Policy rate kept unchanged at 15% for the next six weeks

- In line with ours and general market expectations, the Monetary Policy Committee (MPC) of SBP has decided to keep the policy rate unchanged at 15% till its next meeting scheduled on October 10th, 2022.
- The key factor highlighted by the MPC for maintaining a status-quo is to take a pause and allow the transmission of the 800bps cumulative increase in policy rate since Sep'21, temporary administrative steps to curtail imports, and fiscal consolidation planned for FY23, to work its way through the system in the coming months.
- As part of its forward guidance is concerned, the MPC intends to remain data-dependent, focusing on MoM inflation, inflation expectations, developments on the fiscal and external fronts, as well as global commodity prices and interest rate decisions by major central banks.
- The MPC highlighted three key developments from its previous meeting that include 1) inflation rising to 24.9% with core inflation also inching up, which was however expected, 2) Jul'22 trade balance shrunk sharply and PKR appreciating around 10% against USD during Aug'22, and 3) scheduled meeting of the IMF Executive Board is expected to release a tranche of USD1.2bn under the seventh and eight reviews in addition to commitments of additional USD4bn being secured from friendly countries that are over and above external funding requirements for FY23.
- The MPC noted that both global commodity prices and the US dollar have fallen in recent weeks, in response to signs of a sharper than anticipated slowdown in global growth that is leading to market expectations that the US Federal Reserve tightening cycle may be less aggressive than previously anticipated. As a result, more emerging market central banks have started to hold policy rates in their recent meetings.
- The MPC noted that a greater slowdown in global growth would not be as harmful for Pakistan as for most other emerging economies, given the relatively small share of exports and foreign private inflows in the economy.
- On the domestic side, the MPC highlighted that most demand indicators have softened showing that economic activity has moderated.
- MPC maintains its real GDP growth estimates of 3-4% for FY23 after two successive years of growth at around 6% while the slowdown is expected as a result of tightening fiscal and monetary policies, which will eventually ease pressure on inflation and current account. The MPC highlighted recent heavy and prolonged monsoon season and the resultant flooding as a key risk to growth estimates.
- The MPC estimates FY23 current account deficit at around USD10bn (~-3% of GDP) compared to USD17.4bn (-4.6% of GDP) for FY22.
- The MPC reiterated that the external financing needs of the country for FY23 are over-funded and the foreign exchange reserves with the SBP are expected to increase from USD7.9bn now to USD16bn during FY23.
- SBP in its briefing to the analysts highlighted that short-term external debt is around 6% of the total external debt and there is not concern on the maturity profile of external debt.

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- However, it was highlighted that there is a dire need to increase private flows to diversify the funding sources of the balance of payments such as FDIs and corporate debt etc.
- The MPC appreciated the governments aim at achieving 3% fiscal consolidation during FY23 along with a primary surplus of 0.2%. Besides the fact that these targets are committed with the IMF and are necessary for the continuation of the IMF program and the subsequent quarterly reviews, these would be appropriate to cool the economy and ensure a reduction in inflation and current account deficit.
- MPC maintained its inflation target for FY23 are 18-20% with the monthly readings expected to peak during the first quarter of the ongoing year.
- By the end of FY23, MPC expects a significant reduction in inflationary out-turns as a result of policy measures and high base-effect.
- Furthermore, MPC maintained its view that inflation is expected to a long-term range of 5-7% by the end of FY24.

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Annexure

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