PRIME

The Egyptian Banking Industry

Impact	NEGATIVE
Degree	MODERATE

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The RRR Effect

The good, the bad, and the ugly

The surprise decision: Last Thursday, the Central Bank of Egypt (CBE) surprised the market and increased the required reserve ratio (RRR) from 14% to 18% while keeping interest rates unchanged. This was against our expectation of a 100bps hike. Instead, the CBE preferred to hike the RRR, one of the monetary tools it can use to control liquidity in the banking system as a part of its tightening policy. According to the CBE, accelerating inflation (14.6% in August vs. 13.6% in July) is supply induced, which rendered the decision to hike the RRR more plausible than hiking interest rates in order to curb inflation; it will reduce the money supply. By way of background, this is not the first time for the CBE to use this monetary tool. The RRR has been raised before from 10% to 14% post the EGP floatation in 2016.

What does a higher RRR mean for banks? A higher RRR usually has a negative connotation, reducing the amount of money Egypt banks can lend, hence denting their profitability. However, each bank will be impacted differently, depending on several factors that we highlight in this note. In order to calculate the effect of the higher RRR decision on each bank, we have to first take into consideration the following:

- Not all deposits are subject to the ratio. Indeed, the RRR excludes long-term deposits (i.e. maturity of 3+ years), and SME loans are excluded.
- We believe the expected upcoming rate hikes of 100-200bps through the end of the year will offset the impact of the 4pp higher RRR.
- We also think that as the impact of the decision materializes, the lack of liquidity in the banking system will allow banks to pressure Treasury yields upward, which would somehow compensate banks albeit partially.

The good, the bad, and the ugly: To gauge how each EGX-listed bank would theoretically be impacted by the CBE's decision to hike the RRR, we used banks' June 2022 financials. In our opinion, this is the worst-case scenario. The table on Page 2 illustrates the following on a pretax basis since each bank's effective tax rate would differ depending on its income structure:

(1) The amount each bank is required to shell out to meet the new 18% RRR.
(2) Annual interest income lost.
(3) Annual impact per share.
(4) Impact as a percentage of the market price.
(5) Impact as a percentage of H1 2022 annualized earnings.
(6) Impact as a percentage of H1 2022 book value of equity (BVOE).

All else the same (i.e. assuming no move by banks on the volume or price sides), we believe that the most impacted banks will be Suez Canal Bank [**CANA**], Egyptian Gulf Bank [**EGBE**], and Export Development Bank of Egypt [**EXPA**], while the least impacted banks are Credit Agricole Egypt [**CIEB**], Faisal Islamic Bank of Egypt [**FAIT**], Commercial International Bank [**COMI**], and QNB Alahli [**QNBA**].

Summary of impact

Ticker	Degree of impact
CANA	↘↘↘
EGBE	↘↘↘
EXPA	↘↘↘
SAUD	↘↘
HDBK	↘↘
ADIB	↘↘
QNBA	↘
COMI	↘
FAIT	↘
CIEB	↘

Key:
↘↘↘ High / ↘↘ Moderate / ↘ Low

Source: Prime Research.

Summary impact* on EGX-listed banks (figures in EGPmn)

	Cash kept at end of H1 2022 with the CBE under …		(1)	(2)	(3)	(4)	(5)	(6)
	14% RRR	18% RRR	Additional reserve required	Interest income lost	Impact per share **	as % of market price	as % of H1 2022 annualized earnings	as % of H1 2022 BVOE
CANA	6,990	8,987	1,997	174	0.60	8.2%	32.5%	3.7%
EGBE	7,319	9,410	2,091	230	0.03	6.3%	28.1%	4.5%
EXPA	9,190	11,815	2,626	273	0.52	5.9%	22.5%	3.9%
SAUD	5,635	7,245	1,610	168	0.63	5.1%	10.7%	2.5%
HDBK	7,302	9,388	2,086	241	1.59	4.2%	10.0%	2.5%
ADIB	5,246	6,745	1,499	162	0.41	2.9%	8.3%	2.2%
QNBA	23,125	29,732	6,607	698	0.32	2.1%	7.9%	1.5%
COMI	36,066	46,370	10,305	1,079	0.36	1.4%	6.9%	1.6%
FAIT	8,757	11,259	2,502	241	0.40	2.9%	6.9%	1.4%
CIEB	2,363	3,038	675	68	0.05	0.9%	3.4%	0.8%

* All analysis is on a pretax basis since each bank's effective tax rate would differ depending on its income structure.
** Impact per share for EGBE is in USD.
Source: Bank reports, Prime Research.

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