Economy

# Status Quo Maintained; Policy Rate Appropriate to Anchor Inflation

- In the latest Monetary Policy Announcement (link) the State Bank of Pakistan (SBP) kept policy rate unchanged at 22% in line with market expectation of status quo.
- MPC noted that inflation outlook remains within target range with CPI expected to come down from Oct-23 due to base effect and maintain its downward trajectory especially in 2HFY24. The Committee highlighted that volatility in global oil prices due to middle east conflict and recent increase in gas prices pose risk for inflation and current account. However, alignment of open market and interbank exchange rate, fiscal consolidation and improved supply dynamics would likely offset these risks.
- Considering the reasons highlighted by MPC for status quo which includes expected deceleration in inflation and real rates in positive territory, it may seem that Policy Rates may have peaked. With recent hike in gas prices and volatility in global oil prices, inflation outlook may worsen, however, recent appreciation of PKR, improved growth outlook on the back of promising Kharif crop, increase in LSMI, reduction in fiscal deficit and improvement in supply dynamics are likely to keep inflation under control.

## SBP keeps Policy Rate Unchanged

In the latest Monetary Policy Announcement (link) the State Bank of Pakistan (SBP) kept policy rate unchanged at 22% in line with market expectation of status quo. SBP apprised that real rates are currently significantly positive based on 12 month forward looking basis and remain appropriate to anchor inflation towards target range of 5-7% by end of FY25.

MPC noted that inflation outlook remains within target range with CPI expected to come down from Oct-23 due to base effect and maintain its downward trajectory especially in 2HFY24. The Committee highlighted that volatility in global oil prices due to middle east conflict and recent increase in gas prices effective 1st-Nov-2023 pose risk for inflation and current account outlook. However, alignment of open market and interbank exchange rate, fiscal consolidation and improved supply dynamics would likely offset these risks.

**Exhibit: Monetary Policy Rate Decision**

| | Current | Previous | Chg. (bps) |
|---|---|---|---|
| **Target Policy Rate** | **22.00%** | **22.00%** | **0** |
| Discount rate (Ceiling Rate) | 23.00% | 23.00% | 0 |
| Floor Rate | 21.00% | 21.00% | 0 |

Source: SBP, IGI Research

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**Exhibit: National CPI Heat Map**

| | Sep-23 | Aug-23 | Jul-23 | Jun-23 | May-23 | Apr-23 | Mar-23 | Feb-23 | Jan-23 | Dec-22 | Nov-22 | Oct-22 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **General** | **31.4** | **27.4** | **28.3** | **29.4** | **38.0** | **36.4** | **35.4** | **31.5** | **27.6** | **24.5** | **23.8** | **26.6** |
| Food | 33.1 | 38.5 | 39.5 | 39.5 | 48.7 | 48.1 | 47.2 | 45.1 | 42.9 | 35.5 | 31.2 | 36.3 |
| Transport | 31.3 | 23.0 | 13.6 | 20.3 | 52.9 | 56.8 | 54.9 | 50.4 | 39.1 | 41.2 | 44.2 | 53.4 |
| Utility/Rent | 29.7 | 6.2 | 10.8 | 11.6 | 20.5 | 16.9 | 17.5 | 13.6 | 7.8 | 6.9 | 9.9 | 11.9 |
| Essentials | 18.2 | 16.5 | 16.7 | 16.7 | 17.5 | 16.9 | 16.7 | 14.7 | 14.4 | 14.4 | 15.1 | 14.7 |
| Disc. | 40.8 | 43.1 | 43.5 | 44.9 | 49.4 | 46.4 | 43.5 | 35.8 | 31.0 | 28.6 | 27.2 | 27.2 |

## Key takeaways from analyst briefing

SBP in its post MPS briefing highlighted key updates on CAD, debt repayments and foreign exchange reserves which included:

- Real rates remain in positive territory on a 12 month forward looking basis and inflation. MPC noted that currently policy rate is appropriate to anchor inflation down to target range of 5-7 by end of FY25.
- Total debt repayment for FY24 stands at US$ 24.5bn (US$ 21bn principal and US$ 3.5bn in interest) and out of which US$ 4.3bn (US$ 3.2bn principal and US$ 1.1bn in interest) has been repaid already in 4MFY24. Out of the remaining US$ 20.1bn, US$ 12.3bn is expected to be rolled over with most of it already confirmed. After excluding total roll over, total financing requirement stands at US$ 5.5bn for FY24.
- With CAD expected to be in the range of 0.5%-1.5% of GDP (US$ 1.5-5bn) and foreign exchange reserves of SBP at US$ 7.5bn, SBP expects that current position is sufficient to meet debt repayment requirements. Even without the committed inflows from IMF and multilateral partners, reserve position is sufficient to cover debt repayments whereas any inflows would further strengthen foreign exchange reserves.
- The Governor also highlighted that SBP has met all the quantitative targets set by IMF for Sep-end which includes forward swap ceiling of US$ 4.2bn, NDA ceiling of PKR 15tn, GoP's borrowing from SBP for budgetary support of PKR 4.7tn and floor on net international reserves of US$ 14.5bn. Furthermore, SBP is likely to meet foreign reserve target of US$ 10.4bn by Jun-24.
- SBP highlighted that currency in circulation was reduced due to unwinding of seasonal effect such as Umrah/Haj, higher rates on saving account and economic uncertainties have subsided.

- SBP also noted that there has been improvement in Auto, cement and POL sales evident from LSMI data, which has increased lately. Initial estimates of Kharif crop looks promising and points toward a positive outlook for FY24.

## Outlook

Considering the reasons highlighted by MPC for status quo which includes expected deceleration in inflation and real rates in positive territory, it may seem that Policy Rates may have peaked. With recent hike in gas prices and volatility in global oil prices, inflation outlook may worsen, however, recent appreciation of PKR, improved growth outlook on the back of promising Kharif crop, increase in LSMI, reduction in fiscal deficit and improvement in supply dynamics are likely to keep inflation under control. Thus, we expect that interest rates have peaked for now and monetary easing may be witnessed earlier than expected which is reflected from higher participation in recent TBill auction and drop in 12M PKRV rates.

**Exhibit:** CPI likely to drop from Oct-23 onwards and continue its downward trajectory with real rates also positive on a 12 month forward looking basis.

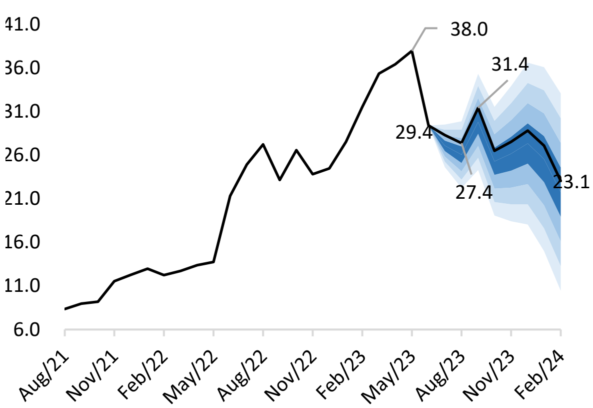
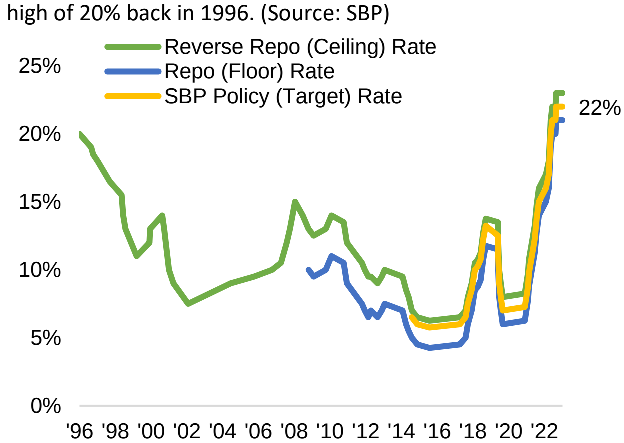



**Exhibit: Pakistan Policy Rate (historical)**

Discount rate of 23% remains at historic high against previous high of 20% back in 1996. (Source: SBP)



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