



# STATE BANK OF PAKISTAN

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## Monetary Policy Decision

November 21, 2015

The average Jul-Oct FY16 inflation at 1.7 percent is lower than the 7.1 percent average inflation in the corresponding period of last year. The decline is broad based as both food and non-food and core inflation measures came down in this period. Going forward, with subdued outlook of international oil price and other major commodity prices and in the absence of any shock to supplies of food items, even though the average inflation would remain below the FY16 annual target of 6 percent, the headline inflation is expected to reverse its declining momentum. Moreover, market surveys indicate a marginal increase in inflation expectations for the coming months.

Current account deficit, despite a year on year 10.6 percent contraction in exports, has narrowed down to USD532 million in Jul-Oct FY16 from USD1.9 billion in Jul-Oct FY15. The improvement largely owes to declining oil price – that has substantially reduced the oil import payments, healthy workers' remittances, and the realization of Coalition Support Fund. At the back of official disbursements and Eurobond inflows, surplus in capital and financial account has supported the overall balance of payments position thus ensuring an upward trajectory in foreign exchange reserves in Jul-Oct FY16. Going forward, continued flow of external resources would be required to maintain the stable balance of payments position. Furthermore, realization of investment inflows stemming from the China-Pakistan Economic Corridor would indeed strengthen the external sector outlook over the medium to long term.

Large-scale Manufacturing (LSM), mainly supported by food and beverages, automobiles, fertilizers, and cement production, increased to 3.9 percent in Jul-Sep 2015 compared to 2.6 percent in the same period of last year. Further boost to this growth is expected from expansion in cotton yarn manufacturing, strong construction activities as per planned development spending, increased automobile production encouraged by government schemes, and improving energy supply at the back of recent LNG imports.

Credit to private sector witnessed a nominal increase in July-October 2015; wherein fixed investments continued to expand for the fourth consecutive quarter – from Q2-FY15 to Q1-FY16. As a result of easy monetary policy, the weighted average lending rates on fresh and outstanding loans, at 7.8 percent and 9.2 percent in September 2015, are the lowest in 10 years. Thus, with current credit cycle now entering in uptake phase and with improving LSM growth, borrowing on account of both the working capital and fixed investment is likely to increase. This outlook would reflect in broad money (M2) growth going forward, which during July 01-November 06 2015 M2 has expanded by 0.2 percent against 0.7 percent during the same period last year. While the Net Domestic Assets declined by Rs78 billion, Net Foreign Assets contribution in M2 growth remained substantial as it increased by Rs106 billion.

In view of the foregoing, the Central Board of Directors of SBP has decided to keep the policy rate unchanged at 6.0 percent.