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PAKISTAN INSTITUTE
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ECONOMICS

CONTINUITY IN MONETARY POLICY

Balancing Stability with Growth

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The Monetary Policy Committee (MPC) of the State Bank of Pakistan (SBP) meets on September 15, 2025, against a backdrop of macroeconomic stability, renewed external pressures, and a fragile but improving growth outlook. At its last meeting on July 30, the MPC held the policy rate at 11 percent. Since then, inflation has continued to decelerate, but the devastating floods in Punjab have reintroduced food supply risks and increased reconstruction-related import needs.



Inflation and External Balances: A Delicate Trade-off

Headline CPI inflation fell to a historic low of 3 percent in August, pushing the FY2025 average down to 4.5 percent—comfortably below the SBP’s medium-term target range of 5–7 percent. While this disinflationary trend provides breathing space, the widespread crop damage to rice, sugarcane, cotton, and vegetables threatens short-term price stability. At the same time, the July 2025 current account deficit of USD 254 million signals renewed pressure on external balances as import demand rises with reconstruction needs.

A premature or aggressive monetary easing could weaken the rupee, erode confidence, and offset recent gains in external stability. Thus, the case for continuity remains strong.



Macroeconomic Stability Anchored in Reforms

Pakistan’s macroeconomic fundamentals have entered a more stable phase. Implementation of IMF Extended Fund Facility (EFF) reforms has restored policy credibility, improved fiscal discipline, and strengthened external buffers. These reforms have created conditions where monetary policy can focus not only on inflation control but also on supporting a gradual recovery in growth and investment.

With real interest rates above 600 basis points, the central bank possesses policy space. However, prudence suggests a pause for now, with the possibility of gradual rate reductions in the months ahead if inflation remains subdued and the current account stabilizes.



Growth Imperatives and the Private Sector’s Case

Industry and businesses argue that the policy stance is too restrictive. High financing costs are limiting credit flows, delaying investment decisions, and weakening domestic demand. From a development perspective, prolonged high rates risk stifling the very recovery needed to generate jobs, incomes, and exports.

PIDE’s earlier analysis proposed a modest reduction of 100 basis points, citing improved inflation dynamics and reform-driven stability. Such a move would have supported private investment without undermining positive real rates. Going forward, monetary policy must align more closely with growth needs—ensuring that stabilization gains under the IMF program translate into expanded credit access, revived industrial output, and stronger private-sector-led growth.



Conclusion: A Stance of Continuity with Caution

The current juncture calls for measured continuity—holding the rate steady while signaling readiness for calibrated easing. This approach balances the dual objectives of safeguarding external stability and creating space for a growth pivot in the near future. For Pakistan, where floods disrupt agriculture and businesses struggle with financing costs, the credibility of policy lies not in abrupt shifts but in a steady, predictable course that builds confidence and supports investment.





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