Day Break

Monday, January 23, 2023

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Economy

SBP Increased Policy Rates by 100bps To 17%

- The Monetary Policy Committee (MPC) decided to increase the policy rate by 100 basis points to 17%.

The Monetary Policy Committee (MPC) decided to increase the policy rate by 100 basis points to 17%. (Link). This is in line with our expectation (Link) and market consensus.

Key Highlights

- The MPC noted that inflationary pressures are persisting and broad-based, which could feed into higher inflation expectations over a longer period.
- The MPC emphasized the importance of anchoring inflation expectations and achieving price stability to support sustainable growth.
- The MPC highlighted three key economic developments: continuing elevated inflation, increased challenges for the external sector, and uncertain global economic and financial conditions.
- The MPC reiterated that the short-term costs of bringing down inflation are lower than the long-term costs of allowing it to become entrenched.
- The MPC emphasized the need for engagements with multilateral and bilateral partners to address domestic uncertainty and near-term external sector challenges.

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Exhibit: Market Survey of Monetary Policy decision

~90% of the participants' surveyed, CFA Society of Pakistan expect rate to increase (Source: CFA Society Pakistan)

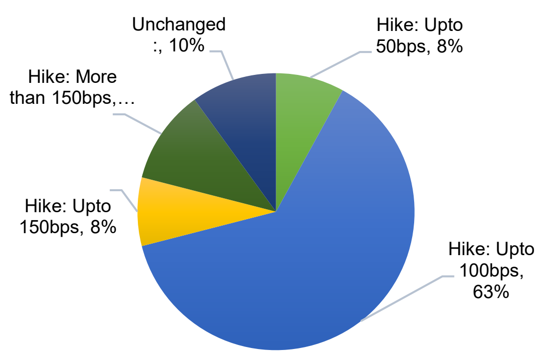
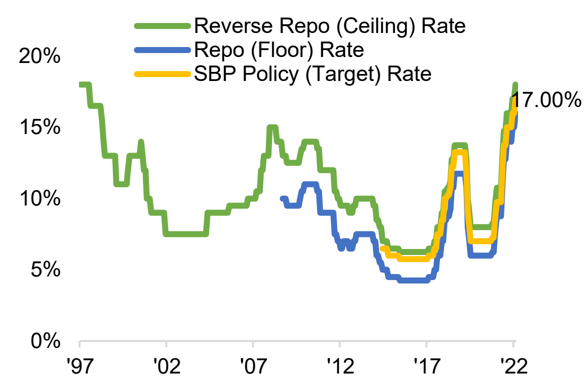


Exhibit: Pakistan Policy Rate (historical)

Last time Pakistan had 18% of Discount rate was back in Jun-98.



Real sector: Downside risks to SBP growth projections remain plenty

- Broad-based and sustained moderation in economic activity due to policy tightening and exogenous shocks like floods.
- Production cuts and supply constraints could pull LSM growth further down.
- Latest data on cotton arrivals point to lower crop production than anticipated earlier, which could potentially weaken the agriculture sector outlook.
- MPC views that downside risks to the SBP's baseline growth (SBP growth projections 2-3% in FY23) outlook for this year have increased.

Exhibit: Large Scale Manufacturing Industries (LSMI)

Index	Weight	Nov-22	Oct-22	m/m	y/y	5MFY23	y/y
LSMI Index	**100%**	**112**	**108**	**3.6%**	**-5.4%**	**112**	**-4.1%**
Textile	18%	83	84.36	-1%	-22%	95	-12%
Food	11%	118	103.04	15%	-13%	103	-9%
Petroleum	7%	99	97.7	1%	5%	88	-14%
Chemicals	6%	105	107.69	-3%	-7%	110	-1%
Wearing Apparel	6%	210	173.91	21%	50%	196	52%
Pharmaceuticals	5%	83	80.98	2%	-8%	78	-22%
Non-Metallic	5%	131	138.65	-5%	-13%	122	-15%
Beverages	4%	87	102.77	-15%	8%	108	1%
Iron & Steel	3%	128	127.66	0%	-9%	130	-3%
Automobiles	3%	108	85.06	27%	-19%	92	-30%
Tobacco	2%	97	104.14	-7%	-20%	87	-25%
Electrical Equipment's	2%	147	154.99	-5%	-3%	165	6%
Paper & Board	2%	139	129.48	7%	4%	134	-1%

Source: PBS, IGI Research

External Sector: Resumption of 9th IMF review critical for stabilizing external accounts

- Current account deficit narrowed due to sharp contraction in imports reflecting the impact of policy tightening and administrative measures.
- MPC noted that effective implementation of energy conservation measures and appropriate pricing of petroleum products is critical for reducing energy imports.
- External sector remains under stress due to delay in realization of official financial inflows, debt repayments, and ongoing political uncertainty.
- MPC views that completion of the pending 9th review under the IMF's EFF is critical for reducing uncertainty and unlocking multilateral and bilateral inflows.

Exhibit: Monthly Current Account Balance								
US$ mn	Dec-22	Nov-22	m/m	Dec-21	y/y	6MFY23	6MFY22	y/y
Exports (G)	2,295	2,241	2%	2,929	-22%	14,211	15,242	-7%
Imports (G)	4,218	4,333	-3%	6,431	-34%	29,510	36,095	-18%
Trade Bal.	(1,923)	(2,092)	-8%	(3,502)	-45%	(15,299)	(20,853)	-27%
Services Bal.	48	35	37%	(426)	-111%	(357)	(2,139)	-83%
Remittances	2,041	2,108	-3%	2,520	-19%	14,051	15,808	-11%
Income Bal.	1,475	1,805	-18%	2,071	-29%	11,989	13,901	-14%
C/a Bal.	**(400)**	**(252)**	**59%**	**(1,857)**	**-78%**	**(3,667)**	**(9,091)**	**-60%**
C/a Bal. (x-oil)	**865**	**1,002**	**-14%**	**(380)**	**n.m.**	**6,438**	**(520)**	**n.m.**

Source: SBP, IGI Research

Fiscal Sector: Fiscal stance inconsistent with monetary tightening

- FBR taxes grew by 17.0% in 1HFY23, slower than the growth envisaged in the budget.
- Expectation of further slowdown in economic activity and reduction in imports poses downside risks to maintaining growth momentum in tax collection.
- MPC noted that the current fiscal stance is inconsistent with monetary tightening, thus it is important for fiscal policy to achieve planned consolidation to help contain inflation and pave the way for sustainable growth.

On Inflation: Near-term adjustments and fuel prices remain a key risk

- Uncertainty on the future path of fuel prices and expected near-term adjustments remain major upside risks to the inflation outlook.
- Consumer and business inflation expectations have drifted upwards over the short and medium term in latest pulse surveys.
- MPC views that anchoring of inflation expectations is important to achieve the medium term inflation target of 5-7% by Dec-2024 and requires coordinated monetary and fiscal policy efforts.

Exhibit: National Core-inflation measures													
	Dec-22	Nov-22	Oct-22	Sep-22	Aug-22	Jul-22	Jun-22	May-22	Apr-22	Mar-22	Feb-22	Jan-22	Dec-21
CPI	**24.5**	**23.8**	**26.6**	**23.2**	**27.3**	**24.9**	**21.3**	**13.8**	**13.4**	**12.7**	**12.2**	**13.0**	**12.3**
SPI	29.7	29.7	28.6	35.9	40.6	34.3	26.5	16.1	16.5	15.8	18.1	19.5	19.3
WPI	27.1	27.7	32.6	38.9	41.2	38.5	38.9	29.6	28.1	23.8	23.6	24.0	26.2
NFNE	16.4	16.2	16.2	15.7	14.9	13.0	12.3	10.4	9.8	9.5	8.4	8.5	8.5
Trimmed	22.2	22.0	23.9	21.5	22.4	20.1	17.7	12.1	11.4	11.0	10.4	10.7	10.6

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