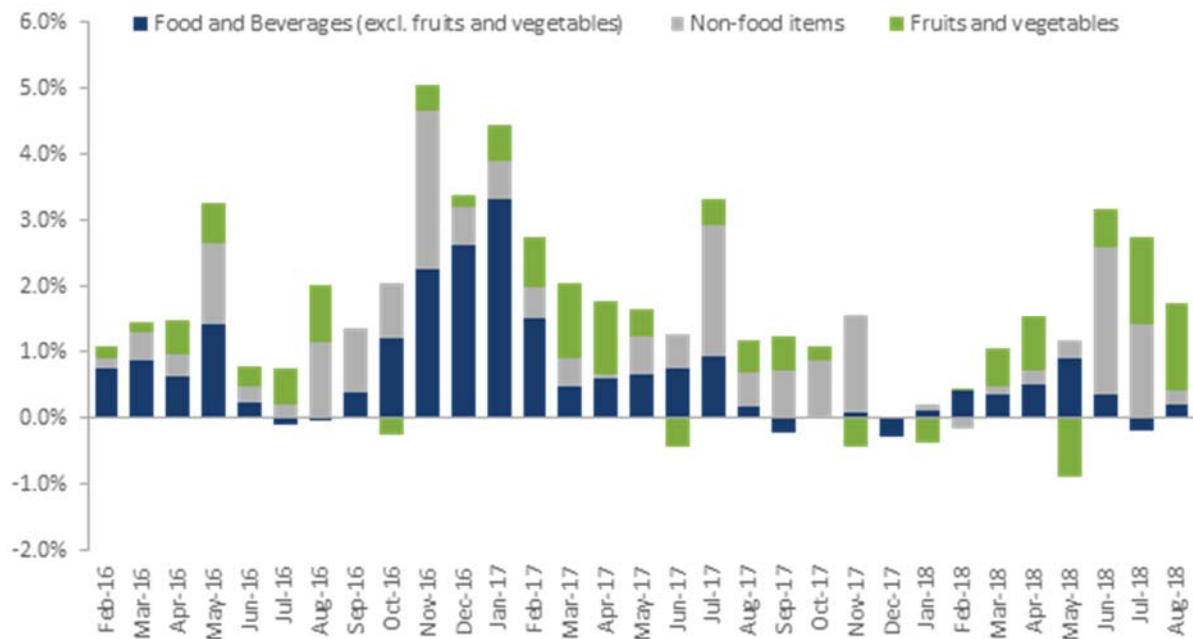


Monthly Inflation Continues its Spike in August But At Slower Pace

The monthly inflation rate decelerated to 1.7% in August, after recording 2.5% in July, while the annual inflation rate recorded 13.6% in August, up from 13% in July. The increase in inflation rate for the past 3 months was expected due to the fiscal consolidation adopted by the Egyptian government in the beginning of FY2018/19.

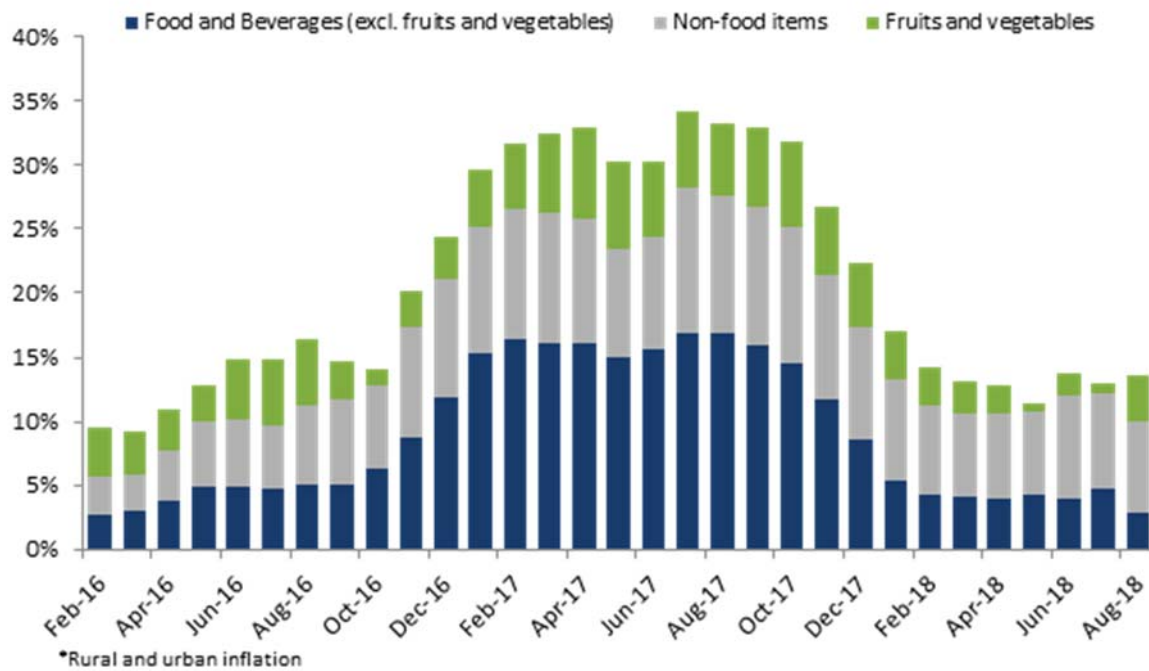
The monthly inflation in August was mainly attributed to the increase in vegetables prices by 8% MoM, fruits prices by 4.9% MoM, and natural gas and gas cylinders by 5.5% MoM.

Chart 1: Contribution to Monthly Inflation



Source: Pharos Research, CAPMAS

Chart 2: Contribution to Annual Inflation



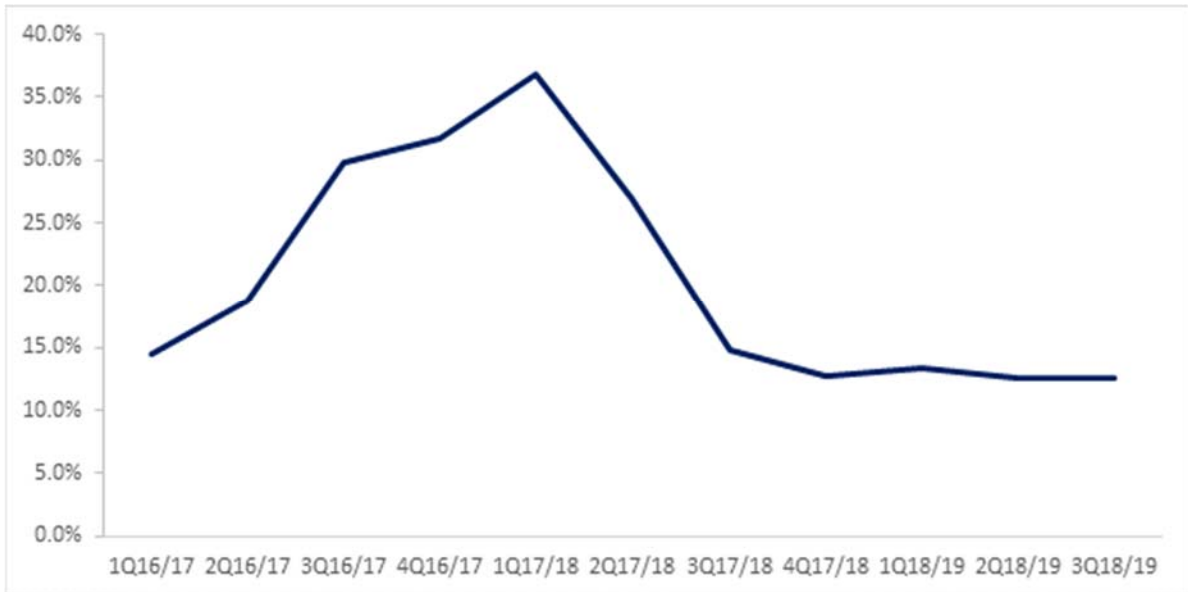
Source: Pharos Research, CAPMAS

Monthly Inflation will Decelerate Below 1% in October-December

Going forward, we expect the monthly inflation rate to decelerate to 1% in September and 0.7% in October, however we expect the annual inflation to stabilize at 13.6% in September and to decelerate to 13.3% in October.

We expect inflation to decelerate from 13.4% YoY in 1Q FY2018/19 to 12.8% in 2Q FY2018/19, and to be 12.7% YoY in 3Q FY2018/19. According to our estimates, the acceleration of inflation should ease after September, once the fiscal consolidation impact is fully absorbed by the market and has fully reflected on the prices of goods and services, in addition to the end of “back to school season”.

Chart 3: Average Quarterly Inflation

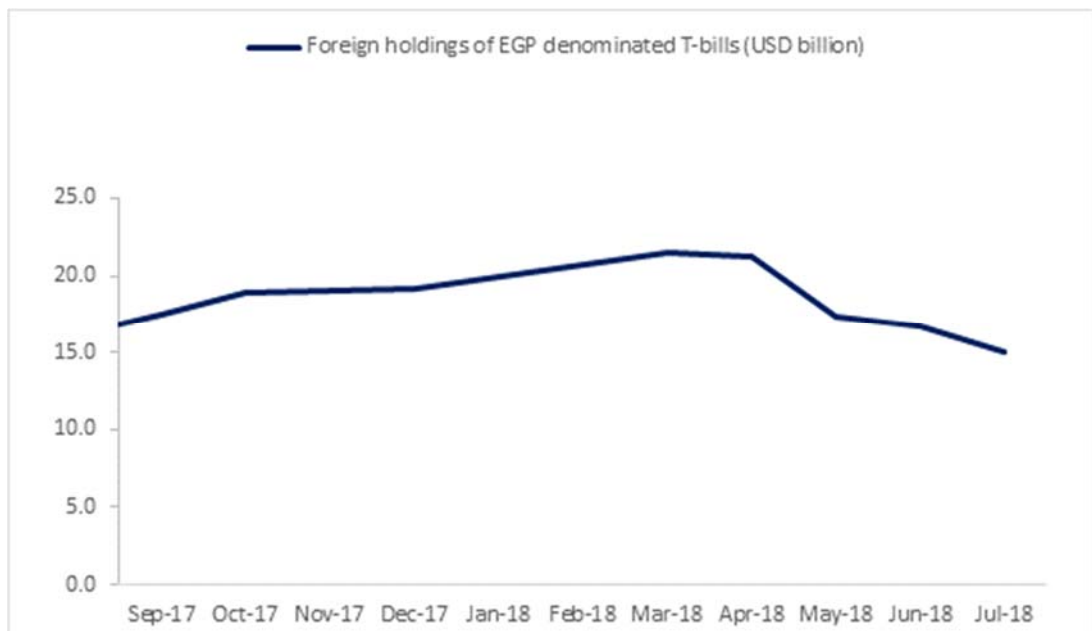


Source: Pharos Research, CAPMAS

Foreign Ownership of Domestic Short Term Debt Declined

The foreign ownership of domestic short term debt has declined 9.7% MoM to its 12-month low to be USD 15.1 billion in July 2018, down from USD 16.7 billion in June 2018. This might lead to a more cautious monetary easing to avoid portfolio investment outflows. It worth mentioning that foreign holdings of T-bills percentage of total T-bills has decreased to its 13-month low to record 21.2% of total outstanding T-bills in July 2018, down from its peak at 32.3% of total outstanding T-bills in October 2017.

Chart 4: Foreign Holdings of EGP T-bills (USD billion)

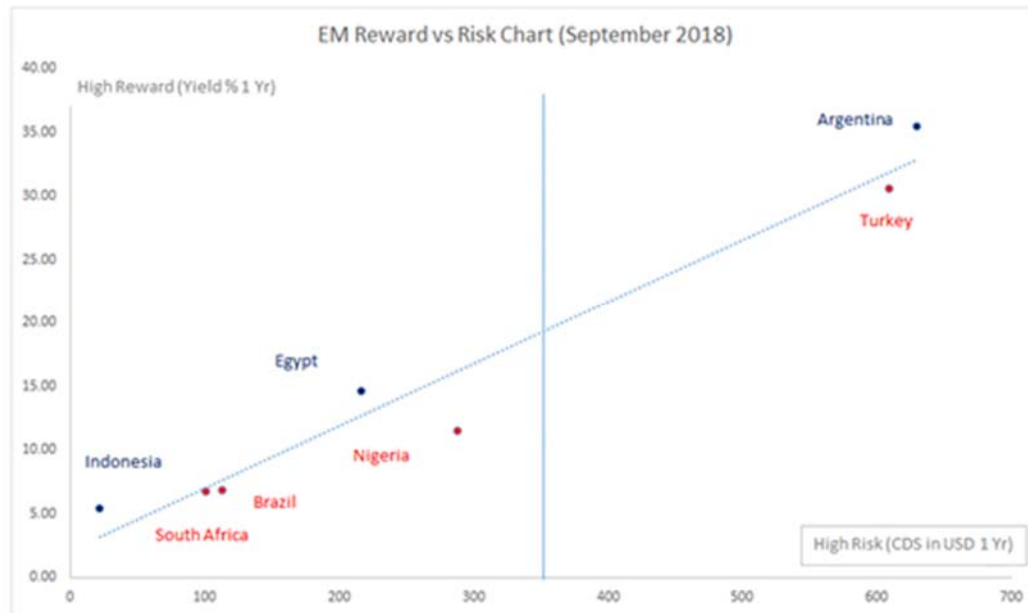


Source: Pharos Research, CBE

Emerging Markets High Yields Dictates Rate Stability

The high yields in other EM such as Argentina and Turkey are putting more pressure on Egypt to maintain policy rates. The after-tax yield on 1Y Argentinian government T-bill has reached 35.56%, while the yield on 1Y Turkish government T-bill has reached 30.70%. However, Egypt is still competitive with these high yields due to its lower risk.

Chart 5: EM Risk/Reward Matrix



Source: Pharos Research, CBE, Bloomberg

In conclusion, global monetary conditions along with the recent decline in foreign holdings of Egyptian T-bills support maintaining rates in the upcoming MPC meeting on September 27.

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