REN # REP - 004

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Economy: SBP slashes policy rate by 200bps to 13%

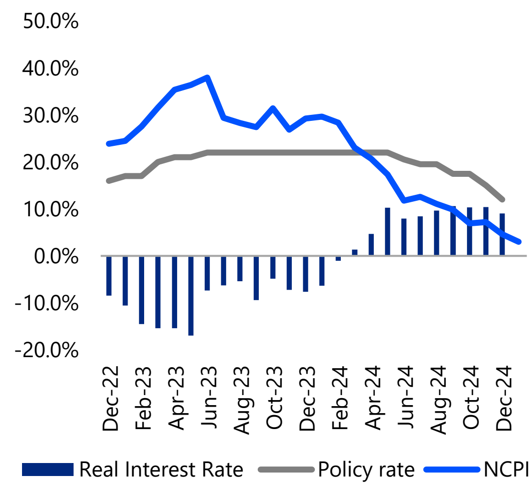
The State Bank of Pakistan (SBP) announced its monetary policy on 16th December (Monday), wherein the policy rate was cut by 200bps to 13.0%, bringing down the real interest rate to ~850bps. This latest move brings the cumulative rate cuts to 900bps since Jun-24.

Some key developments influencing the macroeconomic outlook include (i) the current account recording a surplus for the third consecutive month in October 2024 amidst weak financial inflows and substantial debt repayments, (ii) global commodity prices remaining favorable, with positive spillovers on domestic inflation and the import bill, (iii) credit to the private sector increasing, reflecting the efforts of banks in meeting the advances-to-deposit ratio (ADR), and (iv) widening of shortfall in tax revenues from the target.

Key Takeaways:

- Economic growth prospects have improved, driven by better-than-expected cotton arrivals, positive wheat sowing trends, and strengthening industrial activity. Key sectors like textiles, food, and automobiles show robust growth, supported by high-frequency indicators.
- Going forward, the Monetary Policy Committee expects the real GDP growth in FY25 of 2.5%-3.5% with major growth coming from industry and services sectors.
- The Committee noted that the real policy rate remains appropriately positive to stabilize inflation within the target range of 5%-7%.
- The Committee has revised its FY25 inflation forecast downward from the previous range of 11.5%-13.5%, though near-term risks remain due to potential food inflation, rising global commodity prices, and a revenue shortfall.
- For FY25, the total debt repayments are USD 26.1bn, including USD 22.1bn principal and USD 4bn interest. Of this amount, USD 10.4bn has been serviced, including a USD 5.4bn rollover and payment of USD 5bn. The remaining repayment for the fiscal year, excluding planned rollovers, stands at USD 5bn which will be made without pressure on reserves.
- SBP expects the reserves to exceed the level of USD 13bn by the end of Jun-25.
- The governor highlighted that the sharp decline in the policy rate, along with buybacks of securities and reduced external debt, is expected to lower interest expenses significantly.
- He anticipated that, despite revenue shortfalls, the fiscal balance would stay within the budgeted range. Interest expenses are projected to be below PKR 8.5tn, saving the government PKR 1.3tn, equivalent to 1% of GDP.
- Exports are projected to reach USD 33bn in FY25, while remittances are forecasted to climb to USD 33.5bn, driven by government incentives and easing global inflation.

Real Interest Rates over the Years (%)



Source: SBP, PBS, Akseer Research

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