Monetary Policy Statement

SBP raised the policy rate by 150bps to 13.75%.

In the latest Monetary Policy Announcement (link) the State Bank of Pakistan (SBP) raised the policy rate by 150bps to 13.75%; in-line with our expectation (link). Interest corridor now comes at ceiling (Reverse Repo) 14.75% and floor (repo) rate of 12.75%. The interest rates on EFS and LTFF loans are also being raised, these rates will be linked to the policy rate and will adjust automatically, while continuing to remain below the policy rate in order to incentivize exports.

Key points:

- Current monetary decision along with fiscal consolidation will help anchor down inflation expectations.
- External pressures remain elevated and the inflation outlook has deteriorated due to both home-grown and international factors.
- Domestically, an expansionary fiscal stance this year, exacerbated by the recent energy subsidy package, has fueled demand and lingering policy uncertainty has compounded pressures on the exchange rate.
- The economy has rebounded much more strongly than anticipated, growing by 5.7 percent last year and accelerating to 5.97 percent this year, as per provisional estimates.
- The Rupee depreciated further due both to domestic uncertainty as well as recent strengthening of the US dollar in international markets following tightening by the Federal Reserve

Outlook:

- **Inflation**: The MPC's baseline outlook assumes continued engagement with the IMF, as well as reversal of fuel and electricity subsidies together with normalization of the petroleum development levy (PDL) and GST taxes on fuel during FY23. As electricity and fuel subsidies are reversed, inflation is likely to rise temporarily and may remain elevated through FY23 before declining sharply during FY24 (5-7%). This baseline outlook is subject to risks from the path of global commodity prices and the domestic fiscal policy stance.
- **Growth**: On the back of monetary tightening and assumed fiscal consolidation, growth is expected to moderate to 3.5-4.5 percent in FY23.
- **Current Account Balance:** Current account deficit of around 4 percent of GDP this year, Next year, the current account deficit is projected to narrow to around 3 percent of GDP as import growth continues to slow with moderating demand and the recent measures taken by the government to curtail non-essential imports, while exports and remittances remain resilient.
- **External Fund gap**: This narrowing of the current account deficit together with continued IMF support will ensure that Pakistan's external financing needs during FY23 are more than fully met, with an almost equal share coming from rollovers by bilateral official creditors, new lending from multilateral creditors, and a combination of bond issuances, FDI and portfolio inflows.
- **US$/PKR parity**: As a result, excessive pressure on the Rupee should attenuate and SBP's FX reserves should resume their previous upward trajectory during the course of the next fiscal year.

Analyst
Abdullah Farhan
Abdullah.Farhan@igi.com.pk
Tel: +92 21 111 234 234 Ext: 912

Aariz Raza
Aariz.Raza@igi.com.pk
Tel: +92 21 111 234 234 Ext: 810

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IGI Finex Securities Limited
Research Analyst(s)
Research Identity Number: BRP009

Contact Details

Equity Sales

Faisal Jawed Khan	Head of Equities	Tel: (+92-21) 35301779	faisal.jawed@igi.com.pk
Zaeem Haider Khan	Regional Head (North)	Tel: (+92-42) 38303559-68	zaeem.haider@igi.com.pk
Muhammad Naveed	Regional Manager (Islamabad & Upper North)	Tel: (+92-51) 2604861-62	muhammad.naveed@igi.com.pk
Syeda Mahrukh Hameed	Branch Manager (Lahore)	Tel: (+92-42) 38303564	mahrukh.hameed@igi.com.pk
Shakeel Ahmad	Branch Manager (Faisalabad)	Tel: (+92-41) 2540843-45	shakeel.ahmad1@igi.com.pk
Zaid Farook	Branch Manager (Stock Exchange) Karachi	Tel: (+92-21) 32462651-52	zaid.farook@igi.com.pk
Asif Saleem	Equity Sales (RY Khan)	Tel: (+92-68) 5871652-56	asif.saleem@igi.com.pk
Mehtab Ali	Equity Sales (Multan)	Tel: (+92-61) 4512003	mahtab.ali@igi.com.pk

Research Team

Saad Khan	Head of Research	Tel: (+92-21) 111-234-234 Ext: 810	saad.khan@igi.com.pk
Abdullah Farhan	Senior Analyst	Tel: (+92-21) 111-234-234 Ext: 912	abdullah.farhan@igi.com.pk
Aariz Raza	Analyst	Tel: (+92-21) 111-234-234 Ext: 810	Aariz.raza@igi.com.pk
Ajay Kumar	Analyst	Tel: (+92-21) 111-234-234 Ext: 912	ajay.kumar@igi.com.pk
Huzaifa Yaseen	Analyst	Tel: (+92-21) 111-234-234 Ext: 912	huzaifa.yaseen@igi.com.pk

IGI Finex Securities Limited
Trading Rights Entitlement Certificate (TREC) Holder of Pakistan Stock Exchange Limited |
Corporate member of Pakistan Mercantile Exchange Limited
Website: www.igisecurities.com.pk

Head Office

Suite No 701-713, 7th Floor, The Forum, G-20,

Khayaban-e-Jami Block-09, Clifton, Karachi-75600
UAN: (+92-21) 111-444-001 | (+92-21) 111-234-234
Fax: (+92-21) 35309169, 35301780

Stock Exchange Office

Room # 134, 3rd Floor, Stock Exchange Building,

Stock Exchange Road, Karachi.
Tel: (+92-21) 32429613-4, 32462651-2
Fax: (+92-21) 32429607

Lahore Office

Shop # G-009, Ground Floor,

Packages Mall
Tel: (+92-42) 38303560-69
Fax: (+92-42) 38303559

Islamabad Office
Mezzanine Floor, Office 5, 6 & 7, Kashmir Plaza,
Block- B, Jinnah Avenue, Blue Area
Tel: (+92-51) 2604861-2, 2604864, 2273439
Fax: (+92-51) 2273861

Faisalabad Office
Office No. 2, 5 & 8, Ground Floor, The Regency International 949, The Mall
Faisalabad
Tel: (+92-41) 2540843-45

Rahim Yar Khan Office

Plot # 12, Basement of Khalid Market,

Model Town, Town Hall Road
Tel: (+92-68) 5871652-3
Fax: (+92-68) 5871651

Multan Office
Mezzanine Floor, Abdali Tower,
Abdali Road
Tel: (92-61) 4512003, 4571183

IGI Finex Securities Limited
Research Analyst(s)
Research Identity Number: BRP009