Egyptian Agricultural Bank (Al Massy)

Quarterly report
Q2 2021

Investment Objective

The principal investment objective of the fund is long-term capital appreciation through achieving the highest possible risk-adjusted returns.

Investment Universe

- The fund invests mainly in securities of companies listed on The Egyptian Stock Exchange
- The fund can also invest in treasury bills, treasury bonds, corporate bonds, securitization bonds and time deposits.

Subscription/Redemption

- The fund offers daily subscription to investors
- The fund offers weekly redemption to investors
- The valuation day for the fund is the last business day of every week
- Minimum initial investment is 5 ICs

Fund Details

Type of Scheme	Open Ended
Inception date	April-2008
IC price	EGP 261.46
Dividends Since Inception	EGP 12.00
ISIN	65122941

Fund Manager

Management company	Hermes Fund Management
Fund Manager	Nabil Moussa
Assistant Fund Manager	Mostafa Amer
Managing since	July-2013

Contact Details

Egyptian Agricultural Bank

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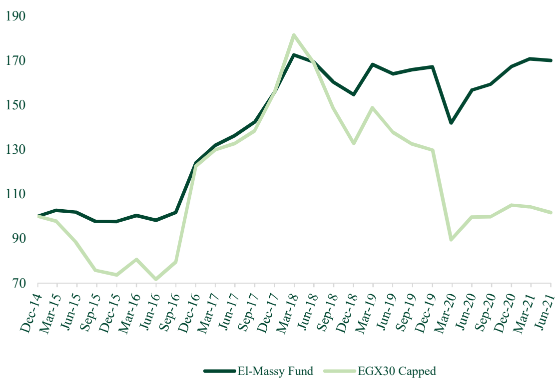
Portfolio

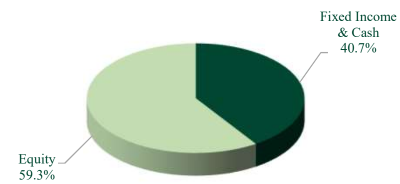
Performance Figures

Date	Return
Q2 2021	-0.4%
YTD	1.6%
2020	0.1%
5-YTD	73.2%
Since Inception	188.8%

Relative Performance



Asset Allocation



Market Outlook

Strategy Update

The Egyptian market is witnessing a divergence in performance between EGX30 and EGX70 for the first time in history. As we are used that either EGX30 outperforms the EGX70 in a bear market, while in a bull market both indices do well. However, this is not the case since the peak of the market in February 2020. The EGX30 had lost 27.3% since February peak till the close of June 30th, 2021 while EGX70 was up 82.3% during the same period. We note that one of the main reasons behind the bad performance in EGX30 is that several foreign investors shied away from the market with the outbreak of COVID-19 and being worried about its impact on Egypt given the country's dependence on tourism, and the magnitude was further magnified when concerns appeared regarding the corporate governance in the CIB.

Finally, we note that MSCI in its latest quarterly rebalance announced removing SWDY from its index while replacing it with FWRY. In addition, the MSCI along with FTSE announced reducing the weight of the CIB in both indices as a result of excluding National Bank of Egypt ownership in the bank from free float. This resulted in around USD80 million direct outflows from the market throughout May and June. We note that the exclusion of the index leads to additional selling from other active managers that track the index. We highlight that foreign institutions sold in the market by around EGP7.56 billion (USD482 million) during May and June that we believe at least 70% of this selling was concentrated in the CIB. On the other hand, foreign institutions bought by around EGP5.96 billion (USD379 million) during the same period that we believe at least 70% of this buying was also concentrated in the CIB trying to capture the stock at a historic low multiple.

The market main index EGX30 declined by 5.4% in 1H2021 pressured by foreign selling across industry heavyweights: SWDY (-13.6%), COMI (-11.9%), HRHO (-9.4%), EAST (-9.1%), and ABUK (-7.1%). On the other hand, FWRY outperformed the market increasing by 35.4% during the period given that it was the only stock witnessing net foreign buying as a result of its inclusion in the MSCI EM index, while on the other hand a stock like TMGH also outperformed the market inching upwards 0.9% given the lack of foreign appetite in real estate sector.

We note that Egypt has been ranked 23 among the 27 markets in the emerging market index during 1H 2021 given that the Egyptian market is among the lowest markets in terms of liquidity among Emerging markets thus being vulnerable to more volatile swings amid outflows. Foreign institutions sold by around EGP17.88 billion during the first half of 2021 while Arab institutions sold by around EGP4.97 billion, this was countered by foreign institutions buying by around EGP15.77 billion and Arab institution purchasing by around EGP4.90 billion implying net outflows of EGP2.19 billion.

Future Outlook

We believe that the worst has passed relative to the Egyptian market given the amount of selling pressure over the past months that pushed the market into a historic low valuation trading at P/E of 7.0x compared to average MSCI EM P/E multiple of 14.4x. Therefore, we believe that the market would recover in the remaining part of 2021 supported by earnings recovery across corporates in addition to the CBE decision to cut interest rates by 10.5% since the beginning of the easing cycle in February 2018 will improve the capabilities of the economy and enhance growth prospects post COVID era.

Moreover, we highlight that oil trading in the range of USD70 per barrel is supportive for emerging markets in general and the industrial sector in Egypt specifically. We believe that although, the industrial sector has been outperforming the market over the past period, stock prices still don't reflect the current global commodity prices and stocks are trading at deep discount to their peers in other emerging markets.

Finally, we highlight, that the political escalation between Egypt and Sudan from one side and Ethiopia from another side might remain an overhang over the market performance although we believe that the dispute is discounted in current market prices.

Economy

The CBE maintained overnight deposit and lending rates stable at 8.25% and 9.25, respectively for the fifth consecutive meeting yet post 10.5% cuts over the period February 2018 to November 2020. The CBE stated that inflation remained subdued while economic activity continued to recover yet rising international food and commodity prices is raising the level o uncertainty regarding future price trajectories.

The IMF announced completing Egypt's Stand-by Agreement (SBA loan programme that Egypt initiated with the IMF upon the outbreak of COVID-19, which paved the way for Egypt to receive USD1.6 billion representing its third tranche of the loan. The IMF indicated that Egypt's net international reserves and the primary budget balance exceeded the program target, while inflation remained stable at 6.1%.

The parliament approved FY 21/22 budget submitted by the government with an expectation of achieving 5.4% real GDP growth while reducing budget deficit to GDP ratio to 6.7%. The budget is targeting total revenues of EGP1.3 trillion, while total expenses to reach EGP1.8 trillion. The government expenditure bill is including 27.6% increase in public investment reaching EGP358 billion in addition to 11.4% increase in wages and compensations of state employees to reach EGP361 billion.

Foreigners purchased additional local treasuries worth USD1.5 billion throughout May raising their total holdings to an all-time high of USD22.3 billion. We note that foreigners currently own 23% of Egypt's total outstanding treasury, and have been net buyers in the market since July 2020 with the exception of March 2021 were they turned into net sellers; however, resumed their buying position in the following two months.

Egypt's current account deficit surged 1.8x from USD7.34 billion in 9M19/20 to USD13.30 billion in 9M20/21. The surge in current account deficit was mainly on the back of diminishing net tourism proceeds to USD1.14 billion only compared to USD6.72 billion in 9M19/20 prior to the outbreak of COVID-19. The drop in tourism was partially offset by increase in private transfers from Egyptians working abroad by 8.8% from USD21.31 billion to USD23.19 billion.

JP Morgan issued a statement saying that Egypt is on index watch list to join its GBI-EM index for domestic debt market. The statement says that Egypt would have a potential weight of 1.8% which would result in around USD4.0 billion of passive inflows. The final decision for the inclusion will be taken in the next index review in October. We note that foreigners currently own around 15% of Egypt's local debt market while lacking any passive money, thus the inclusion should add additional flow to the local market which bodes well for the EGP and help reduce borrowing costs.

The government announced increasing electricity prices by an average of 13% for residential consumption compared to an increase of 19% that occurred in the last year. The government stated that it extended its plan of complete subsidy phase out to FY24/25 instead of FY21/22 taking into consideration the economic impact of the pandemic on citizens. The delayed liberalization is expected to cost the budget around EGP26.7 billion over the next three years.

The CBE announced that Egypt's foreign reserves inched upwards to USD40.58 billion in June 2021 up from USD40.47 billion in May implying an import coverage ratio of 7.1 months. We note that foreign reserves increased by 12.7% from the low of USD36.00 billion recorded in May 2020, yet still below the USD45.51 billion pre COVID-19 level seen in February 2020. However, we note that the CBE holds USD10.1 billion in tier II reserves implying total CBE reserves of USD50.7 billion compared to pre COVID-19 level of USD52.5 billion.
Egypt's headline inflation inched upwards to 4.9% in June compared to 4.8% in May, yet up from 4.1% in April. We note that inflation remains subdued since the beginning of 2020. We expect inflation to gradually pick up in the second half of 2021 in light of constant rise in global commodity prices that will force producers to gradually pass on rising input prices. Despite of the rising inflation we believe that Egypt will remain working in a positive interest rate environment yet we do not forecast any further cuts from the CBE till end of the year.

On the fixed income side, the Fund manager increased durations taking advantage of the improved sentiment towards the Egyptian economy, which led to increased foreign flow into the local treasuries market. Going forward the fund will maintain the same level of duration in anticipation of gradual economic recovery.