



**Press Release  
November 6, 2008**

***The Central Bank of Egypt decided to keep its overnight deposit and discount rate unchanged at 11.5 percent per annum.***

In its meeting held on November 6, 2008, the Monetary Policy Committee (MPC) decided to keep the overnight deposit and lending rates unchanged at 11.5 percent and 13.5 percent, respectively.

Over the past six weeks, turmoil in the global financial markets has severely intensified, leading many central banks in developed and emerging countries to intervene in their respective domestic markets using all tools available to ease liquidity shortages and ensure that their money markets are orderly functioning. The effects on the Egyptian banking sector, however, have been minimal in light of prudent regulations and comfortable domestic liquidity conditions. In the meantime, domestic inflationary pressures are expected to ease supported by the significantly lower international commodity prices and the expected moderation in the domestic economic growth in light of the global slowdown.

**Domestic Inflation and Economic Growth**

For the first time since November 2007, annual headline CPI inflation declined to 21.5% in September compared to 23.6% in August, as domestic food inflation has fallen from 31% to 25.6%. While inflation is still high, the pace of monthly acceleration is moderating, declining from an average of 2.27% between January 2008 and August to 0.27% in September. This comes on the back of a marked decline in international food prices and the softening of domestic inflationary pressures.

Generally speaking, most of the upside risks to inflation, discussed in the previous MPC meeting, have eased. This comes on the backdrop of the improving outlook for international commodity prices in light of the projected slowdown in global economic activity and the consequent moderation in domestic economic growth. Against this background, the domestic inflation outlook is better than previously envisaged.

While the impending global recession will impact exports of goods and services negatively, growth momentum that has been building up over the past three years will contribute to a soft landing for the Egyptian economy, supported mainly by domestic demand. A deeper and more protracted global recession than currently projected presents a downside risk to domestic economic growth. Incoming data over the next few months will be crucial to assess the domestic growth outlook.

**The Banking System**

The Egyptian banking system continues to be relatively isolated from the global turbulence as domestic banks have very limited exposure to the failed and stressed global financial

institutions. Moreover, the exposure of domestic banks to risky assets has been marginal since there are virtually no investments in structured credit products or other impaired derivative products. Prudent regulatory surveillance and effective banking supervision, which have been strengthened under the Central Bank of Egypt's Banking Sector Reform Program launched in 2004, have ensured that the Egyptian banking system continues to function normally amid the global financial turmoil.

The stability of the domestic banking sector has also been aided by the high levels of balance sheet liquidity. Judging by the structure of the banking system's balance sheet, the share of wholesale funding has been marginal whereas retail deposits correspond to more than two thirds of the banking system's liabilities. Accordingly, the financing of loan expansion originates predominantly from domestic deposits, which results in minimal dependence on funds from foreign markets. The overall loans-to-deposit ratio is around 55 percent, with a high proportion of assets being short term and liquid. Furthermore, Egyptian corporates obtain most of their finances domestically which makes them highly sheltered from the freeze in international money markets and the higher cost of funds in light of higher international risk aversion. Hence, the domestic banking system can be characterized as highly liquid and well capitalized. Moreover, the money and foreign exchange markets have been operating in an orderly manner and remain very liquid.

Therefore, it becomes clear that the fundamental requirements for the domestic banking sector to continue to function smoothly are entrenched in the system, lending the necessary support to the economy's growth momentum going forward.

### **Monetary Policy Stance**

Given the monetary tightening since February, the MPC believes that the current level of the policy rate is supportive of disinflation. Yet, ongoing uncertainties surrounding the projected slowdown of external demand pose downside risks to domestic economic growth. The MPC will consider a measured rate cut when needed, so as to prevent economic growth from falling below its potential.

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