November 2018
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Africa Monitor

North Africa

Egypt: Expanding Gas Sector To Support Growth Acceleration

***Key View:** Real GDP growth is set to accelerate in Egypt as exports and investment pick up, boosted by the country's fast-expanding gas sector. Non-hydrocarbon investment and consumption will recover more gradually, as inflation and interest rates remain relatively elevated, keeping Egyptian households and businesses under pressure.*

Forecast Change

- We have revised up our forecast for real GDP growth in Egypt to 5.4% in FY2018/19 (starting July 1), from 5.0% previously, and 5.6% in FY2019/20, from 5.4%.

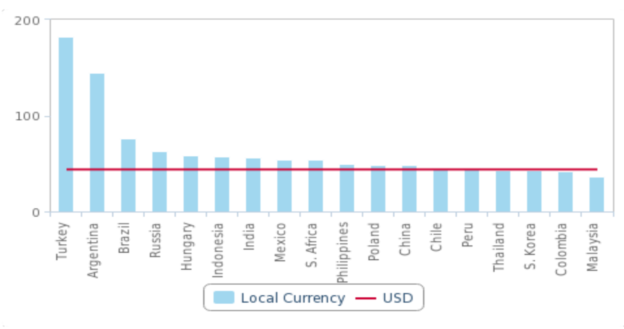
...continued on page 2

Algeria: Political Risk Rising Amid Succession Uncertainty 5

Political risk is increasing in Algeria amid a continued lack of clarity on who will succeed the ageing President Abdelaziz Bouteflika. Policy continuity will be the major area of uncertainty, but we also believe that risks of unrest will rise during the transition process.

Oil Outlook

Currency Depreciation Amplifies Impact Of Oil Rally
Global – One-Year Change In Oil Prices, % LCY & USD



Source: Bloomberg, Fitch Solutions

Oil prices continue to hover just below the key USD80.0 per barrel (/bbl) resistance level, having found strength from market focus on emergent risks on the supply side. Sharp declines in exports from Iran, further deterioration of conditions in Venezuela and outages in the US have driven Brent back up to the high '70s'. Risks to the demand side continue to linger at the periphery of market attention. Global macroeconomic conditions look increasingly challenging, while rising US-China trade tensions and ongoing currency crises in Argentina and Turkey are stoking market fears. We hold to our current forecast of an annual average of USD75.0/bbl for 2018 and USD82.0/bbl for 2019 for Brent, but recognise the growing risk from some of the aforementioned demand dynamics (*see 'Brent: Demand Side Risks Skewed To The Downside, September 10*).

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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	Country
	Political	Economic	Political	Economic	Risk	Risk
Morocco	67.9	48.3	69.9	52.4	52.9	57.7
Tunisia	61.5	32.5	68.6	43.4	46.1	50.1
Algeria	52.3	54.2	54.4	54.5	40.9	49.2
Libya	26.7	40.6	20.2	36.0	28.3	30.0
Regional average	**52.1**	**43.9**	**53.3**	**46.6**	**42.1**	**46.8**
Global average	**63.2**	**53.1**	**62.0**	**53.6**	**49.7**	**55.3**

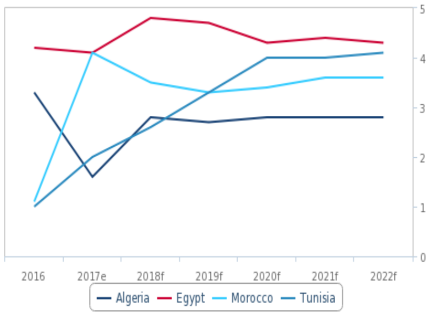
Source: Fitch Solutions

EGYPT – ECONOMIC OUTLOOK

...continued from front page

We forecast real GDP growth to come in at a robust 5.4% in FY2018/19 and 5.6% in FY2019/20. This marks an upward revision from our previous forecasts of 5.0% and 5.4% respectively. This comes on the back of stronger-than-anticipated growth of 5.3% in FY2017/18, primarily boosted by increases in net exports and investment – a trend that we expect will remain in place over the quarters ahead. The natural gas sector will be a key driver of growth, boosting both exports and investment. The Zohr field came online ahead of schedule, and our Oil & Gas team expects a ramp-up to maximum production capacity within the next two years. This, coupled with increasing output from several other offshore fields, will switch Egypt's gas balance from deficit to surplus in 2019 (late-2018 at the earliest), improving the country's external picture. Steady gains in the tourism sector, on the back of improved security conditions and a resumption of flights between Egypt and Russia, will help to further boost exports.

A Regional Outperformer
North Africa – Real GDP Growth, % y-o-y

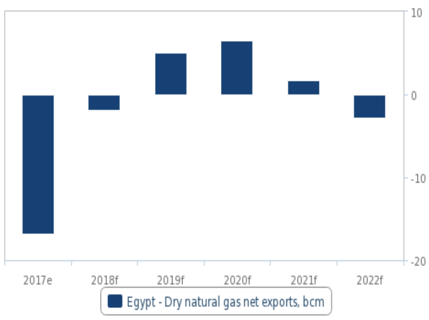


e/f = Fitch Solutions estimate/forecast. Source: National sources, Fitch Solutions

Meanwhile, the high-potential gas sector is also a major bright spot for foreign direct investment: large gas discoveries have been announced in recent months, and efforts are being made to develop Egypt into a regional energy hub – for example through the relaxation of regulations to open up the domestic market to private companies. Non-hydrocarbon activity looks set to pick up at a more gradual pace. The recovery in non-hydrocarbon investment and consumption following the November 2016 currency liberalisation and subsequent spike in inflation has been slow to date. With fresh subsidy cuts on fuel, electricity and piper water implemented in June-July and rising oil prices continuing to fuel inflation, households' purchasing power will remain constrained.

Higher input costs – coupled with restricted credit availability, as the Central Bank of Egypt looks poised to keep its key policy rate at 16.75% till late-2018 – will also ensure domestic investment in non-hydrocarbon sectors remains under pressure. Nevertheless, we do highlight that Egypt's Purchasing Managers' Index re-entered positive territory at 50.3 in July, from 49.4 in June, suggesting that non-hydrocarbon activity will gradually expand over the quarters ahead. Over the medium term, we expect the recovery to pick up pace, as inflation and interest rates fall, and improving overall macroeconomic stability and business environment reforms help to boost consumer and business confidence levels. In a positive sign, unemployment has been falling steadily in recent quarters, officially standing at 10.6% of the labour force in Q118, compared with 11.3% in the previous quarter.

Inflection Point In Natural Gas Budget
Egypt – Natural Gas Supply/Demand Balance, bcm



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

EGYPT – ECONOMIC OUTLOOK

CBE To Err On The Side Of Caution

Key View: *The Central Bank of Egypt (CBE) will keep interest rates on hold in the near term as subsidy cuts fuel a temporary spike in inflation. We forecast just one more cut (late) this year – bringing the overnight lending rate to 16.75% – as dollar strength and rising oil prices encourage the CBE to maintain a cautious stance. We nevertheless expect the broader trend of gradual monetary easing to remain in place over the medium term, facilitated by improving fiscal dynamics and stabilising prices.*

Forecast Change

- We have moderated our forecast for CBE interest rate cuts in 2018, expecting the overnight lending and deposit rates to end the year at 16.75% and 15.75%, respectively, compared with 15.75% and 14.75% previously.

CBE rates are likely to remain on hold in the short term. Following two 100 basis point (bps) cuts in February and March, the CBE has paused its easing cycle as global markets have experienced some volatility (spurring a drop in foreign portfolio investment), as oil prices have rallied, and as the government has introduced a series of IMF-stipulated subsidy cuts. The cuts, in particular – which hiked fuel prices by up to 50%, gas prices by up to 75%, and electricity prices by an average 26% – led inflation to accelerate for the first time in 11 months, reaching 14.4% y-o-y June, compared with 11.4% in May. Rates are likely to remain unchanged over the months ahead, as prices continue to adjust.

We forecast one more cut before end-2018, bringing the overnight lending rate to 16.75%. This compares with a forecast of 15.75% previously. While we had already factored in the effects of subsidy cuts on inflation this year, our Oil & Gas team has made revisions to their oil price forecasts in recent months, now expecting Brent to average USD75.0 per barrel (/bbl) in 2018, compared with USD67.0/bbl previously. Higher oil prices will push transport and utility costs up. In addition, the dollar is strengthening, and risks of faster-than-expected US monetary tightening fuelling global risk-off and weakening the Egyptian pound are on the rise – encouraging greater CBE caution. That said, we still believe annual inflation will fall within the bank's 13% +/- 3% target band for Q418, ending the year around the 13.2% level.

The wider trend of gradual monetary easing looks set to remain in place over the medium term. While the CBE will still look to contain inflation expectations and avoid a scenario in which rapid rate-cutting provokes large-scale capital outflows, improving fiscal dynamics and stabilising prices will enable the bank to walk back the 700bps' worth of cuts it enacted in the aftermath of the 2016 pound liberalisation over the next few years. Easing will further be facilitated by the recovery in foreign exchange reserves (USD44.3bn in June, enough to cover nine months of imports) since 2016, and an expected uptick in foreign direct investment, which will mitigate risks linked to capital flight. Lower interest rates will in turn encourage lending, boosting private consumption and investment.

EGYPT – DATA & FORECASTS

	2014	2015e	2016e	2017e	2018f	2019f	2020f
Nominal GDP, USDbn	300.7	317.3	269.4	194.4	236.8	279.5	325.2
Real GDP growth, % y-o-y	2.2	4.4	4.3	4.2	5.3	5.4	5.5
GDP per capita, USD	3,303	3,725	3,257	2,429	2,856	3,273	3,709
Population, mn	91.81	93.78	95.69	97.55	99.38	101.17	102.94
Consumer price inflation, % y-o-y, eop	10.1	11.1	23.3	21.9	13.2	10.0	9.5
Consumer price inflation, % y-o-y, ave	10.1	10.4	13.7	29.6	15.2	12.1	9.7
Central bank policy rate, % eop	10.25	10.25	16.25	19.75	16.75	13.75	11.75
Exchange rate EGP/USD, ave	7.08	7.70	10.06	17.85	17.88	18.02	18.05
Exchange rate EGP/USD, eop	7.15	7.83	18.14	17.78	17.50	17.90	18.50
Budget balance, EGPbn	-240.4	-267.6	-326.4	-361.9	-415.9	-431.3	-414.6
Budget balance, % of GDP	-11.3	-10.9	-12.0	-10.4	-9.8	-8.6	-7.1
Goods and services exports, USDbn	43.6	44.1	34.8	38.3	47.1	55.3	62.0
Goods and services imports, USDbn	69.0	71.9	66.9	66.9	69.5	75.3	80.8
Current account balance, USDbn	-2.4	-11.7	-19.8	-15.6	-2.5	1.0	3.4
Current account balance, % of GDP	-0.8	-3.7	-7.4	-8.0	-1.0	0.3	1.1
Foreign reserves ex gold, USDbn	15.4	23.0	26.0	27.5	30.2	31.4	33.0
Import cover, months	2.7	3.8	4.7	4.9	5.2	5.0	4.9
Total external debt stock, USDbn	41.8	48.5	67.2	62.7	54.4	52.9	52.3
Total external debt stock, % of GDP	13.9	15.3	25.0	32.3	23.0	18.9	16.1
Crude, NGPL & other liquids prod, 000b/d	549.9	718.0	684.0	657.0	672.2	687.8	695.5
Total net oil exports (crude & products), 000b/d	-252.4	-108.1	-172.9	-159.1	-181.1	-174.0	-174.9
Dry natural gas production, bcm	48.8	44.3	42.1	39.6	58.0	67.3	70.5
Dry natural gas consumption, bcm	48.3	47.8	51.3	56.4	59.8	62.2	64.0

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

MOROCCO – POLITICAL OUTLOOK

Significant Hurdles To ECOWAS Bid Remain

***Key View:** Morocco's application to join ECOWAS underlines the kingdom's ongoing drive to diversify its trade relations and to establish itself as a hub between Europe and Africa. That said, significant obstacles remain, with full accession likely to be several years away at best.*

Morocco's bid to join the Economic Community Of West African States (ECOWAS) is another clear indicator of the country's ambition to broaden its economic relations and become a trade hub between Europe and Africa. We have previously argued that Moroccan authorities are increasingly turning their gaze away from Europe – still the principal source of trade and investment – towards African markets, indicated by Morocco's re-entry into the African Union *(see 'Morocco's AU Readmission To Boost Regional Influence And Trade', February 2 2017)*. The current ECOWAS bid further underscores this point, with membership offering new investment and export opportunities for Moroccan businesses. That said, we note that significant obstacles to accession remain, due to both political and economic concerns, particularly from Nigeria. This implies that membership is likely years rather than months away, and may ultimately be blocked entirely.

ECOWAS Bid Reflects Moroccan Pivot Towards Africa...

Morocco's application to join ECOWAS illustrates the kingdom's ambition to increase its trade and influence in Africa. While much of Morocco's trade and investment has been directed at France, Spain and the US in the past, recent years have seen Moroccan authorities increasingly focus their foreign policy and efforts to expand trade relations on Sub-Saharan African (SSA) markets. King Mohammed VI visited 12 SSA countries in 2017 and H118 alone, bringing along entourages of ministerial attaches and business leaders, and received Nigerian president Muhammadu Buhari for a multi-day visit in June 2018. Buhari's visit resulted in a signed agreement to continue work on a 5,660km gas pipeline between the two countries. The government is also slowly loosening the dirham's peg to the dollar and euro in a bid to improve the country's export competitiveness and facilitate trade beyond traditional markets.

Morocco's export statistics suggest that prior efforts to pivot toward Africa have already started to bear fruit. Africa-bound exports hit 8.8% of Morocco's total exports in 2017, up from 5.0% a decade previously, driven largely by phosphates and fertilisers; ECOWAS-bound exports have seen a similar trend, reaching 3.8% of total exports as of 2017. Africa-bound foreign direct investment (FDI) accounted for 77.5% of total outflows from Morocco in 2017. The majority of FDI outflows from the country are in the banking and telecommunications sectors, at 31.0% and 21.0% respectively in 2015. This has been driven by rapidly growing companies such as Attijariwafa Bank, which had 476 branches in SSA in 2016, up from 322 in 2011. Accession to ECOWAS could enable an acceleration of this trend. Starting in 2013 the group has gradually implemented a common external tariff (CET), with the goal of achieving a full customs union. To the extent that this process continues, accession would give Morocco tariff-free trade with a common market of roughly 350mn consumers. While the purchasing

MOROCCO – DATA & FORECASTS

	2014e	2015e	2016e	2017e	2018f	2019f	2020f
Population, mn	34.32	34.80	35.28	35.74	36.19	36.64	37.07
Nominal GDP, USDbn	109.9	101.3	103.6	109.6	119.6	123.6	124.0
GDP per capita, USD	3,203	2,911	2,936	3,065	3,303	3,372	3,343
Real GDP growth, % y-o-y	2.7	4.5	1.1	4.1	3.5	3.3	3.4
Industrial production, % y-o-y, ave	0.9	0.8	3.0	3.0	3.0	3.0	3.0
Consumer price inflation, % y-o-y, ave	0.4	1.6	1.6	0.8	2.1	1.7	1.5
Consumer price inflation, % y-o-y, eop	1.6	0.6	1.8	1.9	2.5	1.5	1.5
Central bank policy rate, % eop	2.50	2.50	2.25	2.25	2.25	2.75	3.00
Exchange rate MAD/USD, ave	8.42	9.75	10.13	9.33	9.20	9.60	10.00
Exchange rate MAD/USD, eop	9.08	9.93	10.13	9.33	9.20	9.60	10.00
Budget balance, MADbn	-43.6	-41.3	-41.5	-38.0	-39.9	-41.2	-40.0
Budget balance, % of GDP	-4.7	-4.2	-4.1	-3.6	-3.6	-3.5	-3.3
Goods and services exports, USDbn	36.1	33.3	34.3	38.6	45.4	48.2	49.0
Goods and services imports, USDbn	49.7	41.3	45.2	49.3	56.7	59.6	60.1
Current account balance, USDbn	-6.6	-2.2	-4.5	-3.9	-3.7	-3.5	-3.1
Current account balance, % of GDP	-6.0	-2.1	-4.4	-3.6	-3.1	-2.8	-2.5
Foreign reserves ex gold, USDbn	19.7	22.1	24.6	24.3	26.5	28.1	30.5
Import cover, months	5.1	6.8	7.0	6.7	6.0	5.9	6.3
Total external debt stock, USDbn	42.8	43.0	46.3	48.9	51.5	53.0	54.3
Total external debt stock, % of GDP	38.9	42.4	44.7	44.6	43.1	42.9	43.8
Crude, NGPL & other liquids prod, 000b/d	0.5	0.5	0.5	0.5	0.5	0.5	0.4
Total net oil exports (crude & products), 000b/d	-281.7	-283.7	-296.3	-309.9	-324.4	-339.6	-355.3
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. Source: National sources, Fitch Solutions

power of consumers in these markets is far lower than that of traditional European markets – their average GDP per capita (PPP) in 2017 was USD2732.4, compared with USD42779.0 in France – growth opportunities still exist. We highlight phosphates as a key potential export, as it could help supply west Africa's fast-growing agricultural sector. Our Agribusiness team forecasts the market value of Nigeria's agribusiness sector to grow by 6.1% annually over the coming five years, for instance, and the two countries signed an agreement in 2016 that supplies Moroccan phosphates to support an expansion in Nigerian fertiliser production.

... But Accession Far From Certain

Despite the potential benefits of Moroccan membership, we see significant – perhaps intractable – hurdles to accession. A recent impact study by ECOWAS concluded that while a Moroccan membership would be broadly positive, it should only progress gradually to guard existing members against sudden economic shocks. ECOWAS would have to allow Morocco an exemption from the CET, as the kingdom is subject to its own free trade deal with the EU. Alternatively, ECOWAS would have to implement its own economic partnership agreement (EPA) with the EU, which was agreed to in 2014 but has yet to be ratified. Whether through entry into an EPA or re-exports from Morocco, this would subject ECOWAS countries to tough competition from EU manufacturers. Given these risks, we believe that accession will likely take many years to materialise.

We also believe that strong Nigerian opposition raises the risk that a Moroccan membership may not materialise at all. The reason for Nigeria's disapproval is partly political. It is by far the largest economy in West Africa, and as such holds a crucial position as a regional power broker, and while Morocco remains significantly smaller in nominal GDP terms, it would still constitute the second-largest economy in ECOWAS if admitted. This would upset the existing power balance within the group, potentially threatening Nigeria's leading position. Economic concerns also prevail, as Nigeria is the only ECOWAS market with a notable manufacturing sector. Indeed, the Manufacturers Association of Nigeria, a powerful lobby group, has put up stiff opposition to both the EPA and Morocco's ECOWAS bid, indicating a difficult path ahead.

As such, although relations between King Mohammed VI and President Buhari seem warm (the latter endorsed Morocco's recent re-entry into the AU, despite old disagreements about the status of Western Sahara, a disputed territory claimed by Morocco) strong domestic opposition in Nigeria may still push the president to reject Morocco's bid. Because Morocco's entry into ECOWAS would likely require a unanimous decision among current members (as no new members have been admitted apart from Cape Verde, which joined in 1977 just two years after the community's founding), Nigerian opposition would amount to a veto. This raises the risk that Morocco's ECOWAS bid may not progress beyond its current state.

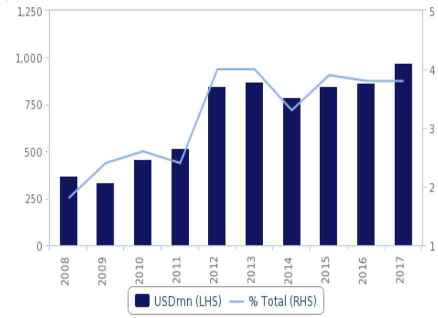
ECOWAS Membership Unlocks West African Market

Africa – Current ECOWAS Members & Applicants

Source: D-Maps, Fitch Solutions

Slow And Steady Growth In ECOWAS Exports

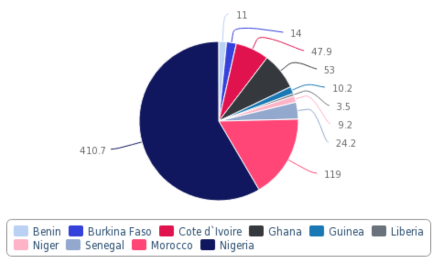
Morocco – Exports To ECOWAS, % Of Total



Source: Trade Map, Fitch Solutions

Nigeria's Economic Dominance Threatened By Moroccan Accession

Select ECOWAS Markets & Morocco – Nominal GDP (2018f), USDbn



f = Fitch Solutions forecast. Source: National sources, Fitch Solutions

ALGERIA – POLITICAL OUTLOOK

Political Risk Rising Amid Succession Uncertainty

Key View: *Political risk is increasing in Algeria amid a continued lack of clarity on who will succeed the ageing President Abdelaziz Bouteflika. Policy continuity will be the major area of uncertainty, but we also believe that risks of unrest will rise during the transition process.*

We believe that uncertainty over the succession of President Abdelaziz Bouteflika is the most pertinent risk to Algeria's political environment presently. Although a lack of public disclosure on the state of Bouteflika's health makes it difficult to predict the timing of his eventual departure, we believe that the absence of a succession plan mean that the transition period will be marked by heightened uncertainty over policy. Furthermore, we believe that the risk of unrest will be high as the various powerbrokers vie for control amid an environment of slow economic growth and rising inflation. Against this backdrop, we have reduced our Short-Term Political Risk Index score from 57.0 out of 100 to 52.3, moving the country down one position to 13th out of the 19 MENA states for which we provide coverage.

Succession Uncertainty Raises Policy Continuity Risks

Ongoing calls from Algeria's ruling elite that President Abdelaziz Bouteflika should run for a fifth term in 2019, despite the leader's ill-health and advancing age, reinforce our view that there is little in the way of consensus on who will eventually take over when Bouteflika departs the scene *(see 'Succession Risks Rising Ahead Of Likely Fifth Term For Bouteflika', May 3)*. At the same time, rumours are swirling in Algeria that the president's health is worse than previously thought or even that he has passed away and that his death is being kept secret. While these rumours are impossible to verify, it seems likely that the 81-year old Bouteflika, who has rarely been seen in public since a stroke in 2012, is approaching the end of his near-20 year rule.

Given the apparent lack of a succession plan, his eventual passing is likely to cause a rupture within the ruling elite, which is comprised of politicians from the ruling coalition (consisting of Bouteflika's Front de Libération Nationale (FLN) and Prime Minister Ahmed Ouyahia's Rassemblement National Démocratique (RND)), the military, trade union leaders and wealthy businessmen. The main unifying theme for this group is a preference for the status quo to remain in place, which is most likely under Bouteflika's continued rule. In the likely event that Bouteflika departs power before consensus is agreed on succession, we believe that there will be a struggle for power that will lead to heightened uncertainty with respect to policy continuity. As such we downgraded the 'policy continuity' subcomponent of our short-term political risk index to 50.0 out of 100 from 75.0 previously.

Risks Of Instability Will Also Rise

We also believe that risks of unrest will rise amid the struggle for power as the population at large becomes frustrated with the lack of development while the political elites tussle over economic and political power. Large-scale protests have been rare in Algeria over last 20 years, owing largely to a collective fear that popular action could lead to a repeat of the bloodshed of the civil war in the 1990s. However, demographic shifts (an estimated 56% of Algerians are under 30) coupled with the passage of time mean that the desire to avoid a repeat of the 1990's violence is likely becoming less and less of a deterrent. Furthermore, slow economic growth, high youth unemployment and rising inflation *(see 'Algerian Economic Growth To Remain Subdued', August 7)* will stoke popular anger and may lead to an increase in support for Islamist parties. The civil war in the 1990s began when a military coup prevented the Front Islamique de Salut from coming to power after defeating the FLN in the 1991 election and we believe that the military will remain opposed to Islamist rule once Bouteflika departs the scene. Against this backdrop, we have also lowered the score for the 'social stability' subcomponent of the STPRI from 37.5 to 32.5.

ALGERIA – DATA & FORECASTS

	2014e	2015e	2016e	2017e	2018f	2019f	2020f
Population, mn	39.11	39.87	40.61	41.32	42.01	42.68	43.33
Nominal GDP, USDbn	213.8	166.4	159.1	174.4	188.9	205.6	221.1
GDP per capita, USD	5,466	4,173	3,917	4,220	4,496	4,817	5,102
Real GDP growth, % y-o-y	3.8	3.7	3.3	1.6	2.8	2.7	2.8
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	2.9	4.8	6.4	5.4	6.8	8.1	6.8
Consumer price inflation, % y-o-y, eop	5.3	4.4	7.0	4.9	8.7	7.5	6.0
Central bank policy rate, % eop	4.00	4.00	3.50	3.75	4.00	4.00	4.00
Exchange rate DZD/USD, ave	80.58	100.36	109.41	110.94	117.38	121.50	124.50
Exchange rate DZD/USD, eop	87.92	107.10	110.40	114.76	120.00	123.00	126.00
Budget balance, DZDbn	-1,257.3	-2,551.0	-2,286.0	-1,207.0	-1,494.8	-1,300.4	-1,335.7
Budget balance, % of GDP	-7.3	-15.3	-13.1	-6.2	-6.7	-5.2	-4.9
Goods and services exports, USDbn	63.6	38.1	32.7	42.7	52.6	56.4	57.7
Goods and services imports, USDbn	71.4	63.6	60.2	62.7	64.9	67.1	69.5
Current account balance, USDbn	-9.4	-27.2	-26.2	-18.5	-10.4	-8.5	-9.5
Current account balance, % of GDP	-4.4	-16.4	-16.5	-10.6	-5.5	-4.1	-4.3
Foreign reserves ex gold, USDbn	179.6	144.7	114.4	97.6	83.0	70.5	64.9
Import cover, months	36.1	33.0	27.8	22.8	18.7	15.4	13.7
Total external debt stock, USDbn	5.5	4.7	5.5	6.0	10.0	14.7	19.9
Total external debt stock, % of GDP	2.6	2.8	3.4	3.4	5.3	7.1	9.0
Crude, NGPL & other liquids prod, 000b/d	1,525.0	1,632.0	1,495.0	1,641.0	1,559.6	1,557.8	1,544.4
Total net oil exports (crude & products), 000b/d	1,134.7	1,254.9	1,093.3	1,240.8	1,151.5	1,138.1	1,111.9
Dry natural gas production, bcm	84.0	86.1	94.8	94.5	97.6	103.8	106.3
Dry natural gas consumption, bcm	37.5	39.5	36.0	37.4	38.1	39.3	40.4

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

LIBYA – ECONOMIC OUTLOOK

Growth To Slow In 2018 On Oil Production Outages

Key View: *Oil export gains will continue to support growth in economic activity in Libya over 2018-2019, albeit to a much lesser extent than in 2017, given production disruptions and waning base effects. Consumption and investment will remain subdued, weighed down by currency weakness and elevated inflation. Structural obstacles, such as underdeveloped infrastructure, will keep growth far below potential for many years – even beyond an eventual resolution to the ongoing political conflict.*

Forecast Change

- We have revised down our forecast for real GDP growth in 2018 to 11.2%, from 17.7% previously, on the back of recent disruptions to oil production.

Oil production gains will boost exports, albeit to a lesser extent than in 2017. Libyan oil production averaged 1.0mn barrels per day (b/d) through January-May 2018, compared with just 664,000b/d over the same period of 2017. Following a sharp drop in June-July as a result of militant attacks and political rivalry, production is now rebounding again, last reported at around 700,000b/d. We expect output will average higher in 2018 than in 2017, but amid recent disruptions and waning base effects, the pace of expansion will be substantially slower this year. Overall, we forecast Libyan net hydrocarbon exports will increase by 3.8% y-o-y in 2018 and 4.5% in 2019, from a jump of 153.6% in 2017. This factors in periodic disruptions resulting from clashes between local militias and groups. But with no end to the political conflict in sight, risks of more severe outages (which would prompt downward revisions to our forecasts) are elevated.

Import shortages and resultant high inflation will weigh on consumption and investment. Severe dollar shortages – illustrated by the wide gap between the dinar's official exchange rate at LYD1.38/USD and the black market rate of LYD5.85/USD – are restricting imports, and in turn fueling inflation. It is worth noting that Libya covers as much as 85% of its needs through imports. The issue is exacerbated by high levels of import fraud: indeed, according to the European Council on Foreign Relations, only 14% of declared imports reach local markets, as importers use the credit extended to them at the official exchange rate to sell dollars on the black market.

Tripoli-based Libyan authorities announced in June that exchange rate policy reforms aimed at addressing this issue would be forthcoming in the coming months. However, with little scope for a resolution to the political conflict, we remain sceptical of the authorities' willingness to fully implement these, amid concerns that they may erode their popular and militant support. Meanwhile, Libyan households and businesses will remain under pressure, constraining growth in private consumption and investment. Structural obstacles will keep growth below potential in the long term. Aside from the macroeconomic imbalances associated with the ongoing political conflict, Libya also suffers from numerous structural impediments to growth, which are likely to persist over the long term – for even many years beyond an eventual reconciliation. Most notably, Libya's infrastructure remains severely underdeveloped, and has suffered significant damage as a result of fighting.

Major investments will be needed to address this issue. However, this is unlikely to be forthcoming on a large enough scale over the years ahead, as Libyan authorities struggle to rein in current spending, and as foreign entities remain deterred by persistent security risks and an exceptionally weak regulatory framework. Illustrating the challenging operating environment is Libya's poor ranking in our Operational Risk Index, in 185th place out of 202 states. Amid these conditions, the process of sustainably developing and diversifying the Libyan economy will likely prove very slow.

LIBYA – ECONOMIC OUTLOOK

Oil Export Disruptions To Slow Budget Deficit Reduction

Key View: *Oil revenue gains will facilitate a narrowing of Libya's fiscal deficit – but only moderately so, as oil production suffers from frequent disruptions and as current spending remains high. Persistent deficits will primarily be funded through domestic borrowing, causing already-high public debt levels to increase further.*

We expect Libya's fiscal deficit to narrow on oil revenue gains, but only moderately so. Global oil prices have rallied in recent months, encouraging our Oil & Gas team to revise its Brent forecasts from USD67.0 per barrel (/bbl) this year and USD75/bbl in 2019 to USD75.0/

bbl and 80.0/bbl respectively. As oil earnings make up the vast majority of Libyan state revenues – 93% in H118 according to the Tripoli-based Central Bank of Libya (CBL) – this will provide a significant boost to the country's fiscal position. In addition, we also expect oil production to average higher in 2018-2019 than in 2017 *(see 'Libyan Growth To Slow In 2018 On Oil Production Outages,' August 3)* – though we note that disruptions in June-July mean that y-o-y gains are likely to be lower than we had initially anticipated. We further caution that more disruptions are likely in the quarters ahead: indeed, with a lasting resolution to the ongoing conflict seemingly a distant prospect – and oil infrastructure still regarded an attractive target for local groups looking to increase their influence and/or receive pay-offs – risks of attacks on production, transportation and storage facilities will stay elevated.

Current spending looks set to remain high. The Tripoli-based CBL and Government of National Accord (GNA) have reportedly agreed to implement reforms to restrict current spending – including cuts to fuel subsidies – in the coming months. 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 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 much-needed increases in capital spending and improvements in public service delivery. Overall, we forecast Libya's official deficit to come in at 6.8% of GDP in 2018 and 6.4% in 2019, from an estimated 8.2% in 2017.

Persistent deficits will primarily be funded through domestic borrowing. The official budget deficit (as worked out by Tripoli-based authorities) will likely continue to be funded by CBL borrowing. In addition, western authorities are able to draw on foreign exchange reserves, which, accumulated in the Qadhafi era, remain sizeable, reported at around USD72.6bn by end-2017. 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 2016) will continue to increase – albeit at a slowing pace, as higher oil revenue leads to gradually narrowing fiscal deficits. 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 – estimated at USD67.0bn – as a result of the lifting of UN sanctions.

LIBYA – DATA & FORECASTS

	2014e	2015e	2016e	2017e	2018f	2019f	2020f
Nominal GDP, USDbn	30.8	37.4	43.0	91.2	70.3	77.9	83.5
Real GDP growth, % y-o-y	-24.0	-6.1	4.3	33.0	16.7	11.6	7.9
GDP per capita, USD	4,960	5,993	6,826	14,308	10,867	11,854	12,539
Population, mn	6.20	6.23	6.29	6.37	6.47	6.57	6.66
Consumer price inflation, % y-o-y, eop	7.1	15.7	25.2	25.0	18.0	14.0	11.0
Consumer price inflation, % y-o-y, ave	2.4	9.8	25.9	27.0	23.0	15.0	12.0
Central bank policy rate, % eop	3.00	3.00	3.00	3.00	3.00	3.00	3.00
Exchange rate LYD/USD, ave	1.27	1.37	1.37	1.39	2.50	2.70	2.90
Exchange rate LYD/USD, eop	1.32	1.35	1.44	1.36	2.50	2.70	2.90
Budget balance, LYDbn	-22.3	-26.4	-20.2	-10.4	-11.9	-13.4	-15.1
Budget balance, % of GDP	-56.9	-51.1	-33.8	-8.1	-6.8	-6.4	-6.2
Goods and services exports, USDbn	24.6	15.7	9.5	13.2	15.9	17.0	18.4
Goods and services imports, USDbn	48.1	29.1	15.9	20.4	23.6	25.2	26.3
Current account balance, USDbn	-21.3	-12.9	-5.7	-6.4	-6.9	-7.3	-7.0
Current account balance, % of GDP	-69.3	-34.5	-13.3	-7.0	-9.9	-9.4	-8.3
Foreign reserves ex gold, USDbn	89.1	73.7	65.9	61.3	58.2	55.9	53.7
Import cover, months	22.2	30.4	49.8	36.1	29.6	26.6	24.5
Total external debt stock, USDbn	5.6	4.7	6.3	6.9	7.5	7.3	7.0
Total external debt stock, % of GDP	18.1	12.5	14.8	7.6	10.6	9.4	8.4
Crude, NGPL & other liquids prod, 000b/d	496.6	415.8	419.2	863.0	909.7	946.4	1,039.0
Total net oil exports (crude & products), 000b/d	272.9	203.2	210.1	649.7	664.6	664.9	729.4
Dry natural gas production, bcm	11.8	11.6	9.3	9.6	11.1	13.3	14.0
Dry natural gas consumption, bcm	5.8	4.5	4.5	4.7	5.4	5.7	5.9

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