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Terminating the CBE's Repatriation Mechanism – Initial View

The Central Bank of Egypt (CBE) has just decided to terminate the repatriation mechanism as of Tuesday, 4 December 2018, for fresh funds entering local debt and equity markets. Below, we highlight our key takeaways:

1) **The original purpose of the mechanism:** The CBE has been utilizing the repatriation mechanism to guarantee FX liquidity for investors. The mechanism guarantees the exit for investors at the market rate with no backlogs. This was intended to clear the uncertainty over FX availability and help boost investors' confidence and – therefore – stimulating inflows.

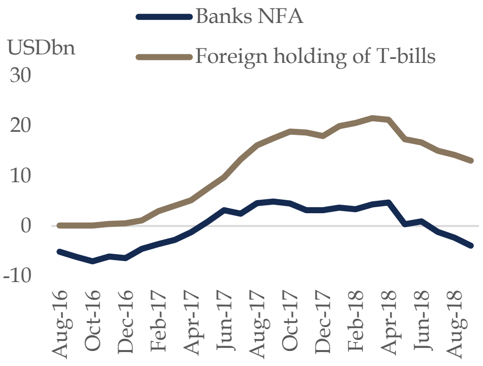
2) **We are not surprised at all; the repatriation mechanism was temporary:** One of the key highlights of Egypt's reform program supervised by the International Monetary Fund (IMF) is to adopt a flexible FX regime. The mechanism, somehow, was considered by the IMF to be some sort of intervention in the FX market and was preferred to be phased out. Egypt authorities, however, preferred to keep the mechanism for some time to enhance investor confidence. The CBE preferred a gradual "shift" towards the interbank market, when it introduced a repriced mechanism a year ago "effective 3 December 2017", encouraging more investors to switch their transactions to the interbank market. Now, the CBE sees it is time for the interbank to be the main marketplace for FX, hence terminating the repatriation mechanism.

3) **The termination brings no particular burdens on banks:** The repatriation mechanism will be terminated for new fresh entries but will continue to be operational for funds outstanding before 4 December 2018. Thus, banks will only deal with new outflows/inflows into the country, thus placing no additional pressure on their foreign exchange positions.

4) **Banks likely to witness more inflows in the near term:** Foreign investors who consider investing in Egypt's debt and equity markets now have only one gateway to use (the interbank system). We believe this will revive banks' net foreign assets in the near term but highly subject to international investors' appetite for Egyptian assets and net trading position as net buyers/sellers.

5) **FX market might witness higher volatility, yet not on a very wide scale:** We believe the termination was mainly a move towards a more flexible FX market. This, by definition, may trigger a wider range between bids and asks at banks. However, the mid-point of USD/EGP rate (that is, the average around which the price hovers) is not expected to move away from current levels (high 17s per USD). We also rule out any negative effect on official reserves of the CBE.

Foreign holdings of T-bills have declined, placing some pressure on banks' NFA



Source: CBE

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