PHAROS

Egypt MPC Watch

Expect MPC to Cut Rates by 75bps

12 November, 2017

Various price indicators confirm that July's subsidy reform measures shock effect is now over

Since the last Monetary Policy Committee (MPC) meeting in September, the annual headline consumer price index change has decelerated from 31.9% YoY in August to 31.6% YoY in September and 30.8% YoY in October. The monthly CPI pace stabilized around 1.0% MoM in both September and October 2017 compared to an average of 2.5% MoM in November 2016 – August 2017. In that context, we note that seasonal factors, namely education fees, contributed to the monthly inflation pace by 0.8% out of a 1.1% MoM in October. Moreover, the producer price index (PPI) monthly change declined from 3.5% in July to 1.5% in September. This marked the slowest pace versus an average of 2.7% in November 2016 – August 2017.

Financial conditions stand moderately tight as demand side pressures remain muted in 1Q FY2017/18

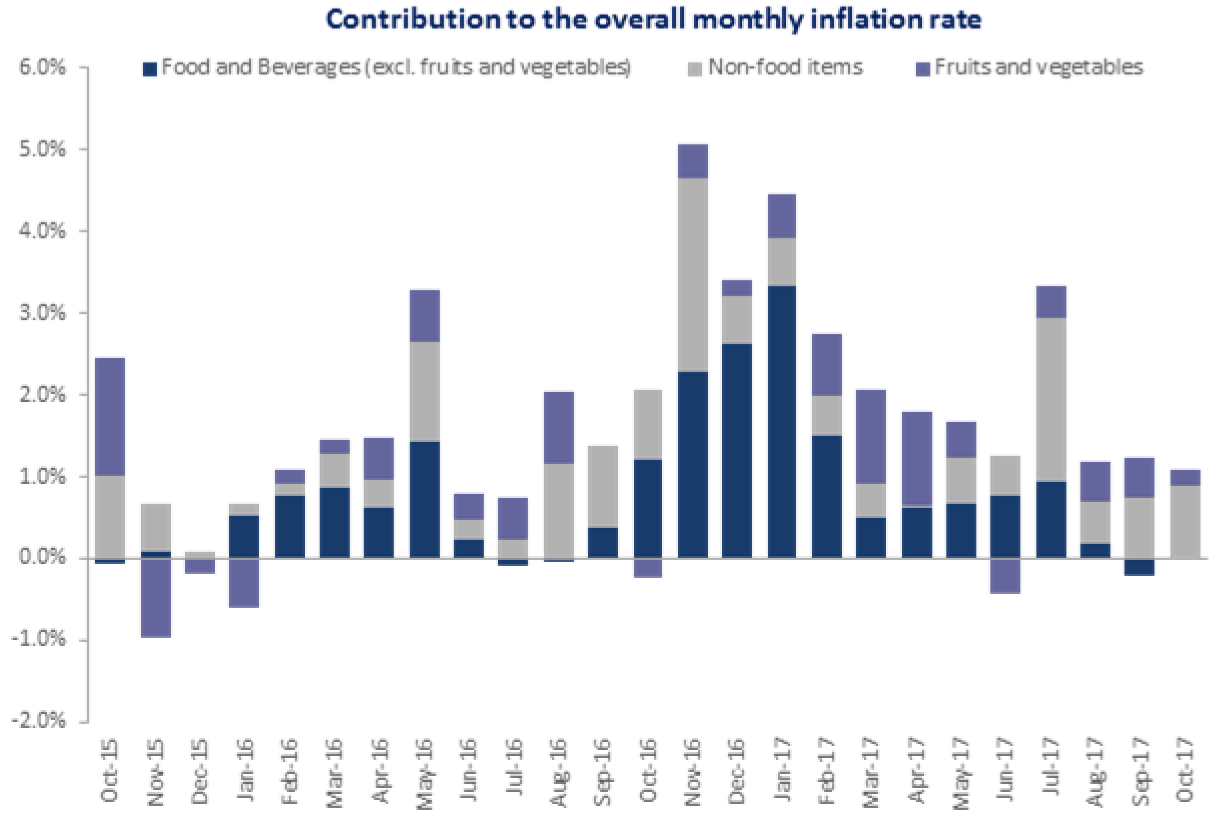
Our Financial Conditions Index (FCI) continued to reflect tight monetary conditions in 1Q FY2017/18 on lower real money supply growth, stable real effective exchange rate, in addition to a negative yield curve slope. As a proxy for the real absorption growth, our Financial Conditions Index (FCI) indicates a slight increase in 1Q FY2017/18, however, it remains below the average growth rate that prevailed post-flotation. In line with the aforementioned argument, we note that the press release, which followed the last MPC meeting in September, dropped the demand side pressures from the overall risks to the MPC's inflation outlook.

Fixed income market dynamics have remain relatively stable since September

The yields continued to decline, albeit at a slower pace, from an average of 17.2% in September to 16.9% in October. We note that both T-bills and T-bonds coverage/supply ratios were slightly lower in October (versus September), partly as the current yield level is still in line with the market participants' policy interest rate outlook. In that context, we note that the foreign holdings of EGP-denominated treasuries rose by 4.4% to USD18.8 billion by the end of October 2017, recording the slowest growth in pace since November 2016.

MPC to cut policy rates by 75bps in November, but monetary easing would be gradual over a longer horizon

We expect that the underlying inflation dynamics would encourage the MPC to cut policy rates by 75 basis points next Thursday. Meanwhile, a key challenge ahead of the MPC in the following meetings will be to manage expectations toward a gradual, rather than an aggressive, monetary easing pace. We believe that the ongoing monetary policy normalization in advanced economies, and the future domestic subsidy reform measures do warrant such a gradual approach over the next couple of years.



Source: CAPMAS

Ramy Oraby
Ramy.Oraby@pharosholding.com

Pharos Research
7 Abu El Feda Street, Zamalek 11211
Cairo, Egypt
Office: +20227393670
Fax: +20227350651
Pharos.Research@pharosholding.com
www.pharosholding.com