Central Bank of Egypt

Press Release
August 17, 2017

In its meeting held on August 17, 2017, the Monetary Policy Committee (MPC) decided to keep the overnight deposit rate, overnight lending rate, and the rate of the Central Bank of Egypt's (CBE) main operation unchanged at 18.75 percent, 19.75 percent, and 19.25 percent, respectively. The discount rate was also kept unchanged 19.25 percent.

Since the MPC meeting on July 6, 2017, annual headline inflation inched up to 33.0 percent in July 2017, after remaining broadly unchanged at 29.8 percent in June 2017 compared to May 2017, where it registered the first decline since October 2016. Meanwhile, annual core inflation rose to 35.3 percent in July from 31.9 percent in June, after declining between March and May.

The recent increase reflected an expected upward adjustment of regulated hydrocarbon prices and a higher VAT rate. In addition to the direct effects of higher hydrocarbon prices on headline inflation, several CPI items echoed indirect effects, notably food, and services such as inland transportation, cafés and restaurants and outpatient services. Moreover, other regulated prices also rose such as tobacco, public hospitals, and landline telephones, while higher prices of motor oils and medical products increased the contribution of retail items somewhat.

Prices of retail items have not been contributing to headline inflation since March 2017, except in June due to the seasonal effect of Eid-El-Fitr on clothing prices. Services have been also only contributing marginally to headline inflation since January 2017, except in May due to higher prices of pilgrimage. Both exceptions reflected a delayed impact of the depreciation of the Egyptian pound on seasonal items. In the meantime, after bottoming in March 2017, the contribution of core food inflation rose somewhat between April and June and by a greater extent in July, while the contribution of volatile food inflation has been declining, except for an uptick in July, leading core food items to be the main contributor to food inflation since May.

Meanwhile, annual real GDP growth continued to strengthen in the quarter ending June 2017 and leading activity indicators solidify this improvement. In the quarter ending June, real GDP reportedly grew by 4.9 percent, up from 4.3 percent, 3.8 percent and 3.4 percent in the preceding quarters. This coincided with the narrowing of the unemployment rate to below 12.0 percent in the quarter ending June 2017 from 12.0 percent, 12.4 percent and 12.6 percent in the preceding quarters. Available data up to March showed that the structure of economic growth shifted towards increased sustainability with declining contribution of consumption and increasing contribution of net exports as well as investment by a lesser extent. Tourism, natural gas, trade, construction and non-petroleum manufacturing were the main sectors driving economic growth.

Given the strengthening of demand indicators, in addition to the strong second-round effects of the economic reform measures implemented in November 2016, and in anticipation of the second-round effects of the subsidy-reform measures implemented in June and July 2017, the MPC had raised the CBE's key policy rates to achieve the targeted disinflation path over the specified horizon. Consistent with the tighter monetary policy stance, annual reserve money (M0) growth adjusted by overnight deposits and seven-day deposit auctions shrunk to reflect the absorption of excess liquidity via longer-term operations. The MPC reiterates that it tolerates higher inflation as a result of first-round effects of such supply shocks and uses its monetary policy tools to contain the second-round effects.

Incoming information since the MPC last met were broadly as expected, accordingly, the MPC judges that current policy rates remain consistent with achieving the inflation target of 13 percent (+/- 3 percent) in 2018 Q4 and single digits thereafter. Nevertheless, there are several risks surrounding the baseline inflation outlook, notably the evolution of inflation expectations, demand-side pressures as well as the magnitude of any subsidy-reform measures and their second-round effects. The materialization of such risks could lead to a stronger than projected loosening or tightening of the committee's stance to ensure that the inflation outlook is consistent with the targeted disinflation path.

The MPC will continue to closely monitor all economic developments as well as the balance of risks, and will not hesitate to adjust its stance to offset anticipated upside or downside deviations from the inflation target.

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