the Covid-19 crisis. This is a welcome step towards foreign exchange control relaxation. Allowing firms to borrow more money from abroad will widen the credit pool and reduce the demand for loans from local banks. The CBT's move will likely increase the flow of foreign credit to Tunisian businesses in the short to medium term, which could potentially allow local corporates to seize more cross-border merger and acquisition opportunities.

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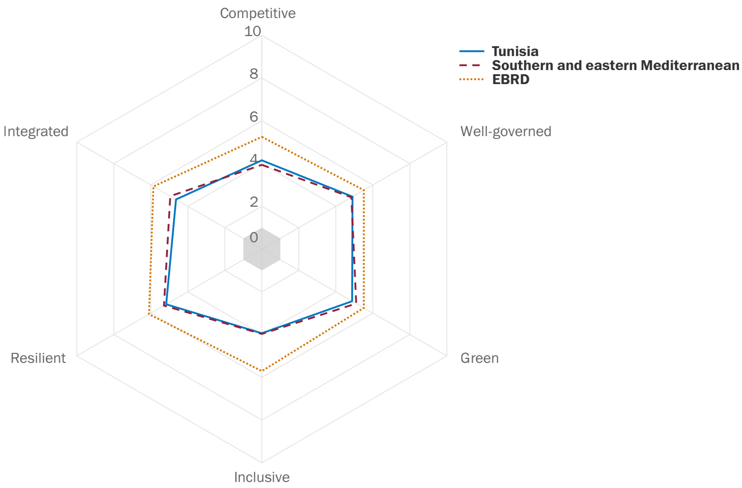
Assessment of transition qualities (1-10)



Structural reform developments

The interbank guarantee fund for bank deposits started operating. Almost all of the 29 banks operating in Tunisia are taking part in this new public body, which began operating in August 2020 and is managed by the state and the CBT. The fund was mandated by the Banking Law of 2016, which brought a number of sizeable amendments to existing rules and regulations and laid out new frameworks. The bank deposit guarantee fund serves to provide reimbursements in cases provided for by law and up to TD 60,000 (US$ 22,000) in case of default or forced administrative liquidation of a bank. The mission of the fund is to protect the savings of bank clients, reimburse them if their deposits become unavailable and contribute to the stability of the Tunisian financial system.

A new law regulating crowdfunding was passed in August 2020. It aims to organise a new means to provide financing – based on raising funds from the public via a dedicated online platform – for projects and companies to promote investment, entrepreneurship, creativity and innovation. The Financial Market Council, the CBT and the Microfinance Control Authority will regulate financing through crowdfunding. This law will help to address some of the economic problems that Tunisia is facing, by introducing new means of financing projects, as the private sector has identified lack of access to finance as one of the main obstacles to doing business.

The authorities implemented direct employment measures to target long-term unemployment, but the feasibility of such a strategy is doubtful. In August 2020 parliament approved a bill that allows the public sector to prioritise recruitment of those aged 35 and over who have been unemployed for more than a decade. Serious questions remain about the feasibility of implementing this law. Tunisia already has one of the highest wage bill to GDP ratios in the world, and several attempts to contain spending and freeze wage increases in previous years faced strong opposition from the powerful labour and trade unions.

Fuel subsidies have been reduced. In March 2020 the government introduced an automatic adjustment mechanism to align domestic prices with the global market price and reduce fuel subsidies. The technical price adjustment committee, set up by virtue of a decree by the energy and finance ministries in March 2020, sets fuel prices each month. The decree outlines that the maximum monthly adjustment step is no more than 1.5 per cent in either direction. As international fuel prices have been falling, the government was able to cut fuel prices for five consecutive months in 2020, with a 1.4 per cent cut on average in August 2020. The reduction in global oil prices is expected to have a favourable effect on Tunisia's energy imports and state budget via a reduction in planned fuel subsidy spending.