

Divergence Between International Food Prices and Domestic Prices Amid Surging Inflation

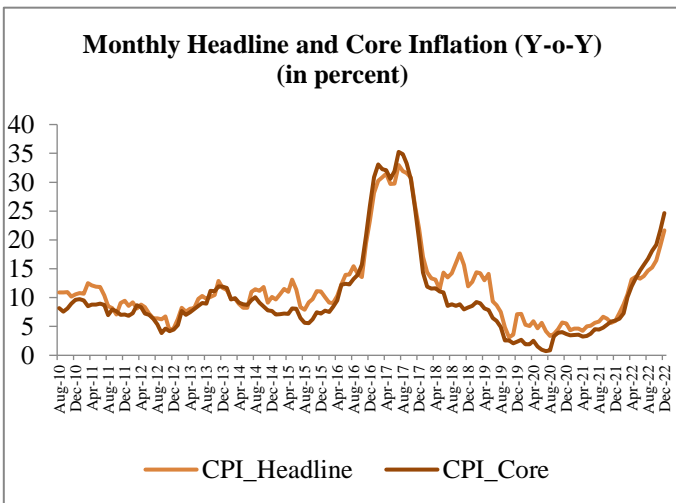
Tuesday 10th of January 2023

Recent dynamics in headline and core inflation ...

Urban headline inflation (Y-o-Y) surged in December to 21.3% up from 18.7% a month earlier. The current acceleration is a continuous increase for six months in a row. In the meantime, core inflation continues on its rapid acceleration to register a double digit since last March to reach 24.4% in November compared to 21.5% a month earlier. This has been mainly attributed to the accelerated domestic food prices.

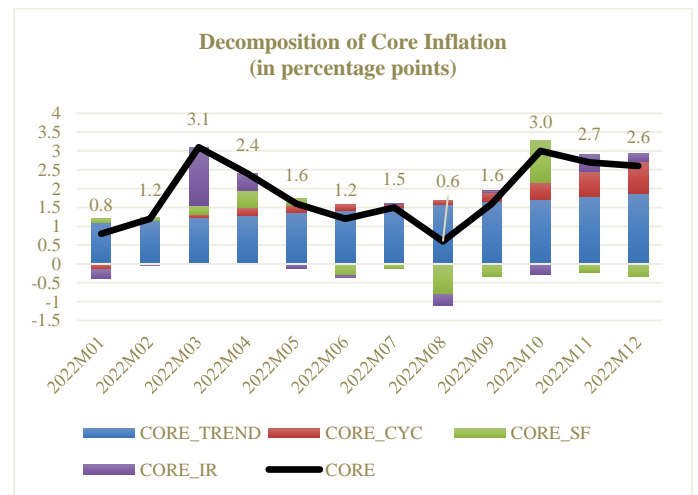
Source: CAPMAS and Central Bank of Egypt.

...Sources of Demand-driven Inflation ... it has



been observed that there is a continuous build-up in Y-o-Y core inflation since the beginning of 2022 jumping from a single digit of 6.4% in January to reach 24.4% in December, which has been accompanied by growing inflation expectations. Also, cyclical factors started to manifest during December's figure accounting for 32% of the monthly core inflation, implying that demand

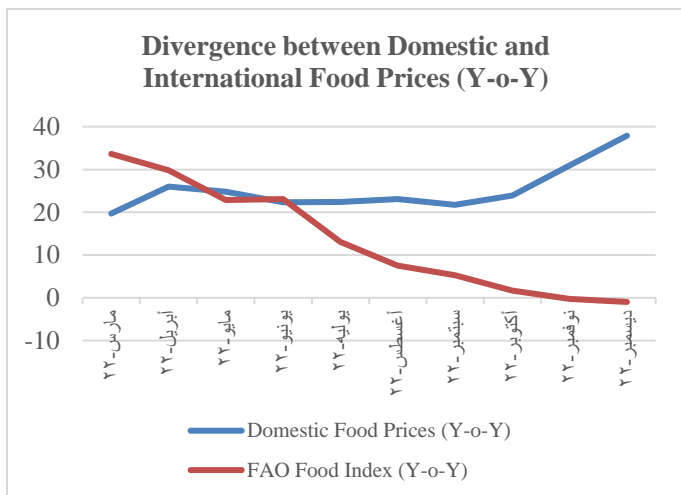
surpass the supply of goods and services. Moreover, the contribution of the pass-through effect appeared to be positive to core inflation for two consecutive months. Such dynamics, shed lot of alarming signs for the policymakers at the Central Bank, wherein, prudent measures have to be taken immediately to curb expected inflationary pressures for the rapid-paced depreciating EGP.



Source: MAP's Estimates, MPED and CBE.

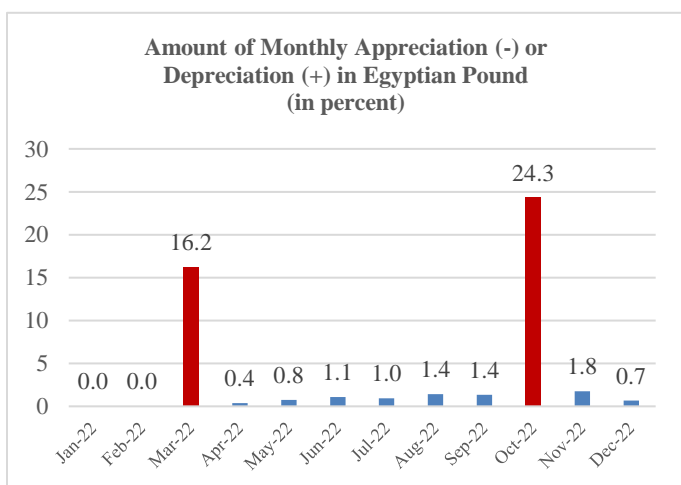
Some Findings and Facts about Food Inflation...

In analyzing the relationship between the international food prices and domestic prices, it has been observed that starting from June 2022, there existed a divergence between the two, wherein, international food prices proxied by the FAO index started to slow down (Y-o-Y), meanwhile, the domestic food prices started to surge gradually till it reached 37.9% in December 2022.



Source: FAO and Tradingeconomics.com.

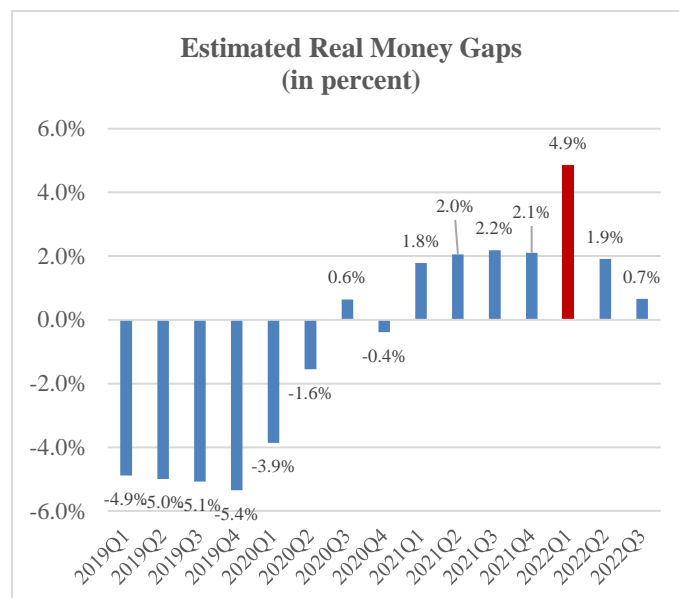
Exchange Rate Dynamics and Domestic Inflation... The EGP value has been devaluated with an accumulated amount of 49% since last February. Such decisions have their repercussions on the domestic inflation and particularly food prices. The pass-through effect has been estimated at 30%-35%.



Source: Central Bank of Egypt.

Some insights about Real Money Balances... Despite the fact that real money gaps are still in the positive zone, yet it is sloping downwards to record only 0.7% during Q3 2022, after it surged to 4.9% during Q1 2022. Worth to note, the expansion in the EGP during the

first quarter of 2022 had its negative externalities on the value of the EGP starting March 2022 and still pressing for further depreciation, which gave no room for more monetary expansion. On the contrary, the CBE now adopt a contractionary policy by hiking the interest rate along with the introduction of new deposit certificates that payoff 25% as an exceptional step to absorb the excess liquidity and to minimize the dollarization tendency within the banking sector.



Source: MAP's Estimates, MPED and CBE.