Economy

Monetary Policy Statement

Status quo expected; Status quo Delivered

- The State Bank of Pakistan (SBP) in its latest Monetary Policy Statement (MPS) announcement on Monday January 24th, 2021 kept policy rate 'Unchanged' at 9.75% in-line with ours and market consensus.
- As per monetary policy statement, several price indicators have started to show moderate improvement. In addition to moderating inflation outlook, the decision to keep rate unchanged also includes sustaining the current economic recovery.
- Given the latest monetary policy statement wordings we sense some softening in overall stance of SBP, compared to early fear of aggressive hikes.

SBP kept policy rate 'Unchanged' at 9.75% amid …
The State Bank of Pakistan (SBP) in its latest Monetary Policy Statement (MPS) announcement on Monday January 24th, 2021 kept policy rate 'Unchanged' at 9.75% in-line with ours and market consensus.

The decision (link) to keep the rate unchanged is in line with the forward guidance provided in the last monetary policy statement issued Dec-21 and consideration includes Improving inflationary outlook and to sustain current economic recovery.

… Improving inflation outlook
As per monetary policy statement, several price indicators have started to show moderate improvement. Although current inflation remains in double digit and will likely remain so, given high base effect and energy prices, but recent Dec-21 (down by 0.02%m) and going forward price trend suggest some moderation in price trend. However, these trends are yet to reflect consumer expectations.

Moreover admittedly, during the first half of fiscal year (1HFy22), the current account deficit has reached US$ 9.1 bn (US$ 1.2bn surplus last year same period), but ex-oil payments current account balance is expected to show minor surpluses in coming months (2HFY22 C/a Deficit ex-oil stands at US$ 521mn).

In addition to this, global monetary authorities have started to take tightening actions, international commodities are expected to stabilize to decline in the short to medium run, thus having minimal costly impact on import side in the second half of the fiscal year (2HFY2022); this also means that pressure on exchange rates will subside eventually.

Similarly, SBP highlighted that the sentiment after the cumulative 275bps policy rate increase last year, has started to show effects on subsiding

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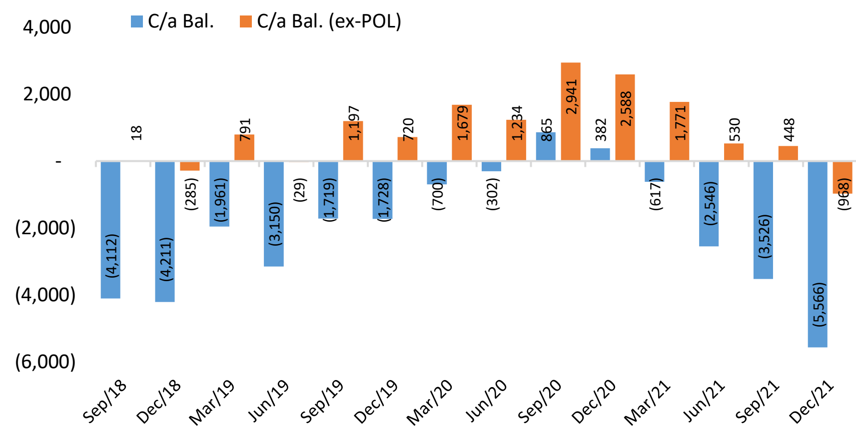
inflationary outlook. For FY22, SBP expects inflation to average 9-11%, thereon 5-7% in FY23.

Exhibit: C/a balance with and without POL Imports

During the 1HFY22, C/a balance excluding POL imports comes at a deficit of US$ 521mn or 0.3% of the GDP.



Source: SBP, IGI Research

…and to sustain current economic recovery

In addition to moderating inflation outlook, the decision to keep rate unchanged also includes sustaining the current economic recovery. Key leading data including cement dispatches, sales of petroleum products, electricity generation, tractors, commercial vehicles, etc. have either stabilized or slowed down lately. Resultantly, impacting Large-Scale Manufacturing production, whereby growth decelerated to 3.3% from 5MFY22. This moderating growth

This slowdown in LSM production along with easing of imports and tax revenue is suggestive of moderating growth outlook. SBP has lowered down its GDP forecast to 4-5% owing to reduced demand and high base (FY21 GDP growth has been rebased; 5.6%)

Outlook: Rising inflation will keep rate on the higher side, but not so aggressively

Given the latest monetary policy statement wordings we sense some softening in overall stance of SBP, compared to early fear of aggressive hikes. In fact e to believe that rates have a more tendency to go down once inflation fears starts to fade. Having said that, we could be completely wrong. A key risk on our outlook is that inflation fails to moderate as expected, forcing SBP to tighten policy more aggressively subsequently hampering demand.

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