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PRESS RELEASE

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Monetary Policy Falls Short: PRAC Calls for Bold Action to Revive the Economy

KARACHI – The Policy Research and Advisory Council (PRAC), led by Chairman Mohammad Younus Dagha, has expressed concern over the State Bank of Pakistan's (SBP) recent decision to maintain the policy rate at 11 percent despite widespread expectations of a reduction. While the Council acknowledges the SBP's cautious stance, it stressed that the decision does not align with the 200 basis points reduction strongly recommended by PRAC. According to Mr. Dagha, the decision falls short of delivering the necessary stimulus to drive the country's economic revival.

Headline inflation has steadily declined, reaching 3.2% in June 2025, with the FY25 average at 4.6%—marking the eleventh consecutive month of single-digit inflation. Despite this sustained disinflationary trend, the real interest rate remains elevated at 7.8%, one of the highest in the region. This high real interest rate continues to suppress private sector investment, inhibit industrial output, and undermine Pakistan's competitiveness in the global economy.

In comparison, regional economies maintain considerably lower real interest rates: India (3.4%), China (2.9%), Bangladesh (1.5%), Vietnam (0.9%), and Indonesia (3.4%). These more accommodative monetary environments have supported investment and growth in peer economies—an opportunity Pakistan risks missing without bolder policy adjustments.

Pakistan's private sector Credit-to-GDP ratio stands at just 11.4%, substantially below levels seen in India (50.1% in 2021), Bangladesh (35.8%), and Indonesia (36.4%). This underscores the chronic credit constraints faced by businesses, particularly small and medium enterprises (SMEs). These economies have demonstrated that sustained growth is achievable through lower interest rates and broader access to credit.

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The domestic business community had anticipated a rate cut to ease borrowing costs and spur industrial activity. However, data from the Large-Scale Manufacturing Index (LSMI) reveals a 1.2% contraction over the first eleven months of FY25—reflecting the strain high financing costs continue to place on productive sectors.

Compounding this challenge is the government's disproportionate share of domestic credit, absorbing 78.0% of total lending as of June 2025. This crowding out leaves the private sector with only 20.1% of available credit, while non-bank financial institutions (NBFIs) and other sectors account for just 1.9%.

PRAC maintains that the current macroeconomic conditions present a clear case for deeper monetary easing. A rate cut of at least 200 basis points is urgently needed to relieve pressure on businesses, improve credit access, and reinvigorate economic momentum.

Mr. Dagha emphasized the importance of increasing private sector credit as a share of GDP and called on commercial banks to expand lending to SMEs and growth-oriented sectors. Simplifying financing procedures and lowering collateral requirements would promote more inclusive access to credit and unlock the private sector's full potential.

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