Governor's Message

Global economy saw a sharp deceleration and buildup of significant challenges in 2022, as the lingering effects of supply chain disruptions and commodity price pressures were further compounded by the outbreak of Russia-Ukraine war. Central banks responded by sharply raising the policy rates to rein in the persisting inflationary pressures. Consequently, the global financial conditions tightened further and developing economies, in particular, faced external account pressures.

The stress in global economy accentuated Pakistan's economic challenges of external and fiscal account deficits and high inflation. The situation was further aggravated by the unprecedented flooding of Q3CY22 and delays in the completion of IMF program reviews. To contain rising macroeconomic imbalances and inflation, SBP adopted various stabilization measures including hike in policy rate, macro-prudential policy adjustments and administrative measures. Resultantly, the current account deficit started to improve, however economic activities started to slow down from H2CY22 onwards.

Despite these rising macroeconomic challenges, the soundness of banking and financial sector of Pakistan remained steady. Particularly, the banking sector continued to grow, posted higher earnings and observed improvement in capital adequacy ratio. While private sector credit moderated, the asset quality of the sector remained stable due to the prudent lending policies of banks. Most of the non-performing loan ratios were recorded at one of the lowest levels of last two decades and the latest performance indicators of corporate sector also depicted an overall steady debt repayment capacity of firms. However, banks' exposure to the government continued to increase in the context of fiscal strains while deceleration in deposits increased banks' reliance on borrowings.

The extant environment entails a number of vulnerabilities for the financial sector, nevertheless. The economic slowdown, elevated inflation and high interest rates portend pressures on repayment capacity of borrowers. Recent turmoil in the US banking sector also highlights a new perspective on hidden vulnerabilities that could emerge in the context of rapid changes in financial conditions and propagated by weaknesses in banks' business models. Besides, climate change and cyber security are also leading emerging risks, requiring enhanced focus of both the policymakers and industry.

In the backdrop of current challenging macro environment, it is important to proactively assess the resilience of the banking sector. As per our latest statistics and forward looking assessment, the banking sector in general, and large systemically important banks in particular, show adequate resilience to hypothetical shocks to specific risk factors and economic conditions. Scenario analysis shows that the capital adequacy ratio of banking sector against the assumed shocks remains above the minimum standard over a projected horizon of three years. However, to revive economic activities and ensure resilience of the financial sector on sustainable basis, the government needs to take appropriate measures to address macroeconomic vulnerabilities including measures to improve productivity, export competitiveness, fiscal consolidation and debt sustainability.

SBP's supervisory process proactively monitors and addresses both firm-specific issues and system-wide risks; besides, there are comprehensive safety nets and bank resolution arrangements to effectively manage any stress in the sector. This framework has worked well against various stress episodes in the past; however, SBP strives to keep the framework consistent with needs of the hour and is making necessary enhancements to ensure financial stability and promote access to finance. Besides various other regulatory developments, Environmental and Social Risk Management Implementation Manual has been issued to assist the industry in managing its underlying risks. Moreover, to promote digital financial services, the second phase of Raast was launched to enable instant Person-to-Person fund transfers, and a licensing and regulatory framework has been introduced for digital banks to promote digital banking in a sustainable manner. These initiatives have attracted overwhelming response from customers and investors.

In the face of challenging external and domestic environment, SBP remains vigilant to the evolving economic and financial dynamics. The Bank stands ready to take necessary measures in a timely manner to effectively address the emerging risks and discharge its mandate of preserving financial stability and supporting economic growth through sustainable flow of credit and continuous provision of financial services.

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