Governor's Message

After a sharp rebound in 2021 from Covid-19 pandemic, the global economic growth decelerated in 2022 and the trend continued in 2023 as well. The moderation reflects strong inflationary pressures and the consequent tightening of monetary policy stance across a number of advanced as well as emerging and developing economies. Nonetheless, tighter policy stance coupled with softening consumer demand, recovery in global supply chains and receding commodity prices put inflation on a falling trajectory in 2023 from its peak in 2022. However, the vulnerabilities that emerged in the wake of tighter monetary and financial conditions contributed to the banking sector turmoil in a couple of advanced economies in March 2023. The timely interventions by authorities, however, helped contain a widespread contagion and preserved the stability of global financial system.

Developing economies also faced pressures on several fronts, including higher debt-servicing costs and debt sustainability concerns. The increased frequency of geo-political tensions, especially the emergence of Middle East conflict and Red Sea disturbances, posed risks of supply-chain disruptions in global trade that could have implications for investors' sentiments and global financial markets.

Domestic economy continued to face some unprecedented economic challenges, particularly on the external front. Inflation touched a multi-decade high during CY23, affecting the purchasing power of households. Concomitantly, weak inflows kept external account under pressure, which translated into pressure on domestic currency. To respond to these challenges, SBP continued to implement tough but needed policy and regulatory interventions, including timely monetary and exchange rate policies along with other demand-management measures. Besides, SBP introduced reforms in exchange companies sector to improve transparency in the foreign exchange market. These stabilization measures have begun to yield desired results. Inflation is gradually coming down from its May 2023 peak; domestic currency has held ground and appreciated towards the end of CY23; and the macro-economy is on a recovery path. However, to put the economy on a sustainable growth path and address internal and external imbalances, it is imperative for the government to implement much needed structural reforms, including fiscal consolidation and broadening of tax base, achieving debt sustainability, and improving productivity and export competitiveness.

Despite tough economic conditions, the financial system remained resilient in 2023. Particularly, the banking sector, which contributes around 80 percent of the financial sector's assets, continued the provisioning of financial services, facilitated payments, exhibited steady performance and maintained its financial soundness. Assets of the banks recorded a notable expansion, which was mainly driven by investments, largely in government securities, reflecting the inadequate external financing and tax revenues that increased government's reliance on domestic sources of finance during CY23. However, the growth in advances moderated. Though deposit mobilization revived, banks also relied on borrowings to fund the asset growth. Nonetheless, banks' earning remained healthy on the back of increased volume of earning assets amid prevailing high interest rate environment.

The risks to financial stability that seemed relatively elevated at the start of the year subsided as the year progressed. The credit risk profile of the banking sector manifested no serious concerns due to adequate provisioning coverage of non-performing loans, though the infection ratio slightly inched up by end CY23, mainly due to moderation in the growth of advances. Solvency indicators such as capital adequacy ratio (CAR) of the banking sector improved further, largely on the back of higher earnings. The ratio remains well above the global standard as well as domestic minimum regulatory requirements.

SBP regularly conducts stress testing of the banking sector to assess its resilience against various hypothetical adverse scenarios. As per the latest assessment, the banking sector is expected to remain resilient to various hypothetical, severe but plausible, shocks over the projected horizon of three years and is expected to maintain its compliance with minimum capital adequacy requirements. As regards the key emerging risks, given the rising frequency of climate-related events in Pakistan and their likely impact on the banking sector, SBP has been incorporating the climate -related risks in its annual stress testing exercises. This year's FSR also includes a detailed 'Climate Risk Scenario Analysis' to assess the potential impacts of both physical and transition risks for the stability of banking sector of Pakistan.

The central bank is also actively engaged with all stakeholders to cater to the banking needs of under-served segments, especially SMEs, agriculture sector, and female clientele. The central bank is working to increase financial inclusion in the country by encouraging the usage of digital means to provide formal financial services to the unserved sections of the society. A significant progress has been made on the introduction and adoption of digital financial platforms in CY23. For instance, in-principle approvals were granted to five digital banks, and SBP's instant payment system, Raast, continued its growth momentum, with its outreach exceeding 34 million users. The introduction of new functionalities such as person-to-merchant (P2M) platform are expected to further boost adoption of this free instant payment system. Encouragingly, overseas Pakistanis increased their footprint as the gross inflows to Roshan Digital Accounts (RDA) have crossed US$ 7 billion, while the number of expatriates with active RDAs exceeded 650,000 in 2023.

SBP remains vigilant to the evolving economic and financial environment and stands ready to take necessary measures to effectively address the emerging risks to financial stability and support the continuation of financial services and flow of credit to the economy. I am pleased to mention that, in order to smoothly navigate the emerging challenges and to capitalize on potential opportunities posed by ever changing economic and financial landscape, SBP has set out its future trajectory with the launch of a five-year Strategic Plan, i.e., SBP Vision 2028. The Vision delineates strategic goals and activities and aspires to focus on five cross-cutting themes, viz., strategic communication, climate change, technological innovation, diversity and inclusion, and productivity and competitiveness to attain the statutory objectives in an effective and efficient manner. We are fully committed to transforming this vision into reality so that SBP is recognized as a credible, dynamic, and independent central bank with a high caliber team, committed to meaningfully contribute towards improving the well-being of the people of Pakistan.

Jameel Ahmad