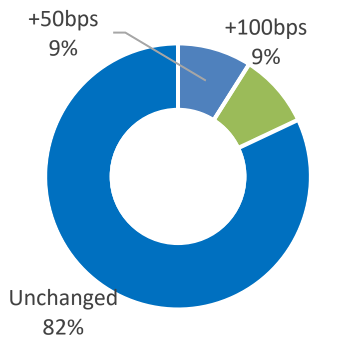
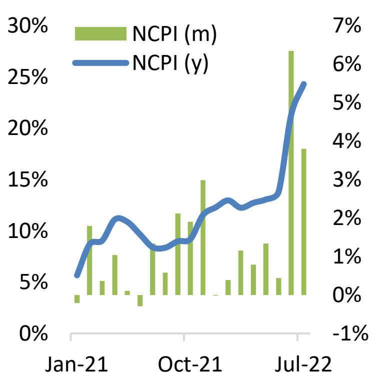
Economy

Exhibit: Majority participants expecting no change in policy rate



Source: IGI Research, CFA Soceity Pakistan

Exhibit: Annual and Monthly CPI



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Monetary Policy Statement

Monetary Policy to Remain Unchanged As Demand Drops Sharply

- The State Bank of Pakistan (SBP) is scheduled to announce Monetary Policy Statement (MPS) for the next two months on Monday 22nd August, 2022. For the upcoming monetary policy review we expect policy rate to remain unchanged at 15%.
- Fore mostly, we consider the significant drop witnessed in sales number of Automobile (down by 48% since Apr-22), Cement (down by 44% since Apr-22) and POL (down by 35% since Apr-22). The effect of slowing demand is also reflective of recent import numbers. As of Jul-22 provisional data country's import bill receded to US$ 4.9bn from US$ 7.9bn recoded in Jun-22; a decline of 37%m/m.
- Start of FY23 global oil prices have started to ease down. As of latest Arab Light oil prices are currently trading close to US$ 104/bbl down by 11% since Jul-22; US$ 117/bbl. This will come as a major relief on domestic inflation front

The State Bank of Pakistan (SBP) is scheduled to announce Monetary Policy Statement (MPS) for the next two months on Monday 22nd August, 2022. We present our preview on the likely policy rate decision and reasons.

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For the upcoming monetary policy review we expect policy rate to remain unchanged at 15%. This is pretty much in-line with market consensus whereby a recent survey held by CFA Institute of Pakistan, 82% respondents expect rate to remain unchanged, whereas 18% expect the rate to rise.

We base our premise on;

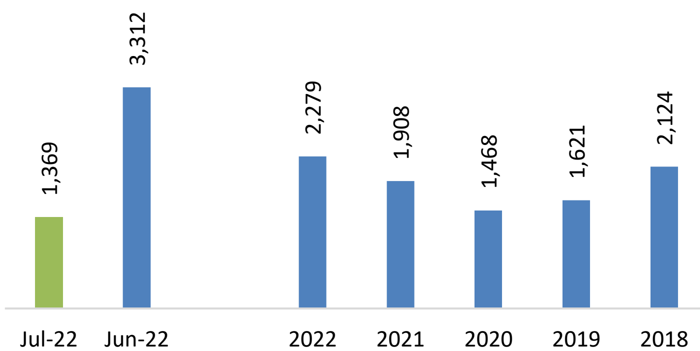
1# Demand Showing Signs of Slow Down…

Sales showing a rapid fall; a leading indicator of slowing demand: Fore mostly, we consider the significant drop witnessed in sales number of Automobile (down by 48% since Apr-22), Cement (down by 44% since Apr-22) and POL (down by 35% since Apr-22). This significant blow to sales numbers is in part due to sharp rise in product prices, a factor of elevated global commodity prices, administrative energy price increases, local currency depreciation and due to previous monetary tightening (since Nov-21 SBP has raised policy rates by 6.75%).

Current account deficit has started to normalise; import curtailment: The effect of slowing demand is also reflective of recent import numbers. As of Jul-22 provisional data country's import bill receded to US$ 4.9bn from US$ 7.9bn recoded in Jun-22; a decline of 37%m/m. Decline in petroleum products & crude import has been a major contributor to this sharp decline witnessed during the month of Jul-22.

Significant slowdown in Import of Petroleum Products: In terms of quantity overall petroleum products & crude declined to 1.37mn Ton during Jul-22 compared to previous month of Jun-22 of 3.3mnTons; that's nearly 60% decline. The number is even less when compared to average monthly import during the COVID19 led period (2019-2021) whereby average monthly sales were about 1.7mnTons.

Exhibit: Petroleum products & crude imports
Imports bill of Jul-22 for Petroleum products and Crude shows a significant decline in quantity, even less than Covid-19 period.



Source: IGI Research, PBS

With import moderating the likely relief is expected on country's current account deficit. To recall, Jun-22 c/a deficit reached US$ 2.3bn taking FY22 total c/a deficit to US$ 17.4bn or 4.6% of GDP. The latest monetary policy statement issued in Jul-22, also hinted to decline in overall imports amid import curtailment measures taken by the government and thus improvement is expected in country's C/a deficit.

2# Global prices have started to ease

Start of FY23 global oil prices have started to ease down. As of latest Arab Light oil prices are currently trading close to US$ 104/bbl down by 11% since Jul-22; US$ 117/bbl. This will come as a major relief on domestic inflation front, as recently oil prices have been key factor in driving inflation in the past three months.

Exhibit: S&P Indices shows major energy related prices on a declining trend

	Chg.	18-Aug-22	30-Jun-22
Petroleum	-13%	350.1	401.3
Energy	-8%	339.8	369.6
Industrial Metals	-1%	435.5	437.9
Food & Beverage	9%	7,597.6	6,940.4

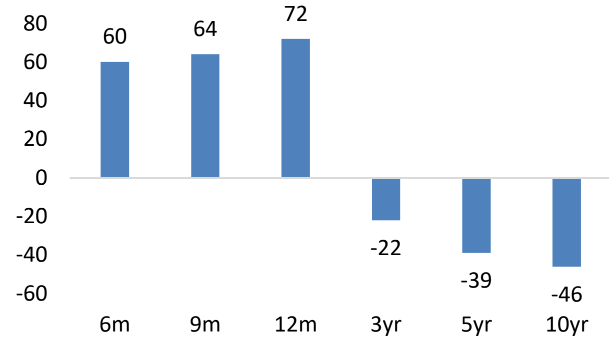
Source: IGI Research, S&P indices

Combined with declining global oil prices, only recently PKR has also found its footing against US$; gaining nearly 8% to reach 217 as of latest. The twin effect is likely to lower inflation expectation ahead. In fact responding to appreciating PKR and declining commodity prices, major automobile assemblers have reduced their ex-factory prices by around 5%-7%, and similarly has been the case for Steel sector.

3# Long-term Inflation trend depicted by yields suggest a downward trend

Slower demand and subsequently slower growth, is setting the stage for lower inflation ahead, and Market participants are expecting the similar scenario ahead. Depicted by sharp decline in long-term tenure yields compared to short-term.

Exhibit: Change in PKRV rates since the last MPS in Jul-22
Short-term yields have increased by an average of 65bps whereas long-term yields decline to a maximum of 46bps for 10 yr. bond.



Source: IGI Research, Bloomberg

Arguably, the decline is eminent but will be gradual. For Pakistan administrative increase in energy prices is still on the horizon; particularly electricity and gas tariffs. Moreover the impact of drop in oil prices and appreciating PKR may not fully feed into domestic prices as government will have to do with previous subsidy correction measures. "*Adjusting to administrative energy price hike and PKR depreciation will elongate the inflationary pain*" (link)

Outlook

Since the last monetary policy meeting, economic activities have further deteriorated and domestic demand has been severely hampered as evidently depicted by leading OMC, Auto and Cement sales in July. Global prices are normalizing and there is no imminent threat of imported inflation from external front, which seems to be stabilizing now.

"Going forward, the MPC will remain data-dependent, paying particularly close attention to month-on-month inflation, the evolution of inflation expectations and global commodity prices, as well as developments on the fiscal and external fronts."

-Monetary Policy Statement; July 2022 (Link)

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