

## Banking cartel

The Competition Commission of Pakistan (CCP) had found Pakistani banks “guilty of promoting cartelisation”. An inquiry committee of the CCP, headed by CCP senior member, cartels and trade abuses, had found seven major banks and the Pakistan Banking Association (PBA) “operating like a cartel to fleece depositors”.

The inquiry committee imposed a fine of Rs30 million on the PBA and Rs25 million on each of the seven guilty banks (which included some of the leading banks in the country).

No wonder the chief executive officer’s (CEO) remuneration at UBL is Rs11.5 million per month, Rs4.5 million per month at MCB, Rs4.4 million per month at ABL and Rs3 million per month at HBL. According to the IMF, the two countries where banks rake in the highest profits on the face of the planet are Pakistan and Columbia.

Over the past couple of years, return on average equity has been as high as 40.7 percent per year at Bank Al Habib. In 2013, returns on average equity were as follows: Citibank 33 percent, MCB 30 percent, UBL 27 percent, HBL 26 percent and ABL 25 percent.

On December 18, 2006, Dr Shamshad Akhtar, while addressing an international conference on ‘Fixed income market development in emerging market economies’, said: “Extraordinary banking spreads in Pakistan in recent years are an evidence of lack of competition and efficiency in Pakistan’s financial markets.” Dr Shamshad Akhtar did not do a thing during her three-year tenure as governor SBP.

Over 2009-2013, as per the Monthly SBP Statistical Bulletins, the lowest overall average spread was 6.2 percent and the highest was recorded at 7.5 percent (banking spread is the difference between the weighted average lending rate and the weighted average deposit rate).

The average interest rate spread in Canada is 1.3 percent; the UK 2.3 percent, Spain 2.4 percent, the US 2.8 percent, Australia 3 percent and France 3.1 percent. Asharaf Wathra, the 18th governor of the SBP, has no plans of breaking the cartel either.

An efficient banking sector accelerates economic growth. There is evidence also that high spreads have a negative impact on economic growth and employment. Wealth, within our society, is being transferred from Pakistani depositors to the banking cartel. Wealth, within our society, is being transferred from borrowers to the banking cartel. This transfer of wealth to the banking cartel amounts to around Rs300 billion per year.

According to the CCP, Pakistani banks are “functioning like an organised cartel and are involved in fixation of spreads and interest rates on different products in consultation with each other and there is no competition among them, which is leading to anti-competitive behaviour.”

Of the 192 member-states of the UN there are two countries where banks make the most money – Columbia and Pakistan. Around the world, forming a cartel is a criminal offence. In Pakistan, forming a cartel remains a civil wrong.

In Pakistan, all bankers are ‘friends’ and their customers are their common ‘enemy’. In the US, such behaviour was criminalised in 1890 (Sherman Act). In 2004, the US Congress passed the Antitrust Criminal Penalty Enhancement and Reform Act increasing the Sherman Act corporate fine to \$100 million and the individual penalty to \$1 million and/or a 10-year jail term.

Pakistan’s banking cartel is impeding our economic growth – the SBP a silent spectator. Pakistan’s banking cartel is maximising profits at the cost of the Pakistani society – the SBP a silent spectator. Whose side is the SBP on – the banking cartel or society?

Over the past decade, there has been an international movement towards criminalisation of cartel behaviour. Australia, Canada, Germany, Ireland, the UK, Denmark, New Zealand, Israel and Estonia have established explicit criminal law regimes to deter cartel behaviour.

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**CLARIFICATION- ARTICLE WITH REGARDS TO THE ISSUE OF “BANKING SPREAD”  
AND REMARKS BEING CIRCULATED IN CERTAIN CORNER OF MEDIA:-**

This is with reference to the article “Banking Cartel” of Mr. Farrukh Saleem published in daily “The News” on July 21, 2015. In this context, we would like to clarify that the understanding of the author is misplaced and are not based on facts. The factual position is given below:-

- a) The administrative action of the Competition Commission of Pakistan was in the context of introduction of the Enhanced Saving Account (ESA) which was introduced by Pakistan Banks Association in consultation with SBP with a view to provide the small bank depositor with an average deposit balances up to Rs. 20,000, a minimum of 4% profit on their saving deposits. Before the launch of this scheme, the small depositors did not have many lucrative options where they could invest their money and receive a worthwhile rate of return. The minimum profit rate of 4% pa was higher than the rates of return then offered by the banks. ESA was struck down by the Competition Commission of Pakistan as violating various provision of the

Competition Commission Ordinance 2007. However, the matter is pending before the Honourable Sindh High Court and is yet to be decided.

- b) As regards the issue of the extra-ordinary spread in the banking sector in Pakistan, the remarks of the author for SBP being a 'silent spectator' are also without merit and not based on facts. SBP has always been making efforts and insisting upon banks to bring efficiency by reducing the spread between the deposit and the lending rates. By the year 2007, SBP has been encouraging banks to develop products which provide reasonable rate of return to saving account holders especially the small depositors. In May 2008, SBP imposed upon banks/DFIs the minimum saving rate of 5% on all types of saving deposits. These instructions were later reviewed from time to time in the interest of the bank depositors.

Currently, the returns on deposits are linked with the interest rate corridor. As a result of above efforts, return on deposits improved and spreads declined. The weighted average deposit rate (WADR) for fresh deposits stood at 4.83 as of end May, 2015 whereas the weighted average lending rate (WALR) on fresh advances was at 8.61 percent. The spread between the two has come down from 7.03 percent in 2011 to 5.44 percent in June 2014 and to 3.78 percent in May, 2015.

- c) Profitability of the banking sector: Banks have earned profit after tax of PKR 627 billion during last 6 years. High earning also led to income tax payments of PKR 344 billion to the exchequer. A considerable portion of this profit has been retained by the banking industry, which has strengthened the capital base of the industry; the shareholders' equity of the industry stood at PKR 1 trillion and the Capital Adequacy Ratio (CAR) at 17.4 percent as of end March, 2015. Also financial business (mostly banking sector) attracted Foreign Direct Investment (FDI) of 21 percent of the total FDI during 2008-2015, which is only second to Oil and Gas Exploration Sector.
- d) Expansion of banking industry: Over the last decade, number of branches and employees almost doubled to around 12 thousand and 170 thousand respectively. In addition, banks have made huge investments in non-conventional modes like branchless/mobile/ internet banking that has facilitated in expanding the outreach of financial services to far flung areas. This healthy expansion also helped in consistent double digit deposit growth over the years. Over the last 4 years, number of domestic deposit accounts increased by 39 percent to 39.87 million while domestic deposits have increased by 53 percent to PKR 8.4 trillion. This healthy growth in deposit accounts and deposits shows trust of depositors in the banking system and negate the very assertion made by the writer that "customers are their (banks') common 'enemy'.

e) As far as compensation practices of banks, it is pertinent to mention that banks being human resource intensive organizations largely spend on human capital. Salaries expense account for around 50 percent of total administrative expenses. To attract high quality human capital, banks' spending on higher executive salaries is relatively high which commensurates well with their output generally.

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