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ICMA
MONETARY POLICY STATEMENT

MPS REVIEW

ISSUE # 25 | JULY 28, 2026

A Brief Assessment of SBP's Monetary Policy on Business and Economy

ICMA Research and Publications Department

Preamble

The State Bank of Pakistan (SBP), in its Monetary Policy Committee (MPC) meeting held on 27 July 2026, decided to maintain the policy rate at 11.5 percent. The decision reflects a cautious approach despite improving macroeconomic indicators, as inflation remains above the medium-term target while geopolitical tensions, global commodity prices and external risks continue to create uncertainty. Against this backdrop, this review assesses Pakistan's monetary policy stance through a comparative analysis of regional policy rates and the prevailing level of economic policy uncertainty to understand the rationale behind the MPC's latest decision.

In the ICMA Pre-Monetary Policy Outlook, it was observed that the monetary policy direction of the SBP has broadly remained aligned with the Federal Reserve, indicating that both central banks have generally moved in the same direction during the recent policy cycle. However, alignment in policy direction does not imply similarity in policy rates. As shown in Table 1, Pakistan continues to maintain the highest policy rate among the selected economies. This reflects Pakistan's domestic macroeconomic conditions rather than a divergence in policy direction. While lower interest rates could stimulate business activity through cheaper financing, Pakistan continues to face inflation above the target range, volatile global commodity prices and heightened geopolitical risks arising from the Middle East conflict. Under these conditions, an aggressive reduction in the policy rate could reignite inflationary pressures and weaken the progress made towards price stability. Therefore, maintaining the policy rate at 11.5 percent appears to be an appropriate and balanced policy response under the prevailing economic environment.

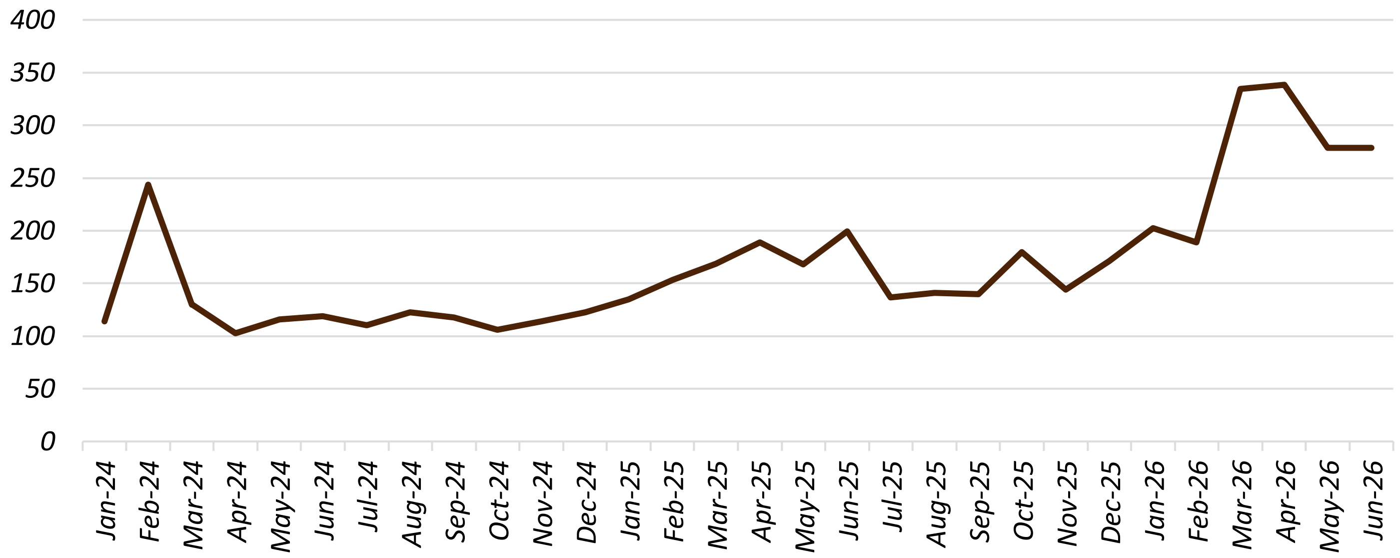
Table 1: Policy Rate Comparison Across Selected Economies

COUNTRY	POLICY RATE (%)
Pakistan	**11.5**
Bangladesh	10.0
Indonesia	5.75
India	5.25
United States	3.63

Source: *State Bank of Pakistan, Federal Reserve, Reserve Bank of India, Bangladesh Bank and Bank Indonesia.*

The need for a cautious monetary stance is further reinforced by the prevailing level of Economic Policy Uncertainty (EPU). Elevated uncertainty surrounding geopolitical developments, commodity prices and the external environment increase the importance of maintaining policy stability. In such circumstances, keeping the policy rate unchanged helps anchor inflation expectations, supports investor confidence and provides policymakers with greater flexibility to respond to emerging risks.

Figure 1: Pakistan's Economic Policy Uncertainty Index (EPUI), January 2024–June 2026



"Overall, the analysis indicates that the SBP's decision to maintain the policy rate at 11.5 percent represents a prudent and balanced response to prevailing macroeconomic conditions. Although headline inflation has moderated, it remains above the medium-term target, while the Economic Policy Uncertainty Index suggests that uncertainty continues to remain elevated amid geopolitical tensions and global economic volatility. Under such conditions, premature monetary easing could amplify inflationary and external-sector risks and undermine the progress achieved in restoring price stability. Maintaining the current policy rate therefore provides an appropriate balance between supporting disinflation and preserving macroeconomic stability. Going forward, monetary policy should remain data-driven and be complemented by targeted financing initiatives, supply-side measures and stronger fiscal-monetary coordination to support sustainable economic growth."

ICMA Policy Recommendations

1. Maintain the Current Policy Stance Until Inflation Moderates Sustainably

While inflation has shown signs of easing, it remains above the SBP's medium-term target range. Therefore, any policy rate reduction should be deferred until inflation demonstrates sustained moderation and inflation expectations become firmly anchored.

2. Support Businesses Through Targeted Financing Instead of Broad-Based Rate Cuts

To ease financing constraints without compromising price stability, the government and SBP should expand targeted financing schemes for export-oriented industries, SMEs and agriculture. Such measures would support productive investment while preserving the current monetary policy stance.

3. Complement Monetary Policy with Supply-Side Interventions

As inflationary pressures are increasingly driven by food prices, global commodity prices and supply-side disruptions, the government should strengthen food supply management, improve logistics and ensure timely availability of essential commodities. These measures would help reduce inflation without placing excessive reliance on monetary policy.

4. Strengthen Policy Coordination to Reduce Economic Uncertainty

Given the heightened uncertainty arising from geopolitical developments and global commodity price volatility, closer coordination between monetary, fiscal and trade policies is essential. A coordinated policy response would strengthen macroeconomic stability, improve market confidence and create the conditions necessary for a gradual monetary easing cycle.

ICMA's Research & Publications (R&P) Department sought views from economists and industry leaders on SBP's decision to retain the policy rate at 11.5 percent. Their perspectives reflected broad support for a cautious monetary policy stance amid external uncertainties, while stressing that sustained high interest rates continue to weigh on businesses and that future policy should gradually shift toward supporting economic growth as inflationary pressures ease.

Experts' Insight

Dr. Imran Batada, President, Pakistan Freelancers Association (PAFLA), shared that the SBP's decision to keep the policy rate unchanged at 11.5% reflects a cautious and prudent approach. Although inflation eased to 11.1% in June, it remains elevated, while global energy prices and geopolitical tensions continue to pose risks. However, the prevailing interest rate continues to pose challenges for businesses, particularly SMEs, exporters, and the technology sector. As inflation stabilizes, the SBP should gradually reduce the policy rate to encourage investment, improve access to financing, create employment, and support sustainable economic growth. While the decision supports short-term macroeconomic stability, future monetary policy should increasingly focus on stimulating productive economic activity.

Abdul Rahim Suriya, Partner at Suriya Nauman Rehan & Co., stated that the SBP's decision to maintain the policy rate at 11.5 percent reflects continued concerns over inflationary pressures arising from external shocks and geopolitical uncertainties. He emphasized that although the policy rate helps anchor inflation expectations, the prevailing interest rate environment continues to increase the cost of trade finance and working capital for exporters and businesses engaged in international markets. He further stated that elevated borrowing costs also influence corporate restructuring, debt management, tax planning, and regulatory compliance, making prudent financial management increasingly important.

Dr. Shahida Wizarat, a renowned economist, Reiterated her longstanding view that Pakistan's inflation is predominantly cost-push rather than demand-driven, limiting the effectiveness of policy rate adjustments in controlling inflation. Referring to a recent SBP statement linking the policy rate outlook to persistent geopolitical tensions in the Gulf region, she argued that monetary policy appears to be influenced by political-economic considerations. However, she emphasized that the policy rate is fundamentally a domestic instrument and should be determined primarily by Pakistan's macroeconomic fundamentals rather than external geopolitical developments.

Industry Insights

Muhammad Raza, Senior Vice President, Karachi Chamber of Commerce & Industry (KCCI), stated that the State Bank of Pakistan's decision to keep the policy rate unchanged is appropriate in view of the anticipated inflationary pressures arising from recent increases in fuel and energy prices, as maintaining price stability remains essential for preserving macroeconomic confidence and exchange rate stability. However, he emphasized that the current inflationary pressures are primarily cost-driven rather than demand-led, and that monetary policy alone cannot address inflation stemming from higher energy prices and taxation. He further highlighted that businesses continue to face elevated financing costs, expensive utilities, and a heavy tax burden, constraining industrial production and investment. He added that once the temporary impact of fuel and energy price adjustments subsides and inflation remains on a sustainable downward trajectory, the State Bank should gradually reduce the policy rate to support economic growth, exports, employment, and private sector

Zulfiqar Alam, CEO, Pakistan Housing Finance Company Ltd. (PHFC), told that the SBP's decision to maintain the policy rate at 11.5% reflects a cautious and prudent approach amid heightened global uncertainties, particularly the evolving US–Iran situation. He emphasized that the potential impact on international oil prices remains a key concern, as any sustained increase could create renewed inflationary pressures and affect Pakistan's external account. In this environment, maintaining the policy rate provides the SBP with the flexibility to assess how these external developments unfold before considering further monetary easing.

Junaid Naqi, Former President KATI, CEO, Prestige Textile, shared that Policy rate plays a critical role in cost of production and cash flows. SBP is tied up with external forces and things are getting more vulnerable. Retaining the rate at 11.5 is surprising. Businesses require better liquidity in these challenging times while more than 39 trillion is kept in banking sector. Government borrowing from commercial banks are increasing yet the decision needed are not taken.

MPC Observations on Key Sectors

Real Sector

- Economic activity slowed during Q4-FY26 due to higher global energy prices, the resurgence of conflict in the Middle East and domestic austerity measures.
- High-frequency indicators, including automobile sales, cement dispatches, fertilizer offtake and business sentiment, indicate a recovery in economic activity.
- The agriculture outlook has improved, particularly due to higher expected sugarcane production, while private sector credit and budgetary incentives are expected to support growth.
- SBP projects real GDP growth in the range of 3.5–4.5 percent during FY27.
- **Outlook:** ICMA believes that maintaining the policy rate at 11.5 percent will support macroeconomic stability while allowing the ongoing recovery in economic activity to continue. However, elevated financing costs may continue to moderate private investment until inflation eases further.

External Sector

- The current account deficit remained limited at US$139 million during FY26 despite a wider trade deficit.
- Record workers' remittances and a financial account surplus strengthened the external position.
- SBP targets foreign exchange reserves of US$20.2 billion by end-December 2026.
- **Outlook:** ICMA expects the current policy stance to support external stability by containing import-driven pressures while stronger remittance inflows and reserve accumulation continue to strengthen Pakistan's external buffers.

Fiscal Sector

- FBR achieved its revised FY26 tax collection target of Rs. 13 trillion.
- The primary balance remained in surplus for the third consecutive year, while fiscal consolidation is expected to continue during FY27.
- The MPC emphasized the need for continued tax reforms and reduction in public sector enterprise losses.
- **Outlook:** ICMA believes that maintaining the current monetary stance should complement ongoing fiscal consolidation; however, sustained structural and tax reforms remain essential to reduce future reliance on monetary tightening.

Money and Credit

- Broad money (M2) growth moderated to 13.2 percent.
- Private sector credit accelerated to 14.9 percent, with growth across working capital, fixed investment and consumer financing.
- Reserve money growth moderated alongside stronger deposit growth.
- **Outlook:** ICMA expects private sector credit to remain supportive of productive economic activity despite the unchanged policy rate, provided inflation continues to moderate and macroeconomic stability is maintained.

Inflation

- Headline inflation eased to 11.1 percent, while core inflation moderated to 8.4 percent in June 2026.
- Food inflation increased due to higher wheat and perishable food prices.
- Inflation is expected to remain above the target range in the coming months before gradually easing towards the 5–7 percent target range by June 2027.
- **Outlook:** ICMA expects the unchanged policy rate to support the continued moderation of inflation by anchoring inflation expectations; however, global commodity prices, food inflation and geopolitical risks will remain key upside risks to the inflation outlook.