Monetary Policy Statement

October 26, 2026

1. The Monetary Policy Committee (MPC) decided to increase the policy rate by 50 bps to 12 percent in its meeting today, with the majority decision of nine out of ten members, with effect from October 27, 2026. The Committee noted that the intensification in the Middle East conflict, and low prospects of its near-term resolution, are keeping global energy prices at persistently elevated levels. While the impact of this global shock on the domestic economy has remained contained so far amidst proactive monetary policy adjustment and continued fiscal discipline, geopolitical developments have worsened the inflation outlook as compared to the earlier assessment. Although the external account and growth outlook remained broadly unchanged, risks have also increased. Considering these developments and the evolving risks, the MPC deemed today's decision as necessary to keep inflation expectations anchored, contain second-round effects of the ongoing supply shock, and bring inflation within the target range of 5 – 7 percent. This will help preserve macroeconomic stability, which is necessary for sustainable economic growth.

2. The Committee noted the following key developments since its last meeting. First, supported by continued FX purchases, SBP's reserves remained stable at around US$21.5 billion – reaching the level of 3 months of import cover. Second, a staff-level agreement was reached with the IMF. Third, in the latest sentiment surveys, inflation expectations of consumers increased, whereas those of businesses declined; meanwhile, confidence indicators for both weakened. Fourth, PBS reported revised real GDP growth for FY26 at 3.7 percent, almost unchanged from the initial estimate. Fifth, FBR exceeded its revenue collection target during Q1-FY27. Lastly, major central banks have increased interest rates in the wake of rising inflationary pressures, whereas the IMF has also revised its global inflation projections upward.

3. While noting these developments and the increasing frequency of global supply shocks, the MPC emphasized the importance of increasing external and fiscal buffers to further strengthen the economy's resilience. The Committee also reiterated that continuing the prudent monetary and fiscal policy mix, alongside timely implementation of structural reforms, is essential for achieving higher and sustainable economic growth.

Real Sector

4. In line with expectations, economic activity has started to recover gradually as compared to Q4-FY26. LSM output grew by 1.9 percent y/y during July-August FY27 against a marginal growth of 0.4 percent during Q4-FY26. Similarly, other high frequency indicators – such as cement and POL sales, private sector credit and Purchasing Managers Index – also point to recovery in economic activity. Moreover, satellite imagery of nighttime lights and NO2 emissions also support this assessment. Meanwhile, first official estimates of Kharif crops turned out better than anticipated, improving the agriculture sector outlook. Available information on high frequency indicators for services sector – such as ICT exports, import volumes, and business confidence of services firms – also indicate gradually improving prospects, supported by positive developments in the commodity-producing sector. Overall, the MPC expects real GDP growth to remain within the earlier projected range of 3.5 to 4.5 percent during FY27. This outlook is susceptible to heightened risks stemming mainly from further intensification in the Middle East conflict, as well as from adverse climate events amidst worsening El Niño conditions.

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External Sector

5. The current account balance recorded a deficit of US$874 million in Q1-FY27. Exports are recovering, led by rice, HVA textiles and services exports, whereas workers' remittances have remained resilient and are projected to turn out higher than the earlier assessment. At the same time, imports are also rising sharply, led by non-energy imports, in line with the recovery in economic activity and higher prices. Based on these developments, the current account deficit in FY27 is assessed to remain within the earlier projected range of 0 – 1 percent of GDP. This, along with higher financial inflows, is expected to increase SBP's FX reserves beyond the current level. This outlook, however, remains susceptible to multiple risks, including elevated global commodity prices, tightening international financial conditions, and supply constraints.

Fiscal Sector

6. During Q1-FY27, FBR tax collection grew 7.0 percent y/y, exceeding the target by Rs33 billion. With the transfer of substantial SBP profit and contained expenditures, the overall fiscal and primary balances are assessed to remain in surplus during Q1-FY27. However, the intensification in the Middle East conflict has made fiscal management more challenging. In this context, the MPC emphasized that sustained and concerted efforts will be required to further strengthen fiscal discipline, enhance revenue mobilization through broadening of tax base, and accelerate the implementation of structural reforms. The Committee reiterated that prudent fiscal management remains imperative to sustain macroeconomic stability.

Money and Credit

7. Broad money (M2) growth increased to 12.7 percent y/y as of October 9 from 11.4 percent on August 28. This was due to an increase in SBP's FX reserves, which accelerated NFA growth during this period. Meanwhile, growth in NDA decelerated amidst continued fiscal consolidation and higher external financing, which led to a decline in net budgetary borrowing from the banking system. This created a space for banks to extend credit to the private sector (PSC), which grew by 14.1 percent y/y. Moreover, PSC growth remained broad-based across working capital, fixed investment and consumer finance. Key borrowing sectors included textiles, wholesale and retail trade, and agriculture. Going forward, PSC is likely to continue its momentum, alongside the projected pickup in economic activity.

Inflation

8. The Committee noted that the re-escalation in the Middle East conflict and domestic wheat supply frictions are two major factors keeping inflation at elevated levels, and their expected continuation over the next few months have worsened the inflation outlook. Elevated prices of energy and wheat and its allied products contributed significantly to the headline inflation of 10.3 percent y/y in September, which turned out higher than the MPC's expectation. Meanwhile, core inflation has steadied at an elevated level of around 8.4 percent. However, there is a risk that elevated food and energy inflation may further increase inflation expectations, which may seep into core inflation going forward. In view of these developments and increasing risks to the inflation outlook, the Committee assessed today's decision as important to keep the real policy rate adequately positive on forward-looking basis. This is necessary to bring inflation within the target range over the medium term. The inflation outlook is subject to multiple risks, including geopolitical tensions, global commodity price volatility, unanticipated adjustments in energy tariffs, further uptick in wheat and allied product prices, and adverse weather conditions.

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