BELTONE FINANCIAL

Alia Mamdouh
amamdouh@beltonefinancial.com | +2 0224616407

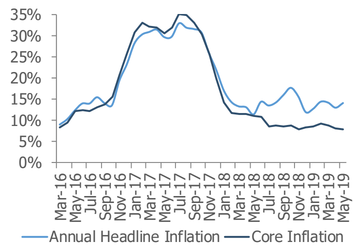
Macro | Egypt

Seasonality drives inflation up in May

Macro Note | Egypt

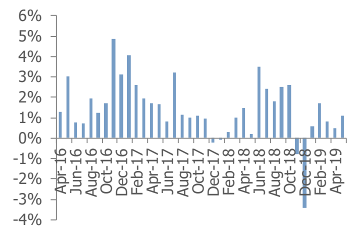
June 10, 2019

Headline inflation rises in May



Source: CAPMAS, CBE

Prices gain momentum on a monthly basis



Source: CAPMAS

Seasonal demand drives higher inflation reading in May; in line with our estimates

May annual headline inflation saw an increase of 14.1%, up from 13% in April 2019, in line with our expectations of 13.9%. This was driven by a 15.1% increase in food prices vs a rise of 13% a month earlier, which we attribute to the seasonal demand accompanying Ramadan and a higher annual increase in fruits and vegetables by 39% vs 27.4% in April. Moreover, the recreation and culture segment continued its increase, rising 7.8%, up from 7% in April. Monthly inflation rose by 1.1% vs 0.5% in April, in line with our expectations of 1%. Core inflation, on the other hand, saw a lower annual reading of 7.8% in May, down from 8.1% in April, with, however, a higher m-o-m reading of 1.2%, up from 0.4% in April.

Monthly momentum to continue with the final round of subsidy cut

We reiterate our view of an expected 2.5-3.5% increase to annual headline inflation throughout 3Q19, driven by the fourth round of fuel and electricity subsidies cuts, and the third increase in water prices. We foresee inflation averaging 13.7% in 2H19, almost flat from 1H19 average of 13.4%, thanks to a stronger local currency that will reduce imported inflation pressures.

We expect interest rates to remain on hold in July's meeting

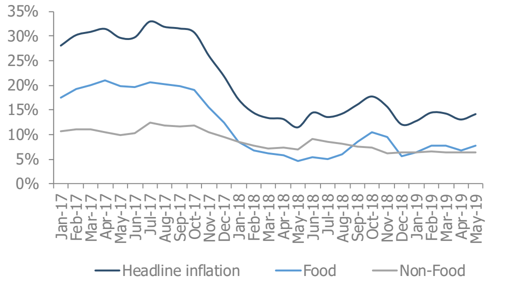
We expect interest rates to remain on hold in the next MPC meeting on July 11, 2019, as we expect a move towards the wider implementation of the fuel indexation mechanism. We reiterate our view of a 100bps cut in rates by the end of the year, which will remain hostage to the pace of inflation deceleration post fiscal reforms. Favorable global conditions, with the ease in monetary tightening, will continue to provide the buffer for the CBE to resume its monetary easing.

Still an attractive carry trade, particularly with the strong EGP appreciation

We believe treasury yields will remain within the current levels (+17%), and thus reiterate our view of a maintained positive portfolio inflow in 2019, guiding a stronger EGP. We still see a substantial carry trade opportunity with an appreciating local currency and solid macro stance, backed by the recent credit rating upgrade to B+ by Fitch. News reported foreign cash inflows of USD4.47bn in May, which confirms our view.

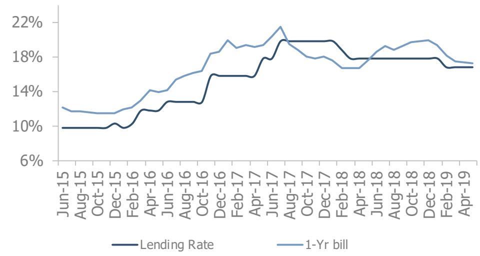
I. Illustrating Charts

Figure 1: Food inflation picks up



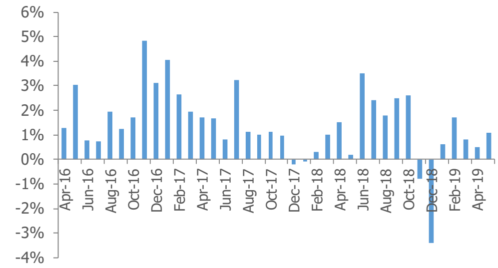
Source: CAPMAS

Figure 2: Treasury yields are still attractive



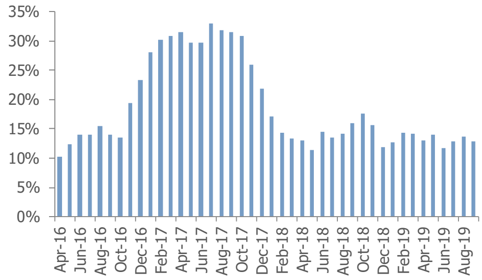
Source: CBE, Bloomberg, March figures are expected

Figure 3: Prices gain momentum on a monthly basis



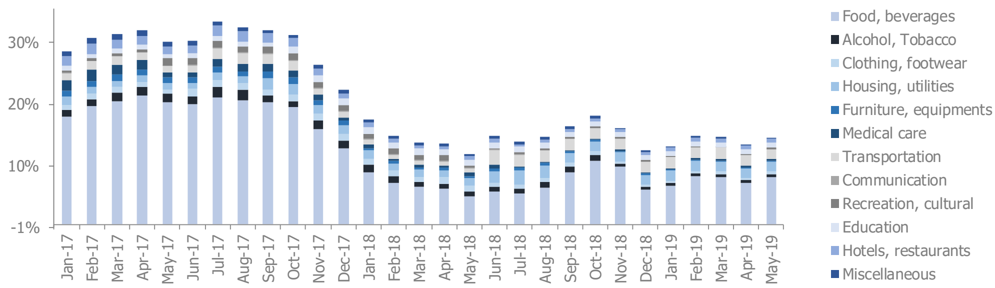
Source: CAPMAS

Figure 4: Annual headline inflation to remain in double digits



Source: CAPMAS, Beltone estimates

Figure 5: Annual headline inflation breakdown (% weighted change)



Source: CAPMAS

II. Macro-economic Indicators

	FY14/15	FY15/16	FY16/17	FY17/18	FY18/19e	FY19/20e	FY20/21e
Real sector							
GDP, current (USDbn)	332	333	235	301	303	372	463
Real GDP growth (%)	4.4%	4.3%	4.3%	5.3%	5.5%	5.9%	6.2%
GDP/capita, current (USD)	3,554	3,608	2,548	2,654	3,161	3,928	4,450
External sector							
Trade balance (USDbn)	(39.1)	(38.7)	(37.3)	(37.3)	(37.7)	(39.6)	(41.1)
Tourism revenues (USDbn)	7.4	3.8	4.4	9.8	12.3	14.0	15.1
Suez Canal revenues (USDbn)	5.4	5.1	4.9	5.7	6.0	6.3	6.6
Transfers (USDbn)	21.9	16.8	21.8	26.5	25.6	25.6	25.8
Current account (USDbn)	(12.1)	(19.8)	(14.4)	(6.0)	(4.6)	(3.9)	(4.3)
Current account % GDP	-3.7%	-6.0%	-6.1%	-2.4%	-1.5%	-1.0%	-1.0%
FDI (USDbn)	6.4	6.9	7.9	7.7	7.3	7.5	7.7
FDI % GDP	1.9%	2.1%	3.4%	2.6%	2.4%	2.0%	1.7%
EGP/USD exchange rate (period avg)	7.36	8.15	14.76	17.72	17.67	17.10	17.86
Net international reserves (end of period) (USDbn)	20.1	17.5	31.3	44.3	46.5	47.4	46.0
Reserves/imports coverage (months)	3.9	3.7	6.4	8.4	8.2	7.8	7.1
Monetary sector							
Inflation (CPI, %)	11.0%	10.2%	23.3%	21.6%	14.6%	15.6%	13.3%
M2 Growth (%)	16.4%	18.6%	39.4%	18.3%	18.3%	19.1%	17.2%
Deposits rate (end of period, %)	8.75%	10.75%	16.75%	16.75%	15.75%	13.75%	12.25%
Lending rate (end of period, %)	9.75%	12.75%	17.75%	17.75%	16.75%	14.75%	13.25%
Fiscal sector							
Fiscal deficit (EGPbn)	279.4	339.5	379.6	433.9	461.5	514.6	540.6
Fiscal deficit % GDP	-11.4%	-12.5%	-10.9%	-9.8%	-8.6%	-7.8%	-6.8%
Primary balance % GDP	-3.5%	-3.5%	-1.8%	0.1%	1.9%	2.0%	1.9%

Source: CBE, MoF, Beltone estimates

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Sales and Trading

Institutional Sales Team

Wafik Dawood
wdawood@beltonefinancial.com

Mohamed Waked
mwaked@beltonefinancial.com

Institutional Trading Team

Nadin Mustafa
nmustafa@beltonefinancial.com

Tamer Salama
tsalama@beltonefinancial.com

Wagih Sharaf
wsharaf@beltonefinancial.com

Beltone Financial

2005C Nile City Towers
North Tower, 33rd floor
Cairo 11221, Egypt
Tel.: +202 24616300
Fax: +202 24619848
research@beltonefinancial.com