SBP maintains status quo!

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State Bank of Pakistan (SBP), with the newly framed Independent Monetary Policy Committee (MPC) has announced its first Monetary Policy Statement (MPS) for the next two months. In line with our expectations, the MPC opted to maintain the policy rate at 6%. Additionally, the committee has signaled the declining trend of policy rate to bottom out as it highlighted the reversal in inflationary trend during the past 3 months. Furthermore, the MPS has stamped the improvement in the private sector credit off take and domestic demand driven by monetary easing and reduced energy demand/supply gap. However, the committee also focused on concerns that could dent the GDP growth which include production declines of Rice and Cotton, lower exports and the deceleration of deposits led by higher currency in circulation. Going forward, we expect the current cycle of monetary easing to bottom out and the policy rate to maintain status quo for the next 12 months. However, access liquidity in the banking sector may reduce the market yields of T-Bills and PIBs improving prospects of higher private sector credit off-take in the coming months, therefore we expect the banking sector earnings decline to stem, while sectors, in expansionary mode will continue to benefit which includes Cement, Power, Allied Products and Textiles.

Key Highlights of the Monetary Policy Statement:

- SBP has maintained a status quo of 6% with a ceiling of 6.5% and a floor of 4.5%.
- Average CPI inflation has declined to 2.1% during 1HFY16, meanwhile trend in year-on-year CPI inflation has reversed; it rose for third consecutive month to 3.2% in Dec 2015.
- SBP expects the average inflation to range in between 3 to 4% for FY16, based on the declining international commodity prices, easing supply side constraints and a moderate pickup in domestic demand.
- LSM grew by 4.4% during Jul-Nov FY16 as compared to 3.1% in the corresponding period last year, driven by monetary easing, slump in international commodity prices, improved electricity and gas supply, expansion of construction activities and improved demand for consumer durables.
- Lower production of Cotton and Rice, the two major crops, have dented the GDP growth. However improved yields from wheat crop is expected to offset it partially.
- External account is expected to improve further in the 2HFY16, driven by lower commodity prices, steady growth in workers' remittances and improvement in FDI's. Furthermore, the continuation of IMF Loan under EFF along with the CSF would improve the surplus of financial and capital accounts, which is expected to have positive impact on the foreign reserves.
- Fiscal deficit remained at 1.1% during the 1QFY16 compared to 1.2% in the corresponding period last year, led by higher tax revenues and curtailment of current expenditure. The Fiscal balance is expected to improve based on additional tax measures announced by the Govt. in Oct 2015 and targeted current spending.
- Credit to Private sector increased by PkR339.8bn during 1HFY16 as compared to PkR224.5bn in the same period last year, driven by monetary easing, better corporate sector financial condition, and improved business environment.

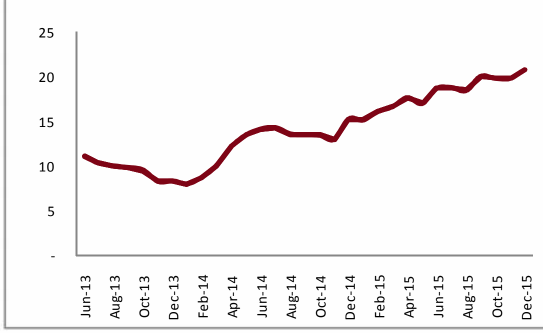
Impact on Equity and Money Market:

- Equity market welcomed the decision of the status quo in the first trading session after the MPS announcement, where the index opened on a positive note, the index at 11.09 am traded at 31,710 i.e. +411.40 points (+1.31%). Importantly, the money market, witnessed the panic in the initial trading hours, but it has also recovered and currently the securities are trading close to Friday's closing.

Outlook:

- We expect the current cycle of monetary easing may end here and the status quo to be maintained for the next 12 months. However, we expect a further decline in the market yields of T-bills and PIBs due to the surplus liquidity in the Banking sector, therefore, we expect the banking sector earnings decline to stem here, while sectors in expansionary mode will continue to benefit which includes Cement, Power, Allied Products and Textiles.

Fx Reserves (US$bn)



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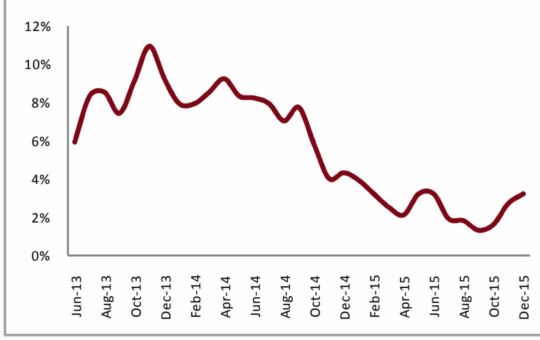
CPI



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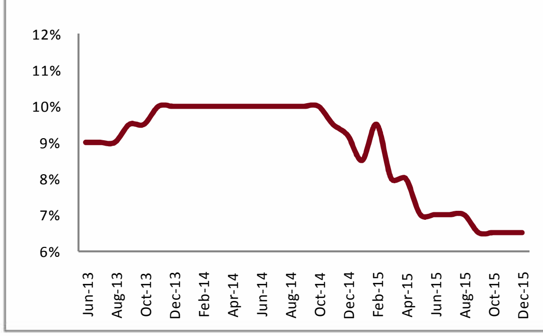
Discount Rates



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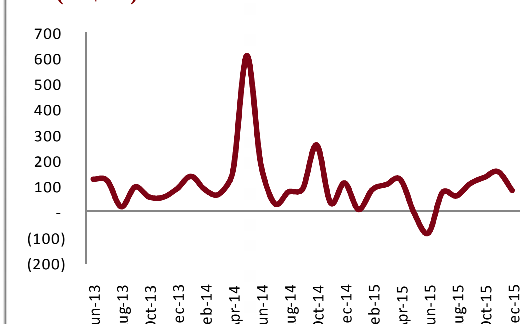
FDI (US$mn)



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Accumulate	>=5% to <=20% upside potential	Market Weight	= Weight in KSE
Hold	<5% to >5% potential	Under Weight	< Weight in KSE
Reduce	<=-5% to >=-20% downside potential		
Sell	<-20% downside potential		

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