MINUTES OF THE MEETING OF THE MONETARY POLICY COMMITTEE (MPC)
<u>HELD ON THURSDAY, SEPTEMBER 12, 2024 AT 10:00 AM</u>

<u>P R E S E N T</u>

Mr. Jameel Ahmad	Chairperson & Governor SBP
Dr. Inayat Hussain	Deputy Governor
Mr. Saleem Ullah	Deputy Governor
Mr. Muhammad Ali Malik	Executive Director
Mr. Fawad Anwar	Director SBP Board
Mr. Najaf Yawar Khan	Director SBP Board
Mr. Muhammad Ali Latif	Director SBP Board
Dr. Naved Hamid	External Member
Dr. Hanid Mukhtar	External Member
Dr. S. M. Turab Hussain	External Member
Mr. Fayyaz ur Rehman	Corporate Secretary

Review of Current Economic Conditions and Outlook for FY25

1. The staff apprised the Committee of recent developments in the key macroeconomic indicators since the last MPC meeting held on July 29, 2024. The assessments and analysis of evolving trends were also shared with the Committee, including key assumptions used in the baseline projections.

2. High-frequency economic activity indicators showed improvement. POL sales (excluding furnace oil) increased by 6.8 percent on month-on-month basis (m/m) in August 2024 against a decline of 16.0 percent in July 2024. Furthermore, domestic cement sales increased by 8.5 percent on m/m basis in August 2024 after posting a m/m decline of 20.2 percent in July 2024. The staff apprised the Committee that Large-Scale Manufacturing (LSM) grew by 0.9 percent on year-on-year basis (y/y) in FY24 primarily supported by High-Value Added (HVA) textiles and intermediate goods, compared to a contraction of 10.3 percent during FY23.

3. On the outlook for FY25, the staff apprised that agriculture sector output is now projected to moderate further, primarily due to downward revision in cotton output estimates. Decline in area under cultivation and significant drop in cotton arrivals by end August 2024 explained this revision. Industrial growth is expected to improve compared to FY24, as indicated by underlying improvements in average capacity utilization. Discussing the services sector, it was apprised that the positive impact emanating from ease in inflation is expected to more than offset the negative knock-on effects of muted activity in the agriculture-related sectors. Consequently, forecast of real GDP growth for FY25 remained unchanged and is projected to remain in the range of 2.5 to 3.5 percent.

4. Discussing the global developments and trends since the last MPC meeting, it was apprised that the international prices for various commodities have eased. The staff also briefed on the recent trends in the global trade. It was apprised that global manufacturing activity experienced contraction in July 2024 as evidenced by a decline in global Purchasing Managers' Index (PMI) for manufacturing. However, global PMI for services-related sectors remained positive. Moreover, it was noted that inflationary pressures are easing in both Emerging Market Economies (EMEs) and Advanced Economies (AEs). Accordingly, AEs' central banks have also started to cut rates, while EMEs have continued their monetary easing since the last MPC meeting.

5. Discussing the latest developments related to Balance of Payments (BoP), it was apprised that the Current Account Deficit (CAD) remained contained in July 2024 at USD 162 million due to low trade deficit. It was stated that the increase in imports, in line with increasing economic

activity, and dividend/profit repatriations was offset by robust workers' remittances and substantial increase in exports. During Jul-Aug FY25, the export of goods grew by 14 percent (y/y), driven primarily by rice and HVA textile volumes. At the same time, the import of goods in Jul-Aug FY25, increased by 5.7 percent due to increase in volumes of non-oil imports on account of increased domestic economic activity. In addition, the services balance has improved due to information and communication technology exports. Regarding workers' remittances, it was apprised that average monthly inflows of approximately USD 3 billion were recorded during the first two months of the ongoing fiscal year in line with the trend observed for remittances in recent quarters. However, net financial inflows remained low during July 2024.

6. Discussing the external sector outlook, it was apprised that export projections have remained unchanged for FY25 as the impact of likely reduction in rice exports are offset by increase in volumes for textile and other manufactured exports. Further, imports are expected to increase slightly in FY25 in line with the increased domestic industrial activity. The outlook for workers' remittances for FY25 is also expected to remain promising, supported by better than expected inflows in the months of July and August, favourable policy measures and stable kerb premium. Considering these developments, the CAD as a percentage of GDP is expected to remain in the range of 0 to 1.0 percent of GDP for FY25.

7. Discussing fiscal developments, the staff informed the Committee about the latest fiscal operation numbers, and apprised that both fiscal and primary balances turned out better than earlier expectations for FY24. It was apprised that during Jul-Aug FY25, growth in FBR tax collection was lower at 20.5 percent as compared to 27.3 percent in the same period last year. The staff emphasized that in order to meet the revenue targets for the current fiscal year, the tax collection rate in the remaining months of FY25 needs to be significantly higher than revenue collection growth witnessed in recent months. The staff further elaborated that the government has set the primary surplus target of 2.0 percent of GDP for FY25.

8. Discussing developments in the monetary sector, it was apprised that Broad Money (M2) growth decelerated from 16.1 percent (y/y) as of June 30, 2024 to 14.6 percent as of August 30, 2024. The Committee was apprised that growth contribution of the Net Foreign Assets (NFA) in M2 remained positive. Additionally, the growth contribution of the Net Domestic Assets (NDA) in M2 decelerated due to a more than seasonal decline in Private Sector Credit (PSC) and Commodity Operations Financing (COF). After witnessing higher growth in June 2024, the PSC witnessed a higher than seasonal retirement in the month of July 2024. On the liability side, interest sensitive deposits continued to be the primary contributor to M2 growth despite showing signs of some moderation. On the other hand, the contribution of Currency in Circulation (CiC) picked up slightly after remaining subdued in the past few months. The Committee was apprised that growth in reserve money (RM) at 5.9 percent as of end-August has accelerated from 2.6 percent recorded as of end-June, yet remained lower than the historical average level. Regarding the outlook for monetary aggregates for FY25, the Committee was apprised that M2 growth is expected to remain in the range of 13-15 percent.

9. Discussing the inflation trends and developments, the staff apprised the Committee that headline inflation eased to 9.6 percent y/y in August 2024, down from 11.1 percent in July 2024. This decrease was primarily attributed to contained demand, noticeable decline in global oil and other commodity prices, delay in upward adjustment in administered energy prices and improved supply of key food items. Moreover, it was apprised that core inflation decelerated to 11.9 percent in August 2024, from 13.8 percent in July 2024, primarily due to ease in goods inflation.

10. However, recent surveys indicate that inflation expectations of consumers slightly worsened compared to the last survey iteration while the inflation expectations of businesses eased.

11. Discussing the inflation outlook, it was apprised that the inflation projections for FY25 are revised downward due to lower-than-expected inflation in the months of July and August 2024, delay in implementation of adjustments in administered energy prices, and favorable global

commodity prices and exchange rate. However, the Committee was informed that the near-term inflation outlook is subject to certain risks including uncertainty related to the timing and magnitude of adjustments in administered energy prices, volatility in the global commodity markets and any additional fiscal contingency measures. Taking into account these developments and risks, the average inflation for FY25 is expected to remain in the lower bound of the range of 11.5 to 13.5 percent.

Financial Market and Reserve Management

12. Apprising the Committee on monetary policy implementation, the staff stated that the overnight repo rate averaged 19.32 percent during the review period, compared to the target of 19.5 percent. The SBP's liquidity support was approximately PKR 11.79 trillion in the current review period (since the last MPC meeting), compared to PKR 11.76 trillion in the previous review period.

13. It was apprised that a downward shift in the yield curve was observed across all tenors of government securities reflecting the impact of expected decline in the policy rate. Shorter-term secondary market yields have recorded a somewhat more pronounced decline as compared to longer-term secondary market yields during the review period. In primary auctions of Market Treasury Bills (MTB), market participation has shifted towards 6 and 12 month tenors, reflecting expectations of declining interest rates.

14. In the recent fixed-rate Pakistan Investment Bond (PIB) primary auction, yields of both medium-term (3 and 5 years) and long-term (10 years) tenors showed a small decline, as market participants had already factored in a decline in interest rates. However, the primary focus of the government remained on floating-rate PIBs, as acceptance of bids was higher for floating-rate PIBs compared to fixed-rate PIBs to lengthen their maturity profile.

15. The staff informed the Committee that Pakistan Eurobond yields and Credit Default Swap (CDS) spreads have remained almost unchanged since the last MPC meeting. Since January 2024, both CDS spreads and Eurobond yields have significantly improved, although they remain elevated.

16. In the FX market, the PKR has remained broadly stable against the USD since the last MPC meeting. However, the USD Index has weakened by 2.7 percent against other major currencies during the review period.

Model-Based Assessment

17. The staff apprised the Committee about the medium-term inflation projections conditional on the policy rate path in a general equilibrium framework. The model took into account the impact of recent developments including lower than anticipated inflation outcome for August 2024, expected adjustments in administered energy prices in the second quarter of FY25 and the recent stability in exchange rate.

18. Keeping in view the above development, the MPC discussed the monetary policy stance to bring the inflation down within the target range under various scenarios.

Result of SBP Surveys for Monetary Policy

19. The staff apprised the Committee that in August 2024, both the Consumer Confidence Index and the Consumer Inflation Expectations Index deteriorated marginally. On the other hand, the Business Confidence Index and Business Inflation Expectations Index improved. Moreover, moderate improvements were recorded in business sentiments and capacity utilization by firms.

20. The staff apprised about the results of the survey of professional forecasters. It was noted that forecasters expect a gradual uptick in GDP growth going forward into FY25 and beyond. They

also see inflation moderating in FY25 despite the expected impact of delayed adjustment in energy prices.

Monetary Policy Deliberations and Decision Vote

21. The MPC decided to decrease the policy rate by 200 bps with a majority of seven votes out of ten, while two Members voted to decrease the policy rate by 100 bps and one member voted to decrease the policy rate by 150 bps.

DECISIONS:

- *The policy rate is reduced by 200 bps to 17.5 percent.*
- *The Monetary Policy Statement – September 2024 is approved.*