

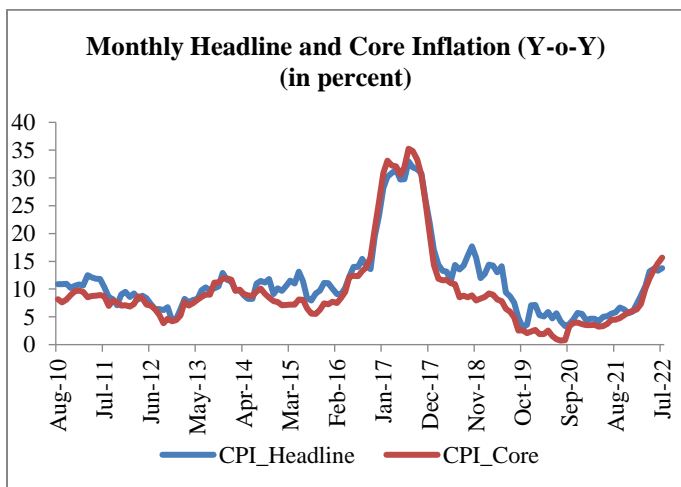


Limited Supply-Side Shocks due to Fuel Price Hikes in July 2022

Wednesday 10th of August 2022

Recent dynamics in headline and core inflation ...

Urban headline inflation (Y-o-Y) increased in July to 13.6% up from 13.2% a month earlier. The monthly dynamics has been also significantly accelerated by 1.3% in July compared to negative 0.1% during the previous month. Meanwhile, core inflation is still on the upward trajectory surging to 15.6% in July compared to 14.6% a month earlier. This has been accompanied by a monthly rate of 1.5% in July up from 1.2% in June 2022. Worth to mention, the monthly acceleration in headline inflation has been caused by movement in fuel prices; an increase ranging from 50 piasters to EGP 1 per liter in the local markets including the Diesel, the latter price has gone up for the first time in three years.



Source: CAPMAS and Central Bank of Egypt.

...Sources of demand-driven inflation ... The monthly dynamics for the period January-June 2022, indicates that core inflation has been the downward trajectory, with a record high of 3.1% in March, emerged

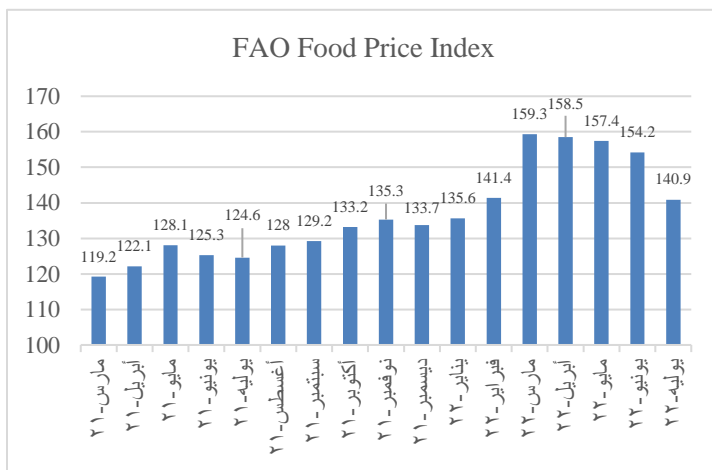
primarily from irregular factors which is assumed to be the pass-through effect accounting for 1.6 percentage points. Nevertheless, implied inflation followed by the cyclical factors appeared to be the main contributors to core inflation during the last 6 months. Inflation expectations started to build-up contributing by 56% of the core inflation dynamics. Coming to the cyclical factors emerged from positive real money gaps, contributing by 22% of the core dynamics during H1 of 2022.

Core Inflation Heat Map for the Period Jan-Jun 2022



Source: MAP's Estimates, MPED and CBE.

...Inflation upside and downside risks... In light of the recent economic dynamics, it is noticed that the main source of inflation emerged from domestic sources primarily the positive real money gaps which represent a forward-looking indicator for the inflationary pressures and has been manifested on a double-digit core inflation for five consecutive months. In the meantime, international upside risks on inflation through the commodity channel started to tame out in April 2022 and onwards as represented in the FAO food price index. It has

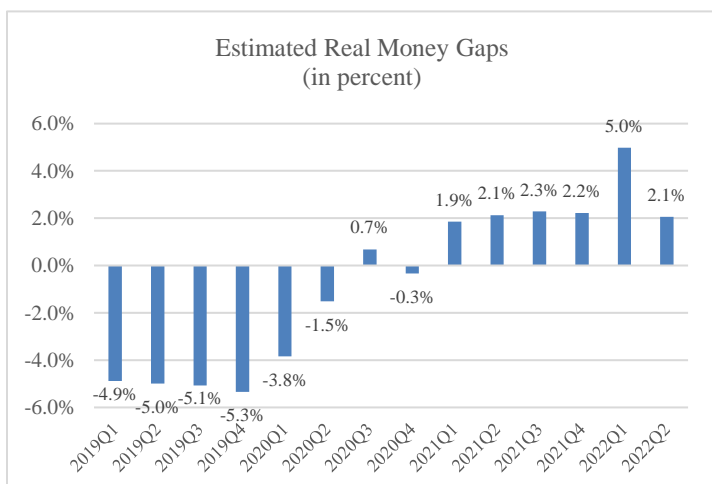


softened since then supported by the eased cereal and vegetable oil prices, according to FAO.

Source: FAO.

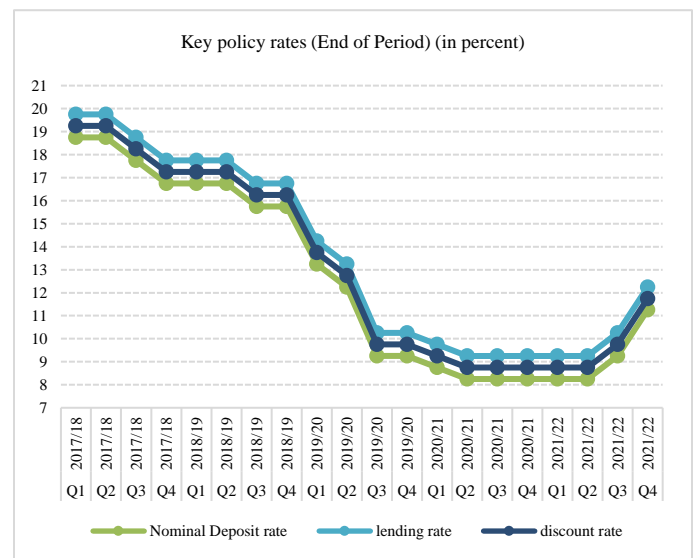
Source: Central Bank of Egypt.

...Expected Monetary Policy Decision... In light of the recent inflation dynamics, it is obvious that headline inflation is breaching the targets previously set by the Central Bank to be $7\% \pm 2\%$, for the fifth month in a row.

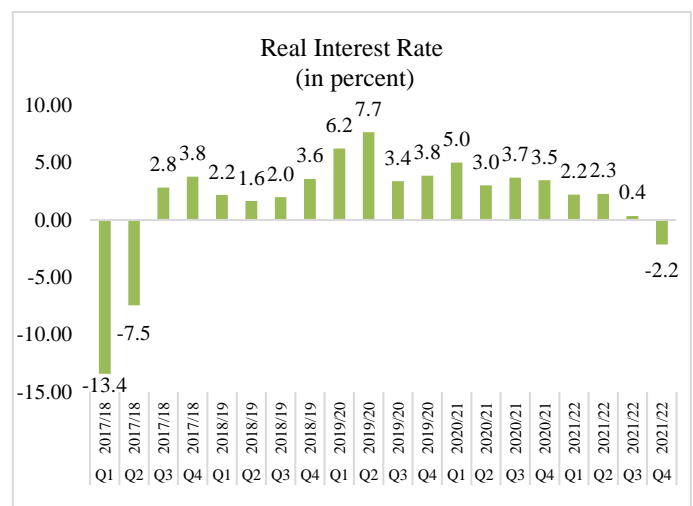


Also, the core inflation is well-above the 10-years average of 9.8%. Knowing that the major source of inflation is purely domestic and demand-pull risks as previously presented. In the sense, that the economy is expecting the crystallization of the second-round effects of the fuel prices hikes took place during July.

In this context, it is recommended that the monetary policy committee would take a tightening decision in its upcoming meeting that is scheduled on August 18th. The interest rate hike is recommended to be ranging between 100-150 basis points to anchor inflation expectations and curb the inflationary pressures expected to appear in the near future.



Source: Central Bank of Egypt.



Source: CAPMAS and Central Bank of Egypt.