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Egyptians ditch imports and buy local as pound sinks

An Egyptian worker works at a local chocolate factory in Cairo, Egypt, February 5, 2017. Picture taken February 5, 2017. REUTERS/Mohamed Abd El Ghany

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By **Asma Alsharif** and **Mohamed Zaki** | CAIRO

Egyptian chocolate spread maker Swifax has doubled its sales and is struggling to keep up with demand since the pound currency dived in November, forcing shoppers traditionally "obsessed with everything foreign" to ditch pricy imports and buy local.

"People started changing their habits," Swifax's commercial director Mohamed El Gammal told Reuters. "We could sell even more ... but we have a problem with our capacity."

The pound's flotation and an ensuing increase in tariffs on more than 300 products shipped from abroad have hit importers hard, but have been a boon for domestic manufacturers such as Swifax.

Once shunned in favor of prestigious foreign brands perceived to offer higher quality, Egyptian-made products are much more affordable for customers who are increasingly price conscious as inflation has shot above 28 percent.

The bonanza began when Egypt abandoned its peg of 8.8 pounds to the dollar on Nov. 3. Since then, the currency has roughly halved in value to around 17.75.

Sitting in his office next to a glass cabinet crammed with varieties of the sandwich-filler popular with sweet-toothed Egyptians, Gammal said sales have jumped from 2 million pounds ($112,700) a

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few months before the flotation to 4 million, as rival imported brands become unaffordable to many.

A 350-gram jar of Swifax's high-end spread, Moltobella, costs 36 pounds while its budget brand costs around 17 pounds. Its main imported competitor sells for about 70 pounds a jar.

Floating the pound helped Egypt to secure a $12 billion IMF loan in return for a reform program that includes tax increases and electricity subsidy cuts, driving up inflation in a country where millions live a pay check from hunger.

Egypt also raised customs tariffs on many luxury goods to over 50 percent, plugged customs loopholes, and tightened quality controls in an effort to rein in a trade deficit the central bank blames for depressing the currency.

Importers criticized the increases, saying local producers don't have the capacity to fill the gap left by declining sales of foreign goods.

According to Emad Maher, manager of hypermarket chain Samy Salama, switching to local products has increased by 90 percent, mainly because of the price difference.

"In some products, you can compare the local and imported and not find much difference (in quality). But Egyptians are obsessed with everything foreign," he said.

At Covertina, another chocolate-maker, business is also booming. Chief Executive Mostafa Sayed Salam said production had risen 19 percent in 2016 from the previous year. "After the flotation of the currency, it became hard for importers to sell the chocolate at the old prices," he said. "My market share has increased from 50 percent to 65-70 percent."

NARROWING THE DEFICIT

Multinationals are taking notice. Nestle, the packaged food giant, said in January it had signed a deal to acquire Caravan Marketing Company, an Egyptian instant coffee maker that had increased its domestic market share due to competitive pricing.

With Egypt long dependent on imports, the trend suggests the government's efforts to narrow a big trade deficit and boost domestic industries are starting to work.

Even before the float, imports had been falling due to shortages of foreign currency. Egypt had struggled to attract dollars and revive the economy after the 2011 overthrow of president Hosni Mubarak, with subsequent political turmoil driving away tourists and foreign investors.

Official trade figures for 2016 have yet to be released but a government official told Reuters earlier this month that the deficit had narrowed by 17.4 percent compared with 2015. Imports fell to $62.93 billion from $70.28 billion, said the official, but higher exports also helped to shrink the gap. These rose to $20.26 billion in 2016 from $18.67 billion.

As the unofficial figures suggest, the weaker pound is also helping Egyptian exporters.

Hesham Zahra, chairman of Yasmine cosmetic company, said production had risen 25-35 percent since the flotation boosted sales both at home and abroad. "Today our prices have become competitive in foreign markets, and we can compete with some countries in exports," he said, adding that Yasmine lotion retails for a quarter of the price of some imported brands.

Trade and Industry Minister Tarek Kabil told Reuters in October that Egypt had produced $4 billion worth of import substitutes since the start of 2016 and aimed to expand domestic industry by 8 percent in three years.

Food industries were leading the way, he said, but local products were also compensating for a retreat in imported building materials, chemicals, leather and furniture.

"This is a golden opportunity for Egyptian producers," said Abu Bakr Emam, head of research at financial firm Prime Holding. "Local producers used to be unable to compete but now is the right time to go in to compete against imported goods due to the price advantage after the dollar rises."

RISING PRICES

Still, the pound's dive is a double-edged sword for local manufacturers who

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pivotal week for markets gets underway

largely depend on imported raw materials.

At Swifax, Gammal said the cost of cocoa butter and hazelnut had more than doubled since the flotation. A tonne of hazelnut used to cost 90,000 pounds but now it costs 230,000.

This forced the company to dip into funds that had been earmarked for expansion. This will now take longer despite the more pressing need to raise capacity. "In the end we increased production without the expansion by tripling the shifts at our factories which adds a lot of strain on the machines," he said.

With Egypt aiming to raise economic growth under the IMF program to 5.5 percent by the 2018-19 fiscal year from 4.3 percent in 2015-16, the government can ill-afford large numbers of firms to delay investment like Swifax.

But as prices rise, ever more families are looking to save money. "People right now don't care about the quality, it's all about the price," said once shopper in Cairo who called himself Abu Abdulla. "I walk around the supermarket and just look at the prices," he said as he pushed a trolley piled with seven family-size boxes of Egyptian-made biscuits.

Tapping into the trend, a Facebook group called "Made Proudly in Egypt" lists tried and tested local products, from foods to detergents and even pots and pans.

One of the more than half a million members of the group, writing under the name of Om Khaled, said the bargains sell fast. "I used to get (imported) nappies and baby food for my son and now I get local alternatives but unfortunately the cheap Egyptian products are not always available. I have to look hard for them," she said.

($1 = 17.7500 Egyptian pounds)

(Writing by Lin Noueihed; editing by David Stamp)

NEXT IN BUSINESS NEWS

Oil touches three-month lows, as U.S. supply swells

LONDON Oil hovered around three-month lows on Monday, as rising U.S. inventories and drilling activity offset optimism over OPEC's efforts to restrict crude output.

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U.S. stocks were little changed on Monday as investors preferred to hold their bets ahead of a widely expected interest rate hike by the Federal Reserve later this week.

U.S. inflation expectations flatten after run-up: NY Fed

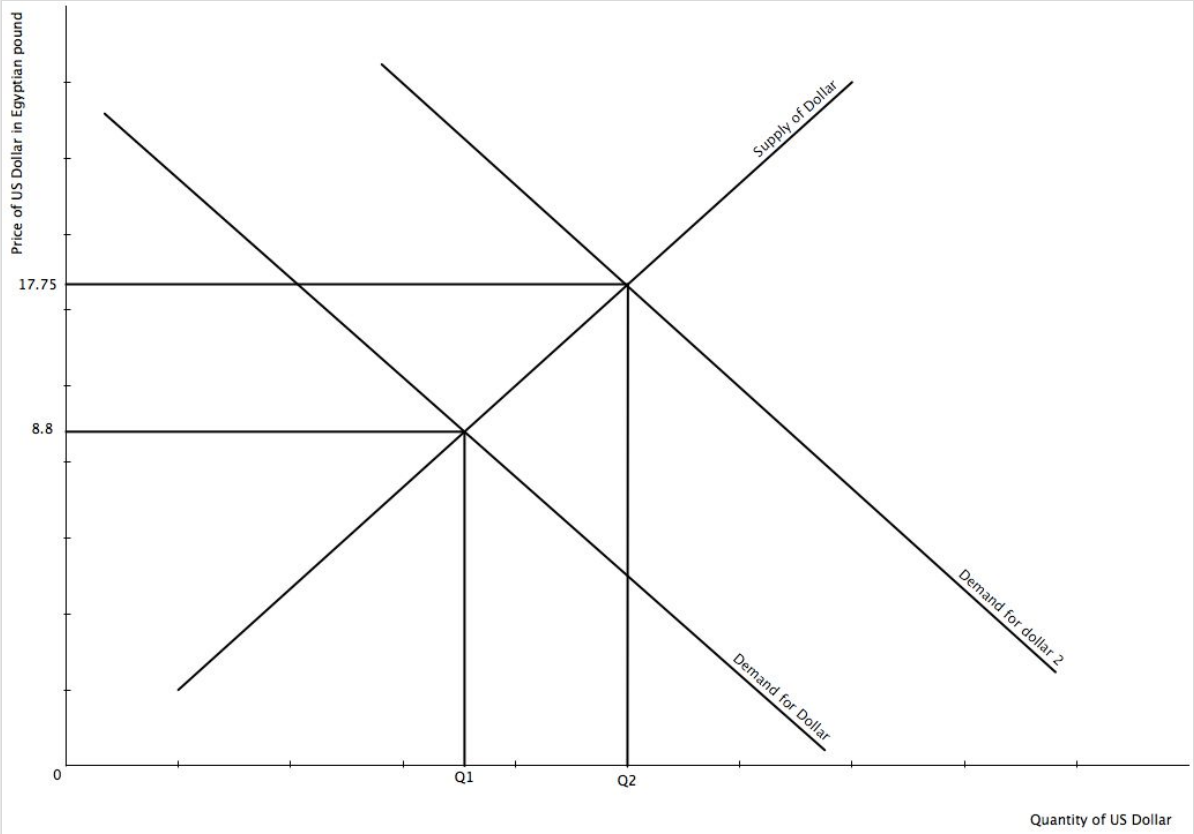
NEW YORK A measure of U.S. inflation expectations mostly flattened in February after having risen in the previous two months, according to a Federal Reserve Bank of New York survey released on Monday.

Commentary 3

"Egyptians ditch imports and buy local as pound sinks"

The following article depicts the depreciation of the Egyptian pound and raised tariffs that the Egyptian government imposed on imported goods. In November 2016 the Egyptian government abandoned its fixed exchange rate system of "8.8 pounds to the dollar[1]", allowing it to float freely, letting the value of the currency be determined solely by the demand and supply in the foreign exchange market. Simultaneously, domestic consumers were "obsessed with everything foreign[2]" and the quantity of imported goods was immense. In particular, goods from the US were in high demand, causing much Egyptian currency to be sold to purchase US dollars.

Figure 1: Exchange rate of the US Dollar in terms of the Egyptian pound showing a depreciation of the Egyptian pound and an appreciation of the US dollar as a result of increased demand

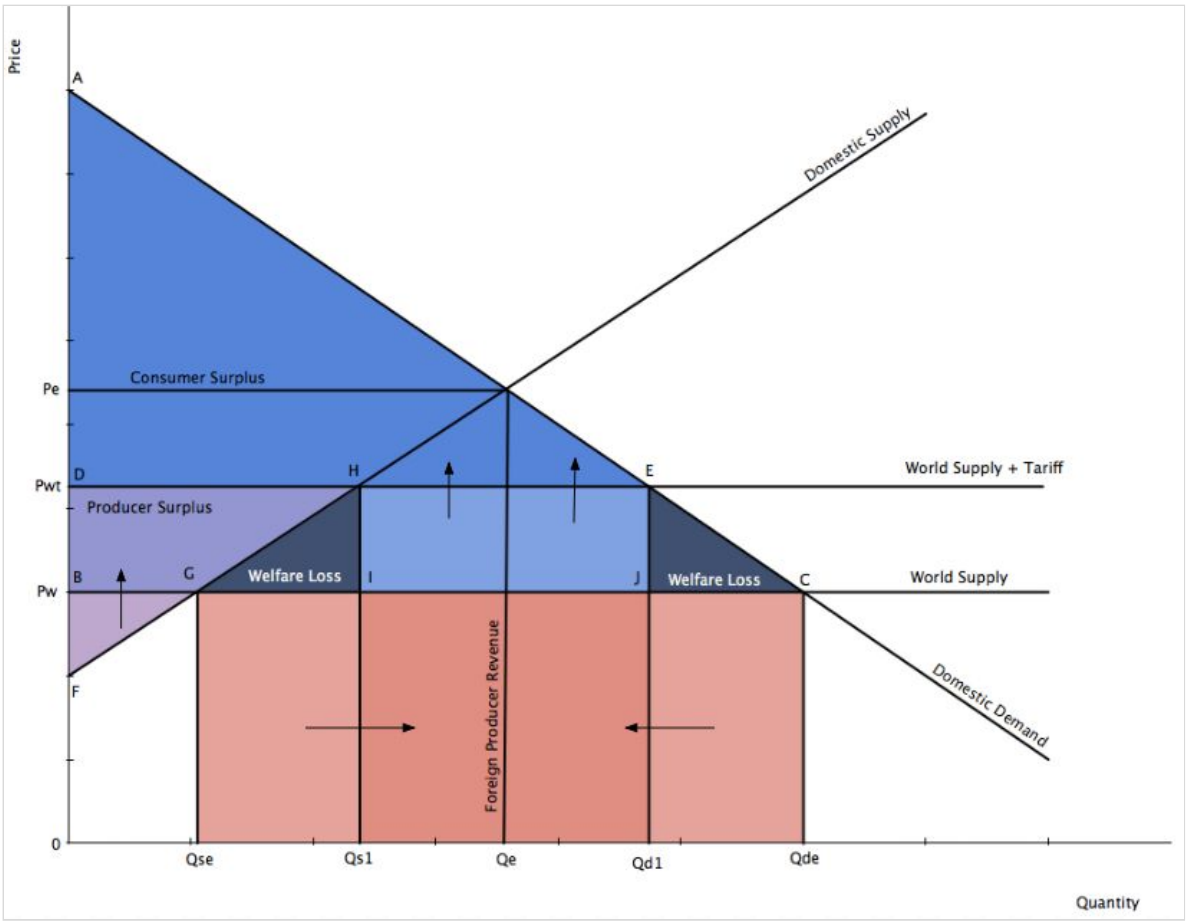


The increased demand for the dollar, represented by an outward shift to the right (figure 1), resulted in the depreciation of the Egyptian pound, defined as the decrease in value of a currency in terms of another. The pound "roughly haved in value to around 17.75[3]", resulting in a lower purchasing power for Egyptian consumers.

[1] Alsharif, Asma "Egyptians Ditch Imports and Buy Local as Pound Sinks." *Reuters*. Thomson Reuters, 12 Feb. 2017.
[2] Alsharif, Asma "Egyptians Ditch Imports and Buy Local as Pound Sinks." *Reuters*. Thomson Reuters, 12 Feb. 2017.
[3] Alsharif, Asma "Egyptians Ditch Imports and Buy Local as Pound Sinks." *Reuters*. Thomson Reuters, 12 Feb. 2017.

Moreover, the high quantity of imports resulted in low demand for domestic goods, leading to low output and revenue. Domestic exports similarly suffered and were relatively low compared to the high levels of imports, causing a trade deficit. In response to this deficit the government "raised tariffs of many goods to over 50 percent... and tightened quality controls[4]". A tariff is a tax by the government on imported goods, aimed at protecting domestic producers of the goods from cheaper foreign competition. The tariff raised the prices of imported goods significantly, making domestic goods a cheaper alternative.

Figure 2: A tariff imposed by the Egyptian government on imported good, raising the world price for imported goods.



The implication of the tariff pushes up the world price from Pw to Pwt, causing the quantity of imports to decrease from Qse-Qde to Qs1-Qd1. For the goods that are imported the government gains tax revenue, marked by the area HIJE. For domestic producers the supply has increased from 0-Qse to 0-Qs1.

The tariff, in addition to the depreciation of the Egyptian pound will have a variety of impacts on the stakeholders in the market.

[4] Alsharif, Asma "Egyptians Ditch Imports and Buy Local as Pound Sinks." *Reuters*. Thomson Reuters, 12 Feb. 2017.

Domestic consumers experience a decrease in consumer surplus from the area ABC to ADE (Figure 2). The price they would have paid before has increased and thus they must pay a higher price if they wish to consume the same imported goods, consequently decreasing consumer demand. Consumers will in turn switch to domestically produced goods which are cheaper.

Domestic producers benefit from the increased demand for domestic goods and experience an increased surplus from the area FBG to FDH. The greater demand results in greater revenue as well as a reduction of unemployment. In order to keep up with demand, industries will need to to expand and boost production, creating jobs. Although many domestic consumers are switching to local goods, some producers are worse off. The domestic producers which rely on imported raw materials to make their goods are faced with higher production costs. The company Swifax was "forced to dip into funds that had been saved for expansion[5]" to buy resources, essential for the production of their product, the price having been raised from "90,000 to 230,000 pounds[6]".

Furthermore, exporters are benefiting from the depreciation of the pound. Figures suggest that "the weaker pound is helping Egyptian exporters" by making exports less expensive and thus more competitive in foreign markets. This is evident in the rise of exports revenue to "20.26 billion from 18.67 billion[7]". Increased exports promotes employment as more labour is required to meet the greater quantity demanded by the foreign market. On the contrary, foreign exporters experience a fall in revenue as domestic consumers purchase cheaper alternatives. As consumers are "increasingly price conscious" they have begun to "ditch the pricey imports and buy local"[8], resulting in a decrease in exports by foreign producers.

The government obtains a tax revenue on the imported goods that are consumed, which provides money that can use to invest within the economy. However, the tax revenue made by the government does not account for the fall in consumer surplus, thus resulting in a total welfare loss, presented by the black shaded areas in figure 2.

In the short run, the imposition of the tariff will benefit domestic producers and consumers by providing cheaper goods and new jobs in domestic industries. However, in the long-run the depreciation of the pound may lead to greater inflationary pressure, which has already "shot above 28 percent". The government must hence be cautious and prepared to intervene, should inflation continue, causing production costs to rise, leading to higher prices in the economy over time.

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[5] Alsharif, Asma "Egyptians Ditch Imports and Buy Local as Pound Sinks." *Reuters*. Thomson Reuters, 12 Feb. 2017.
[6] Alsharif, Asma "Egyptians Ditch Imports and Buy Local as Pound Sinks." *Reuters*. Thomson Reuters, 12 Feb. 2017.
[7] Alsharif, Asma "Egyptians Ditch Imports and Buy Local as Pound Sinks." *Reuters*. Thomson Reuters, 12 Feb. 2017.
[8] Alsharif, Asma "Egyptians Ditch Imports and Buy Local as Pound Sinks." *Reuters*. Thomson Reuters, 12 Feb. 2017.