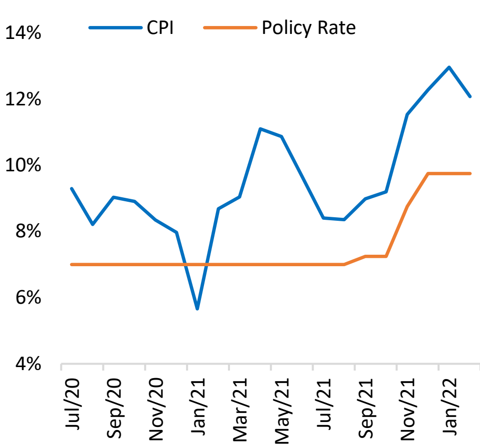
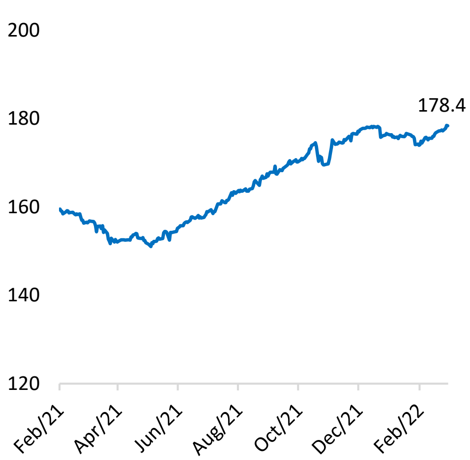
Economy

CPI and Policy rate



Exchange rate close to all-time high



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Monetary Policy Statement

Status quo maintained; ready to intervene if necessitated

- The State Bank of Pakistan (SBP) in its latest Monetary Policy Statement (MPS) announcement on Tuesday March 8th, 2022 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 guidance, SBP is ready to intervene if any threat rises from external front.

SBP kept policy rate 'Unchanged' at 9.75% amid …
The State Bank of Pakistan (SBP) in its latest Monetary Policy Statement (MPS) announcement on Tuesday March 8th, 2022 kept policy rate 'Unchanged' at 9.75% in-line with ours and market consensus.

Since the fiscal support comes into play to curb spikes in imported inflation in the form of reduction in fuel and power prices, SBP decided (link) to keep rates unchanged and continue supporting economy going forward. The decision to keep the rate unchanged is in line with majority of market consensus and consideration includes improving inflationary outlook, improved debt-to-GDP ratio since pandemic, and to sustain current economic recovery as demand moderates.

… Improving inflation outlook since December
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 price trend from Dec-21 (m/m basis) onward have averaged 0.51% during Dec to Feb-22 compared to first 5MFY22 averaging 1.8%, showing signs of declining trend since peak in Nov-22.

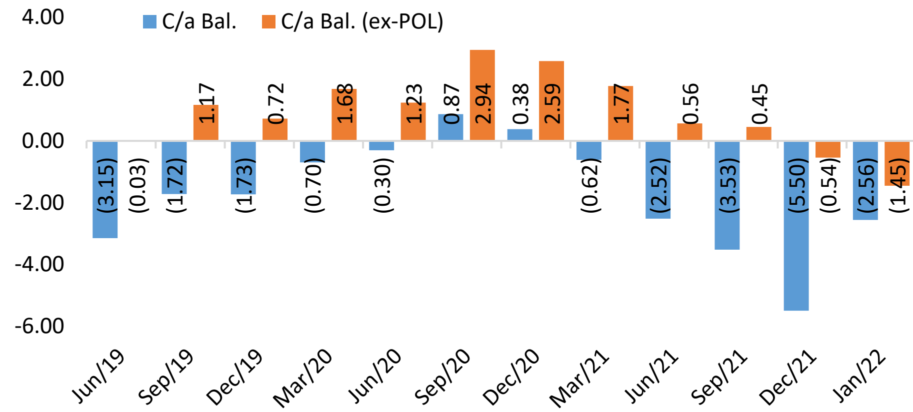
Moreover, there is a growing disturbance in the external account, but this may not be long lived. Recent uncertainty in geo-political situation, specifically Russia-Ukraine conflict, has created further surge in prices of commodities, especially oil prices, and if they sustain for a longer period, MPC is prepared to meet earlier than upcoming meeting (scheduled to take place by mid of next month), and if necessary, take timely and calibrated action to safeguard external and price stability.

In addition to this, global monetary authorities have started to take tightening actions, especially FED already hinted to aggressively tackle rising trend of commodities prices in their upcoming meeting by start of third week this month. International commodities are expected to stabilize and decline in the medium run, thus having minimal cost impact on import side in the later second half of the fiscal year (2HFY22); 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 inflationary outlook since peak in November. 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 7MFY22, C/a balance excluding POL imports comes at a deficit of US$ -1.54bn.



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.

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

Outlook: Real rates on a forward-looking basis are appropriate to guide inflation for now; prepared to intervene earlier if necessary

Given the latest monetary policy statement guidance, SBP is ready to intervene if any threat rises from external front, however, for now real rates are justified to support the ongoing economic recovery process. The MPC continues to expect inflation to moderate between 9-11% by fiscal year end and thereon decline towards the medium-term target range of 5-7% later in FY23 after global commodity prices begin to normalize after the geo-political tensions ease and aggressive monetary stance by global economies.

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