Central Bank of Egypt

Press Release

May 21, 2017

In its meeting held on May 21, 2017, the Monetary Policy Committee (MPC) decided to raise the overnight deposit rate, overnight lending rate, and the rate of the Central Bank of Egypt's (CBE) main operation by 200 basis points to 16.75 percent, 17.75 percent, and 17.25 percent, respectively. The discount rate was also raised by 200 basis points to 17.25 percent.

Headline inflation registered 1.69 percent (m/m) in April 2017, recording its third consecutive decline due to fading cost-push pressures after averaging 4.01 percent (m/m) between November 2016 and January 2017. Meanwhile, annual headline inflation registered 31.46 percent. Monthly inflation during April was mainly driven by volatile and core food items, while non-food items remained broadly unchanged. Accordingly, core inflation which excludes volatile food items grew by 1.10 percent (m/m) in April, recording a slight increase after decelerating in February and March from the average 4.89 percent (m/m) registered between November 2016 and January 2017. Nevertheless, as monthly core inflation was lower than the respective month of the previous year, the annual rate declined for the second consecutive month to record 32.06 percent.

While the previous tightening of policy rates and the consistent reduction of short-term excess liquidity have so far successfully managed to contain underlying inflation excluding supply-shocks, as evident in the inflation developments above, the balance of risks surrounding the inflation outlook has tilted more strongly to the upside with recent economic and monetary data releases pointing to strengthening demand-side pressures. Furthermore, the MPC envisages risks related to inflation expectations resulting from elevated annual inflation levels despite the continued moderation of monthly rates. Consequently, the MPC decided that tightening monetary conditions are warranted in commitment to its price-stability mandate.

Information received since the MPC met in March show continued improvement of economic activity and a reduction of unemployment. Annual real GDP grew by 3.9 percent in 2016/17 Q3, strengthening from the 3.8 and 3.4 percent recorded in the preceding quarters as well as from the 3.6 percent recorded in 2015/16 Q3. This coincided with the narrowing of the unemployment rate to 12.0 percent in 2016/17 Q3 from 12.4 and 12.6 percent in the preceding quarters.

From the monetary perspective, annual broad money growth has been strongly affected by revaluation effects of its foreign currency components. However, annual broad money growth has also increased excluding revaluation effects due to the recovery of net foreign assets, evident by the CBE's international reserve accumulation, as well as higher loans to the private sector in domestic currency.

Developments in the external environment show that there has been some firming of international commodity prices primarily due to higher oil prices while food price increases were relatively tame. Meanwhile global inflation and economic growth continue to maintain weak pressures on domestic prices, despite their recent recovery.

To further anchor inflation expectations, the MPC decided to increase transparency regarding the targeted disinflation path in its regular statements as well as in the quarterly series of the monetary policy report introduced in March 2017. In accommodation of first-round effects of supply-shocks, the elevated annual headline inflation rate will be temporarily tolerated before it is targeted to decline to 13% (+/- 3%) by 2018 Q4 and to single-digits thereafter. The MPC believes that this target path is appropriate to minimize undesirable macroeconomic volatility. Achieving low and stable inflation over the medium-term supports real incomes and sustains achieved competitiveness gains, which represents a challenge according to Egypt's economic history.

Monetary policy tools are utilized to anchor inflation expectations, contain demand-side pressures and second-round effects resulting from supply shocks that may lead to deviations from inflation targets, as well as to achieve reserve money targets that were designed to be consistent with the inflation targets. The MPC believes that such a flexible monetary targeting framework is appropriate under the liberalized exchange rate regime.

Against this background, the MPC judges that hiking the CBE's key policy rates is consistent with the targeted disinflation path, and reiterates that the objective of its tighter stance is not to offset effects of supply-shocks, rather to contain underlying inflation excluding supply shocks that is affected by inflation expectations and the build-up of demand-side pressures.

The MPC will continue to closely monitor all economic and monetary 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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