



STATE BANK OF PAKISTAN

Monetary Policy Statement

March 21, 2015

Increasing number of economic indicators in the current fiscal year have moved in a favorable direction. Headline CPI inflation continues to follow a downward trajectory and is expected to be well below the annual target of 8.0 percent; latest SBP projection range is 4-5 percent for average CPI inflation in FY15. At the same time, GDP growth is on course to surpass the FY14 outcome. Owing to recent foreign exchange inflows and lower oil price, external sector outlook continues to improve. Government's efforts to contain the fiscal deficit have been on track in the first half of FY15, despite slightly slower growth in revenue collection. IBA-SBP survey-based indices of March 2015 report increase in consumer confidence and in current economic conditions. The current macroeconomic stabilization has thus opened a window of opportunity to gear up reforms to ensure improvements in the economy are sustainable.

As per the recent trend, moderation in inflation is broad-based with food and non-food inflations receding, both the measures of core inflation, Non-Food Non-Energy and Trim-Mean, are also recording decline. However, due to current decline in inflation in general and commodity prices in particular, there could be an increase in aggregate demand which may have inflationary repercussions beyond FY15.

After growing by 2.2 percent in Jul-Jan FY15, Large-scale Manufacturing is likely to gain traction due to recent cut in policy rate and low prices of raw materials that could boost the manufacturing sector. In the agriculture sector, improved outcomes in major *kharif* crops (cotton and rice, in particular) and incentives in place along with favorable weather conditions for *rabi* season wheat crop, GDP growth is expected to be higher than that of FY14.

With strong workers' remittances and declining import growth, current account deficit has shrunk in Jul-Feb period of FY15 as compared to same period last year. The improvement is in spite of subdued exports performance. Nonetheless, with lower price impact in imports and multilateral inflows on track, the external sector outlook remains stable. This is most visible in the stability in foreign exchange market and in an upward trajectory in foreign exchange reserves.

During Jul-Feb FY15 period, Net Domestic Assets decreased and Net Foreign Assets increased, which is a welcome development in contrast to the trends in the same period last year. The Year-on-Year growth in broad money (M2) by February 27, 2015 was 11.5 percent; lower than the average growth of 13.6 percent in the past five years. This deceleration is largely due to contraction in Net Domestic Assets of the banking system. Growth in credit to private sector during Jul-Feb FY15 has also remained subdued at Rs 158.9 billion compared to Rs 298.3 billion



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in the same period of FY14. Thus, these monetary indicators have largely reflected the underlying trends in falling inflation.

The Central Board of Directors has decided to reduce the SBP policy rate by 50 basis points from 8.5 percent to 8.0 percent effective from 24th March 2015.