THE EXPRESS
TRIBUNE
The New York Times
Thursday

Following Clarification published by Express Tribune on April 23, 2020 entitled: 'SBP rejects allegations of 'facilitating speculative behavior'

Express Tribune

SBP rejects allegations of 'facilitating speculative behaviour'

NEWS DESK

The State Bank of Pakistan, while rejecting the allegation of 'facilitating speculative behavior of commercial banks', has said that the issues raised in a news report "do not reflect the facts and are in fact misleading".

The central bank said the allegation was based on poor understanding of the monetary policy framework and its operations.

"As a matter of principle, the SBP considers it inappropriate to comment on issues raised on the basis of alleged leaked information," it said in a statement. "However, SBP also believes in the right of the public to authentic information that is based on facts and devoid of misconceptions. The issues raised in the said news report do not reflect the facts and are in fact misleading."

The SBP said its policy formulation and implementation was engrained in a sound framework based on best practices adopted by central banks across the globe. The transparency in implementation and a strong oversight mechanism is also reflected in the information disclosures by SBP.

"In May 2015, the SBP introduced a reformed interest rate corridor framework in accordance with the international best practices. The key feature of the framework is the introduction of a Policy (Target) Rate that unambiguously signals the SBP's monetary policy stance to achieve its objectives," the statement read.

"The Monetary Policy Committee (MPC) announces the Policy (Target) Rate and mandates the SBP to keep the overnight interbank money market repo rate close to this Policy (Target) Rate.

Thereafter, the monetary policy operations aim at keeping the short-term interest rates aligned to the Policy (Target) Rate with minimal volatility so as to ensure its better transmission to other benchmark interest rates like KIBOR."

The central bank said to ensure transparency in all its operations, it had committed to the market that the overnight repo rate would remain close to the policy rate through its various circulars.

"Accordingly, all open market operations (OMOs) of SBP, mop ups or injections, are conducted at levels which are close to the Policy (Target) Rate and this practice is being followed consistently since 2015." The State Bank further said to ensure oversight an internal Monetary Policy Operations Committee (MPOC) at the central bank consistently reviewed the implementation of the monetary policy.

"The MPOC is chaired by the governor and comprises members including deputy governors and other senior executives from various departments of the SBP. Further, update is also provided to MPC in each of its policy review meeting on the compliance to the mandate given by MPC that the overnight repo rate remains close to the Policy (Target) rate."

The central bank said in light of the facts mentioned above, it could be ascertained that assertions that open market operations conducted between January to May 2019 "facilitated speculative behaviour" which caused a loss of Rs6.5 billion to the national kitty" were baseless and misleading.

Following Clarification/Rebuttal was issued to Express Tribune in response to an article published on April 19, 2020 entitled: ' Finance Ministry accuses SBP of causing Rs.6.5b loss kitty'

As a matter of principle, SBP considers it inappropriate to comment on issues raised on the basis of alleged leaked information. However, SBP also believes in the right of the public to authentic information that is based on facts and devoid of misconceptions. The issues raised in the said news report do not reflect the facts and are in fact misleading.

1. At the outset SBP rejects the allegation of 'facilitating speculative behavior of commercial banks'. This allegation is based on poor understanding of the monetary policy framework and its operations. Monetary policy formulation and implementation by SBP is engrained in a sound framework based on best practices adopted by central banks across the globe. The transparency in implementation and a strong oversight mechanism is also reflected in the information disclosures by SBP.

2. In May2015, SBP introduced a reformed interest rate corridor framework in accordance with the international best practices. The key feature of the framework is the introduction of a Policy (Target) Rate that unambiguously signals the SBP's monetary policy stance to achieve its objectives. The Monetary Policy Committee (MPC) announces the Policy (Target) Rate and mandates the SBP to keep the overnight interbank money market repo rate close to this Policy (Target) Rate. Thereafter, the monetary policy operations aim at keeping the short term interest rates aligned to the Policy (Target) Rate with minimal volatility so as to ensure its better transmission to other benchmark interest rates like KIBOR.

3. To ensure transparency in all its operations SBP has committed to the market that the overnight repo rate will remain close to the policy rate through its various circulars. Accordingly, all open market operations (OMOs) of SBP, mop ups or injections, are conducted at levels which are close to the Policy (Target) Rate and this practice is being followed consistently since 2015.

4. To ensure oversight, an internal Monetary Policy Operations Committee (MPOC) at SBP consistently reviews the implementation of the monetary policy. MPOC is chaired by the Governor and is comprised of members including Deputy Governors and other senior executives from various departments of SBP. Further, update is also provided to MPC in each of its policy review meeting on the compliance to the mandate given by MPC that the overnight repo rate remains close to the Policy (Target) rate.

5. In the light of the facts mentioned above, it can be ascertained that assertions that open market operations conducted between January to May2019 "facilitated speculative behavior" which caused a loss of Rs6.5 billion to the national kitty" are baseless and misleading

Following article published in Express Tribune, Karachi on April 19, 2020

Finance ministry accuses SBP of causing Rs6.5b loss to kitty
By Shahbaz Rana Published: April 19, 2020

ISLAMABAD: The Ministry of Finance (MoF) has said that State Bank of Pakistan (SBP) "facilitated speculative behaviour" of commercial banks last year which caused a loss of Rs6.5 billion to the national kitty in just first five months on account of additional borrowing cost.

The central bank being the regulator of the banking sector is responsible to ensure that the banks do not exploit their customers, including the largest client – the federal government.

In addition to putting Rs6.5 billion additional burden on the national exchequer from January to May 2019 period, the federal government's non-tax revenues also took a hit due to the same reason, revealed a letter that the MoF had sent to the SBP Board in May last year.
The MoF had proposed to the SBP Board to take up this matter and order an investigation and also urged the central bank to review and improve its internal governance by reshuffling SBP officers who were serving in the same position for a considerable period.

The letter had been sent during the period when Younus Dagha was the federal finance secretary.

However, after he was transferred, the finance ministry did not push the matter further despite leveling serious allegations of facilitating speculative behaviour.

According to a senior ministry official, the MoF did not receive any reply from the central bank.

When contacted, SBP spokesman Abid Qamar said that the central bank would not respond to the questions.

The allegations of facilitating speculative behaviour surfaced amid a turf-war between the central bank and MoF on the issue of absolute autonomy to the central bank.

The federal government complained to the SBP board that certain activities were encouraging, rather facilitating; speculative behavior on part of some banks facilitated by certain elements in the management of SBP and hampering the objectives of ensuring transparency and efficiency of the financial markets.

The ministry stated that such actions forced the government to pay Rs6.5 billion in additional cost on borrowings from the commercial banks since January to May 2019.

The MoF also recently proposed that the chairman of the SBP board should be any ex-officio board member instead of the central bank governor.

In the letter, the MoF stated that the SBP elements facilitated the speculative behavior by misusing Interest Rate Corridor Policy (IRCP).

The central bank had introduced IRCP in 2009 aimed at defending its key policy rate and ensuring that the interest rates remained stable and banks do not exploit each other and their clients.

The interest rate corridor consists of two end-of-day standing facilities offered by SBP – repo facility to absorb excess funds of banks at the floor rate and a reverse-repo facility to lend to banks facing shortage of funds at the ceiling rate.

The stated purpose of introducing IRCP was to reduce the volatility in short-term interest rates and to bring more transparency in implementation of monetary policy.

The corridor policy allows the SBP to borrow from banks the surplus cash at rates 1.5% below the policy rate, known as floor rate.

It also allows providing banks loans at rates 0.5% above policy rate to meet their financing needs, known as ceiling.

Instead of penalising the banks by absorbing its surplus cash below 1.5% interest rates, the SBP borrowed at rates close to the then policy rate at a time when the federal government was in dire need of bank financing to meet its expenditure obligations.

According to the MoF, the central bank borrowed surplus liquidity from the banks without any regard to unexpected or autonomous liquidity shocks.

The ministry said that the surplus cash that the banks were not investing in the government bills was then borrowed by the SBP at rates close to the interest rates, which also caused loss to the federal government due to less profit of the central bank.

The central bank management supported speculative activities by the banks worked against the objectives of development, efficiency and transparency of financial markets, it added.

It significantly increased the borrowing cost of the government as the banks chose to avail one-week or two-week borrowing facilities of central bank rather than investing in 3-month government treasury bills when only a few days were left in the next monetary policy decision.

This was the period when the central bank was increasing its interest rates as part of prior conditions set out by the International Monetary Fund for extending the bailout programme.

The MoF also cited an example to prove its allegation of facilitative role played by the central bank to encourage speculative behavior by the banks.

It said that the T-bill auction of May 8, 2019 was a classic illustration of this issue.

With a maturity of Rs2.177 trillion and government target of Rs1.2 trillion, the banks only submitted bids to the tune of Rs560 billion.

The banks largely preferred to sit on idle liquidity instead of participating in the auction and then the central bank absorbed surplus liquidity of Rs1.918 trillion subsequent to the auction that facilitated this speculative decision.

The finance ministry further alleged that the central bank reduced the opportunity cost for the banks by mopping up their surplus cash at rates close to the key policy rate.

The SBP’s own profits were unduly reduced by several billions of rupees when borrowing at much higher rates than the floor rate of interest rate corridor without adequate justification, it added.

However, the central bank spokesman did not respond to the question whether the SBP had brought the issue before its board.

He also did not reply whether the SBP management had fixed responsibility against its officers.

Qamar also avoided a question whether this case was referred to National Accountability Bureau or Federal Investigation Agency.