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# SBP, Government working closely to restore macroeconomic stability: Dr Akhtar

Dr Shamshad Akhtar, Governor State Bank of Pakistan has said that the Federal Government and the central bank are working in tandem to restore macroeconomic stability.

In a press statement today she said that the Government and the central bank are taking several measures to improve the macroeconomic situation which has been adversely affected as a consequence of various global events such as seizing up of financial markets in the U.S. and Europe or escalating commodity and fuel prices in the international markets.

"The timing of these global developments could not have been worse. Not only was our economy's business cycle maturing after a strong and resilient performance but the socio-political set-up was also undergoing a transitional phase," she said and added that a combination of these elements would put the resolve of any government to test and Pakistan is no exception.

Dr Akhtar said that there has been a 350 basis point cumulative increase in interest rates since July 2007 which has been accompanied by appropriate market-led exchange rate adjustment in the wake of the balance of payments challenges. The Government has further assured of its resolve to curtail fiscal deficit -- a critical element of the macroeconomic stabilization program -- and to strive to ensure net zero central bank borrowings for each quarter with a view to achieve these objectives, fiscal tightening is being pursued through a combination of measures ranging from recurrent expenditure controls, removal of subsidies and rationalization and prioritization of development expenditures. She said and added that the early indications are that revenue growth is above expectations for the current fiscal year.

Referring to financing plan for meeting the budget and external sector requirements of the Federal Government, Dr Akhtar said that the Government plans to selectively privatize some assets and has been in dialogue with International Financial Institutions to meet the financing gap. "Advanced is the discussion with Asian Development Bank which has negotiated a $500 million program for accelerated economic transformation that focuses on supporting financial sector reforms among others," she said and added that in parallel, the World Bank has reassured its support for fast tracking investment programming of close to $1 billion which is focused on high priority development projects.

Dr Akhtar observed that continued resolve to deal with the short-and-medium-term power sector constraints and the dialogue with overseas investors is likely to bear fruitful results in attracting more foreign investment in the sector. Further deepening of macroeconomic stabilization program and more sector-based structural reforms should alleviate the constraints facing growth, while restoring investor confidence, she added.

SBP Governor said that in order to support the efforts to diversify the borrowings mix, the Government and the State Bank are working to launch the first Government of Pakistan Ijara Sukuk in the first week of the Holy Month of Ramadan. “This will not only help deploy the liquidity available with Islamic Banks but also help the Government to diversify its debt,” she said and added that given the growth in the Islamic Banking Industry, Shariah-compliant Government securities are imperative to bring the Islamic Banks parallel to their conventional counterparts in terms of instruments available for liquidity management.

Dr Akhtar said that eventual uniformity of regulatory reserves of Islamic banks with that conventional bank is also essential for ensuring stability of financial/banking system. The State Bank has urged the Islamic Banks to aggressively mobilize new deposits and play their role in bringing the currency in circulation into the banking system. Banking system is also being incentivized through introduction of minimum deposit rate (to better remunerate savers) and easing of reserve ratios to mobilize more aggressively long term resource mobilization to be able to meet the growing and diverse requirements of the economy.

SBP Governor pointed out that first quarter (January-March of CY 2008) statistics show that the banking system is on track in terms of solvency, asset quality, earnings, and service to society. She said that the system also registered a growth though at a slackened pace as compared with past trends for the first quarter. The asset base of the banking system since last quarter of 2006 has grown by 22% to Rs5.2 trillion that is well supported by 36% growth in the equity and 21% growth in deposits. The risk based capital adequacy ratio stands at 13.1%, well-above the minimum required level of 8 percent. “It is this buffer that continues to provide resiliency to the banking system,” she added.

She said although Non-performing loans (NPLs) in volume increased by Rs18 billion during the first quarter, the higher level of provisioning has ensured that the infections impact remain in check as evidenced from the Net-NPL-to-Net-Loans ratio which was 1.3% in March 2008 as compared to 1.6 % in December 2006, signifying that the banks set aside more reserves out of their earnings to cover the increase in loans that had become non-performing. Accordingly, the NPL coverage ratio and capital impairment ratio have improved; NPL converge ratio stood at 84.1% in March 2008 as compared to 78% in December 2006, while capital impairment improved from 9.7% in December 2006 to 6.8% in March 2008.

“This improvement was also backed by regulatory drive of SBP whereby the provisioning requirements were further strengthened in line with best international practices,” she said and added that due to this change in regulatory requirement, banks had to provide additional provisioning expenses in 2007. The banks’ strong earning capacity enabled them to absorb this additional charge and post a pre-tax profit of Rs 28.1 billion in March 2008 quarter – which was slightly less than the Rs 33.1 billion profit of corresponding quarter of March 2007, she added.

She asserted that it is important to see the current conditions in a long term perspective. “There is ample room for growth in banking assets as the current level of penetration of financial services is still quite low,” she said and added the banking sector is the major credit provider to the real Sector and growth in GDP provides an essential impetus to the growth in banking products. She said this potential demand in the country would be the driving force for the growth and performance of the Banking sector and added that the challenge for banks is to show resilience in times of temporary adverse market trends, which due to their capital and reserve build-up they are in a position to do.

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