One visible sign of the best reform story in the Middle East, perhaps in any emerging market, is the billboards in Cairo advertising the government’s new digital payments system. Designed to raise revenue, reduce corruption, and bring poor citizens out of the financial wilderness, the “Meeza” program distributes benefits on a debit card and collects payments electronically. To this end, the government of retired Gen. Abdel Fattah el-Sisi has installed some 7,000 terminals in government, universities, and other public spaces.

On a recent visit to Cairo we met with tech start-ups, venture capitalists, and corporate executives, and heard time again that the government has “taken all the right steps” to create a more business friendly environment and rein in the swelling deficits. They added that “the guys running the country are brave and making tough decisions” and “the worst seems to be over.” The belt-tightening has largely achieved its objectives, setting the economy up for a strong run. At a time when a secular slowdown in the global economy is lowering the definition of rapid growth (see Tales—Investing in a Four D World, July 2019), any country at Egypt’s stage of development, with an average income under $5,000, is doing well if it is growing faster than 5 percent. And we think Egypt is on track to grow as fast as 6 percent in coming years.

Facing a collapsing currency and runaway inflation after the coup that brought it to power, the el-Sisi government entered a loan agreement with the International Monetary Fund (IMF) in 2016 and has since moved aggressively to meet its conditions. It cut subsidies from 11 percent to 5 percent of gross domestic product.
(GDP)\(^2\), and made deep cuts to civil servant salaries. As a result, the primary balance has improved from a 4 percent deficit to a 1 percent surplus, and public debt has come down from 108 percent of GDP to 88 percent\(^2\). The big fiscal reforms are largely done, but to keep investor confidence up, the government plans to extend the IMF program.

Cairo was buzzing about government investment in large power and infrastructure projects, including 14 new cities, six tunnels connecting Sinai to the Egypt mainland and 7,000 kilometers of new road, some linking the Suez Canal to Cairo. A new capital is rising 30 miles east of Cairo, on a spit of land between the Suez and the Nile, with a new presidential palace. While some critics describe these projects as “Ramses building the pyramids,” many of them serve a purpose larger than ego inflation.

Energy investments have helped Egypt, the largest oil and gas consumer in the Middle East, reduce its dependence on fossil-fuel imports. The current account deficit is down to 2 percent of GDP from a 2017 peak of 6 percent\(^3\). And by 2022, Egypt expects to generate 20 percent of its electricity from local renewable sources\(^4\), which should further stabilize its external balances.

Beyond mega projects, officials of the finance ministry told us that much of the 40 percent increase in public investment since the early 2010s has gone into healthcare and education. The government aims to screen all 100 million citizens for Hepatitis C and other diseases, and to digitize all schools.

As part of its deal with the IMF, the el-Sisi government floated the battered Egyptian pound, which subsequently fell by more than 50 percent to nearly 20 to the US dollar. Though it has since recovered (to 16 to the dollar) the pound still feels cheap, a perception that is drawing in a flood of tourists, and has spurred double-digit growth in exports over the last two years.

Egypt’s longer term aim is to become a low-cost manufacturing hub, a task that will be difficult in the age of deglobalization. Still, the cheap currency and the large domestic market have drawn foreign direct investment from regional players like a Turkish food company that is investing $200 million to expand its biscuit plant, and strong interest from well known Western firms. Big US tech firms are expanding in Egypt, and some are said to be in talks about opening data warehouses. Nonetheless, three CEOs volunteered independently that foreigners were not likely to invest more heavily until private Egyptian companies do, and that has yet to happen in a big way.

We spent a day visiting tech companies, which say Egypt is just starting to move beyond entertainment to wider mobile services. US and other foreign rideshare firms invested heavily in Egypt, introducing millions to mobile apps, and now many of their former employees are moving to local start-ups. Nearly 9 in 10 Egyptians don’t use a bank\(^2\), and fintech firms are starting to sell them hard on mobile banking. E-commerce has also yet to take off, stymied by the cash economy and the logistical nightmare of delivering in Cairo traffic. But the opportunities are so wide that tech execs say that, so long as Egypt is growing faster than 3 percent, they can grow at 100 percent—from a very low base.

It’s not just e-tailers who have had a slow go of it in recent years either. Consumption was boosting GDP growth by 4 to 5 percent a year as recently as 2015\(^5\). Then the big devaluation and

---

\(^3\) Source: Haver. Data as of Dec 2018.
subsidy cuts began to hit consumption, and its contribution fell to just one percent a year\(^6\). At the bottom, a bank exec told us that one beverage distributor marveled that he couldn’t make money selling “the most popular drink in the world, in an incredibly hot country.”

There are signs, however, of a rebound. The final fuel subsidy cut (and price hike) was implemented late last month, so consumers face no further jolt on that front. Some are already trading up to luxury goods, and consumer companies told us their sales volumes have only recently recovered to levels of 2016, before the devaluation. They expect stronger growth from here.

Though the subsidy cuts have fueled headline inflation, which currently stands at 13 percent\(^7\), it is trending downward thanks to the recent appreciation in the pound and weak oil prices. High inflation had compelled the central bank to keep rates high—the overnight lending rate, for example, is still above 16 percent\(^8\). But with inflation easing, the market’s consensus view is that the bank will start cutting rates in coming months, by as much as 3 to 4 percent over the next two years, which should provide a further boost to growth.

All of this has made Egypt a great economic reform story in the eyes of the market, even if the global media still covers it as a regime born in a bloody coup and backsliding toward dictatorship. Markets are never shy about embracing strongmen who generate accelerating growth, but they also sense that economies subject to the whims of an autocrat can be erratic.

We’re optimistic for Egypt, which is now moving past fiscal reform to focus on measures to increase private sector competitiveness, including tax cuts for small- and medium-sized enterprises and land reforms. We’ll be watching progress closely, knowing investors will flee at the first sign that el-Sisi’s reform discipline is faltering. On balance, however, we think Egypt is on track to become a breakout nation.

**Risk Considerations:** There is no assurance that a portfolio will achieve its investment objective. Portfolios are subject to market risk, which is the possibility that the market values of securities owned by the portfolio will decline. Accordingly, you can lose money investing in this portfolio. Please be aware that this portfolio may be subject to certain additional risks. In general, equities values also fluctuate in response to activities specific to a company. Investments in foreign markets entail special risks such as currency, political, economic, and market risks. The risks of investing in emerging market countries are greater than the risks generally associated with investments in foreign developed countries. Stocks of small- and medium-capitalization companies entail special risks, such as limited product lines, markets, and financial resources, and greater market volatility than securities of larger, more-established companies. Derivative instruments can be illiquid, may disproportionately increase losses and may have a potentially large negative impact on the portfolio’s performance. Illiquid securities may be more difficult to sell and value than public traded securities (liquidity risk). Non-diversified portfolios often invest in a more limited number of issuers. As such, changes in the financial condition or market value of a single issuer may cause greater volatility.

**About Morgan Stanley Investment Management\(^9\)**

Morgan Stanley Investment Management, together with its investment advisory affiliates, has 665 investment professionals around the world and approximately $497 billion in assets under management or supervision as of June 30, 2019. Morgan Stanley Investment Management strives to provide outstanding long-term investment performance, service and a comprehensive suite of investment management solutions to a diverse client base, which includes governments, institutions, corporations and individuals worldwide.

For more information, please visit our website at www.morganstanley.com/im. This material is current as of the date specified, is for educational purposes only and does not contend to address the financial objectives, situation or specific needs of any individual investor.

---


\(^7\) Source: Haver. Data as of June 2019.

\(^8\) Source: Bloomberg. Data as of August 2019.

\(^9\) Source: Assets under management as of June 30, 2019. Morgan Stanley Investment Management ("MSIM") is the asset management business of Morgan Stanley. Assets are managed by teams representing different MSIM legal entities; portfolio management teams are primarily located in New York, Philadelphia, London, Amsterdam, Hong Kong, Singapore, Tokyo and Mumbai offices. Figure represents Morgan Stanley Investment Management’s total assets under management/supervision.

**Definitions:** Gross Domestic Product (GDP) is the monetary value of all the finished goods and services produced within a country’s borders in a specific time period. It includes all, private and public consumption, government outlays, investments and net exports. Fintech is an umbrella term for any kind of technological innovation used to support or provide financial services.

**Important Disclosures:** The views and opinions are those of the author as of the date of publication and are subject to change at any time due to market or economic conditions and may not necessarily come to pass. Furthermore, the views will not be updated or otherwise revised to reflect information that subsequently becomes available or circumstances existing, or changes occurring, after the date of publication. The views expressed do not reflect the opinions of all portfolio managers at Morgan Stanley Investment Management (MSIM) or the views of the firm as a whole, and may not be reflected in all the strategies and products that the Firm offers. Forecasts and/or estimates provided herein are subject to change and may not actually come to pass. Information regarding expected market returns and market outlooks is based on the research, analysis and opinions of the authors. These conclusions are speculative in nature, may not come to pass and are not intended to predict the future performance of any specific MSIM product. Certain information herein is based on data obtained from third party sources believed to be reliable. However, we have not verified this information, and we make no representations whatsoever as to its accuracy or completeness. The information herein is a general communications which is not impartial and has been prepared solely for information and educational purposes and does not constitute an offer or a recommendation to buy or sell any.
be considered to be the subject of an invitation for subscription or purchase, whether directly or indirectly, to the public or any member of the public in Singapore other than (i) to an institutional investor under section 304 of the Securities and Futures Act, Chapter 289 of Singapore (“SFA”); (ii) to a relevant financial intermediary under section 305 of the SFA, and such distribution is in accordance with the conditions specified in section 305 of the SFA; or (iii) otherwise pursuant to, and in accordance with the conditions of, any other applicable provision of the SFA. In particular, for investment funds that are not authorized or recognized by the MAS, units in such funds are not allowed to be offered to the retail public; any written material issued to persons as aforementioned in connection with an offer is not a prospectus as defined in the SFA and, accordingly, statutory liability under the SFA in relation to the content of prospectuses does not apply, and investors should consider carefully whether the investment is suitable for them. This material has not been reviewed by the Monetary Authority of Singapore.

Australia: This publication is disseminated in Australia by Morgan Stanley Investment Management (Australia) Pty Limited ACN. 122040337, AFSL No. 314182, which accepts responsibility for its contents. This publication, and any access to it, is intended only for “wholesale clients” within the meaning of the Australian Corporations Act.

Japan: For professional investors, this document is circulated or distributed for informational purposes only. For those who are not professional investors, this document is provided in relation to Morgan Stanley Investment Management (Japan) Co., Ltd. (“MSIMJ”)’s business with respect to discretionary investment management agreements (“IMA”) and investment advisory agreements (“IAA”). This is not for the purpose of a recommendation or solicitation of transactions or offers any particular financial instruments. Under an IMA, with respect to the client’s investment, the client retains the discretion to make investment decisions based on an analysis of the value, etc. of the securities, and MSIMJ accepts such investment. The client shall delegate to MSIMJ the authorities necessary to carry out both the selection of investments which satisfy the client’s investment policy and the making of investment decisions. The client shall not make individual instructions. All investment profits and losses belong to the clients; principal is not guaranteed. Please consider the investment objectives and nature of risks before executing an agreement. This document is disseminated in Japan by MSIMJ, Registered No. 410 (Director of Kanto Local Finance Bureau (Financial Instruments Firms)), Membership: the Japan Securities Dealers Association, The Investment Trusts Association, Japan, the Japan Investment Advisers Association and the Type II Financial Instruments Firms Association.

Morgan Stanley Investment Management, Inc. Marketing Communication: This marketing communication has been issued by Morgan Stanley Investment Management Limited (“MSIM”). Authorised and regulated by the Financial Conduct Authority. In the UK, Morgan Stanley Investment Management is a branch office of Morgan Stanley Investment Management Limited, a company registered in England. Registered No. 1981121. Registered Office: 25 Cabot Square, Canary Wharf, London E14 4QA. The information contained in this communication is not a research recommendation or ‘investment research’ and is classified as a ‘Marketing Communication’ in accordance with the applicable European or Swiss regulation. Msim has not authorised financial intermediaries to use and to distribute this material, unless such use and distribution is made in accordance with applicable law and regulation. Additionally, financial intermediaries are required to satisfy themselves that the information in this document is suitable for any person to whom they provide this document in view of that person’s circumstances and needs. Msim shall not be liable for, and accepts no liability for, the use or misuse of this document by any such financial intermediary. The whole or any part of this work may not be reproduced, copied or transmitted or any of its contents disclosed to third parties without Msim’s express written consent.

All information contained herein is proprietary and is protected under copyright law. Morgan Stanley Investment Management is the asset management division of Morgan Stanley.