MINUTES OF THE MEETING OF THE MONETARY POLICY COMMITTEE (MPC)
HELD ON MONDAY, JULY 29, 2024 AT 10:00 AM

P R E S E N T

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. Muhammad Ali Latif	Director SBP Board
Dr. Naved Hamid	External Member
Dr. Hanid Mukhtar	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 June 10, 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 continued to reflect moderate economic activity. Auto, Petroleum, Oil, and Lubricants (POL) sales (excluding furnace oil), and fertilizer offtake increased on month-on-month (m/m) basis in June 2024. However, domestic cement sales declined by 8.3 percent m/m in June 2024, following a seasonal uptick in May 2024. Discussing developments in the real sector, the staff apprised the Committee that Large-Scale Manufacturing (LSM) grew by 1 percent in Jul-May FY24, compared to a contraction of 9.6 percent during the same period last year. This increase was primarily driven by growth in High Value Added (HVA) textiles and intermediate goods.

3. On the outlook for FY25, the staff apprised that agriculture sector output is anticipated to moderate due to the high base effect and relatively less favourable input conditions. Furthermore, the latest satellite images also support this assessment. Industrial growth is expected to improve compared to FY24, driven by underlying improvements in capacity utilization, relatively lower interest rates, and increased budgeted development spending. Additionally, knock-on effects of commodity producing sectors and easing of inflationary pressures would improve growth in the services sector. Consequently, real GDP growth for FY25 is projected to remain in the range of 2.5 to 3.5 percent, compared to 2.4 percent recorded last year.

4. Discussing the global developments and trends since the last MPC meeting, it was apprised that the international oil prices have been volatile. However, metals' prices in the international market have declined, primarily due to lower demand from China. The international prices of agricultural commodities have decreased, mainly driven by reductions in rice and wheat prices. Moreover, the staff informed that the IMF has slightly revised its global GDP projection for 2025 upwards in its July 2024 World Economic Outlook, compared to its earlier projection. The staff apprised the Committee of the significant increase in global shipping costs due to the Middle East crises. Additionally, it was noted that inflationary pressures are easing in general, both in Emerging Market Economies (EMEs) and Advanced Economies (AEs). Accordingly, more central banks in AEs and EMEs have started to ease their policy rates since the last MPC meeting.

5. Discussing the latest developments related to Balance of Payments (BoP), it was apprised that after three consecutive surplus months, the current account recorded a deficit in May and June 2024. These deficits were primarily due to higher dividend/ profit repatriations, interest payments, as well as a seasonal increase in imports. Cumulatively, the Current Account Deficit (CAD)

narrowed by 79 percent to USD 0.7 billion during FY24, compared to USD 3.3 billion in FY23. This improvement was largely supported by a better trade balance and increased workers' remittances inflows. During FY24, the export of goods grew by 10.7 percent year-on-year (y/y), driven primarily by rice and High Value Added (HVA) textile volumes. Conversely, the import of goods contracted by 0.7 percent due to improved domestic crop output, subdued demand from the industry and lower global commodity prices. Regarding workers' remittances, it was apprised that remittances increased to USD 30.3 billion in FY24 from USD 27.3 billion in FY23. This growth is attributed to an enabling policy environment, increase in average emigrants compared to previous years, and improving real wages in major host countries. Moreover, during FY24, net financial inflows were approximately USD 4.7 billion, compared to net outflows of around USD 0.5 billion during FY23.

6. Discussing the external sector outlook, it was apprised that export projections have been revised slightly upward for FY25 owing to improvements in the global GDP and trade outlook. Further, imports are expected to increase slightly in FY25 in line with the improved domestic growth outlook. The outlook for workers' remittances for FY25 is also expected to remain promising, supported by favourable policy measures and a sustained number of workers going abroad. 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 government's revised estimates for FY24. The primary balance turned into a surplus of 0.4 percent of GDP, compared to a deficit of 1 percent of GDP in FY23; and the overall deficit declined to 7.4 percent of GDP in FY24 from 7.8 percent in FY23. The staff explained that the improvement in fiscal accounts was mainly driven by an increase in non-tax revenues and a reduction in non-interest expenditures. The staff also informed the Committee that the government has set the primary surplus target of 2.0 percent of GDP for FY25. The staff emphasized the importance of achieving the envisaged fiscal consolidation to support overall macroeconomic stability.

8. Discussing developments in the monetary sector, it was apprised that Broad Money (M2) increased by 16.0 percent as of June 30, 2024 (y/y) from 14.2 percent as of June 30, 2023. The Committee was apprised that growth contribution of the Net Foreign Assets (NFA) in M2 remained positive throughout FY24, in contrast to negative growth contribution in the last two fiscal years, owing to multilateral/bilateral FX inflows. Additionally, the growth contribution of the Net Domestic Assets (NDA) in M2 decelerated significantly despite higher net budgetary borrowing (entirely from commercial banks). Growth in Private Sector Credit (PSC) observed a seasonal uptick in June 2024; however, the overall growth in PSC for FY24 remained below the historical average levels. It was apprised that working capital loans to businesses increased in FY24 compared to FY23, while fixed investments remained subdued, primarily, owing to net retirements in SBP concessionary schemes. On the liability side of M2, growth in bank interest-sensitive deposits continued to be the primary contributor to M2 growth, while the contribution of Currency in Circulation (CiC) remained negligible, with CiC staying almost at the last year's level. The Committee was apprised that growth in reserve money decelerated sharply to 2.6 percent in FY24, down from 22.4 percent in FY23.

9. Regarding the outlook for monetary aggregates for FY25, the Committee was apprised that M2 growth is expected to be in the range of 13 to15 percent.

10. Discussing the inflation trends and developments, the staff apprised the Committee that headline inflation increased to 12.6 percent y/y in June 2024, up from 11.8 percent in May 2024. This rise was primarily attributed to Eid-related price increases and upward adjustments in administered electricity prices. Moreover, it was apprised that core inflation marginally eased to 14.1 percent in June 2024, down from 14.2 percent in May 2024. However, recent surveys indicate that inflation expectations of both consumers and businesses have edged up following the announcement of budgetary measures and the upward revision of administered energy prices.

11. Discussing the inflation outlook, the Committee was informed that the near-term inflation outlook remains favourable due to staggered electricity tariffs for the low-end consumers and the delayed impact of budgetary measures. The staff also highlighted potential risks to the inflation outlook, including adjustments in administered energy prices, rebound in wheat prices and fiscal contingency measures. Taking into account these developments and risks, the average inflation for FY25 is expected to remain in 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 20.16 percent during the review period, compared to the target of 20.5 percent, indicating improved short-term liquidity conditions.

13. The SBP's liquidity support was approximately PKR 11.7 trillion in the current review period (since the last MPC meeting), compared to PKR 11.0 trillion in the previous review period. Short-term secondary market yields (up to 12-month tenors) have recorded relative decline as compared to medium and long-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 recent fixed-rate Pakistan Investment Bonds (PIB) primary auctions, yields of both medium-term (3 and 5 years) and long-term (10 years) tenors showed minimal change, as market participants had already factored in a decline in interest rates. While participation in PIB auctions has picked up, the government acceptance of bids for fixed-rate PIBs was lower compared to floating-rate PIBs.

15. The staff informed the Committee that Pakistan Eurobond yields and Credit Default Swap (CDS) spreads have significantly improved in recent months, 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 1 percent against other major currencies during the review period.

Model-Based Assessment

17. The staff apprised the Committee about the medium-term inflation projections within a general equilibrium framework. This time, the model took into account the impact of two developments into the baseline: first, lower than anticipated inflation outcome for June 2024; and second, lower nowcast for July 2024 inflation owing to the staggered adjustment of electricity tariffs.

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

Result of SBP Surveys for Monetary Policy

19. The staff apprised the Committee that both the Consumer Confidence Index and the Business Confidence Index declined in July 2024, reflecting a deterioration in near-term sentiments after the release of the FY25 budget. While discussing inflation expectations, it was noted that both businesses and consumers expect inflation to rise in the near term.

20. The staff then apprised the results of the survey of professional forecasters. It was noted that forecasters expect relatively higher inflation and lower GDP growth one to two years ahead,

compared to the last survey iteration. They also anticipated higher likelihood of a rate cut in the current MPC meeting.

Monetary Policy Deliberations and Decision Vote

21. The MPC decided to decrease the policy rate by 100 bps with a majority of six votes out of eight, while two Members voted to decrease the policy rate by 50 bps.

DECISIONS:

- *The policy rate is reduced by 100 bps to 19.5 percent.*
- *The Monetary Policy Statement – July 2024 is approved.*