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# SBP Governor's briefing on State of Pakistan Economy to Senate Committee on Finance

Dr Shamshad Akhtar, Governor State Bank of Pakistan, today stressed the need for aggressive implementation of anti-inflation policies which will provide relief to the general public and restore investors' confidence.

While giving a presentation on 'State of Pakistan Economy' to the Senate's Standing Committee on Finance, Revenue, Economic Affairs and Statistics in Islamabad, Dr Akhtar emphasized that fiscal sustainability is a key factor for macroeconomic stability, which requires increase in tax-to-GDP ratio; containment in non-productive expenditures and expanding public-private partnership. She said that there is also a need to increase exports through diversification of products and markets and enhancing productivity while imports need to be curtailed through containing aggregate demand.

Dr Akhtar said that inflationary trends in the country will settle as the global inflation has come down and Government has reiterated its commitment to achieve net zero borrowing from central bank. Decline in fiscal deficit to sustainable level and low inflation can play an essential role in improving saving rate, she added.

SBP Governor said additional funding needs to be secured to meet the Current Account Deficit which will require i) increase in savings to reduce reliance on external financing, ii) restoration of investor's confidence to encourage investment inflows and restrict outflows and iii) consistency and continuation of prudent policies. She said that with the inflow of $3.1 billion from the International Monetary Fund, the country's foreign exchange reserves climbed back to $9.4 billion by November 26, 2008.

Dr Akhtar gave a detailed account of the country's current economic situation in the backdrop of global financial crisis and highlighted issues, challenges faced by the economy. While referring to SBP's recent decision to raise its key policy rate to 15%, she said that under the current situation further monetary tightening was necessary to ease demand pressures and ensure long-term growth on sustainable basis.

She said the move will create room for government to borrow from market sources, improve rate of return on savings, control inflationary expectations and stem second round effect of inflation, check depletion of foreign exchange reserves and depreciation of exchange rate. She, however, mentioned that even after the 200-basis-point increase in the policy rate, current real interest rates are negative and credit to private sector remained strong.

She pointed out that with the adjustment in interest rates and other policy measures, the rupee has appreciated by 3.6 percent during end October to November 25, 2008.

Dr Akhtar also highlighted several other measures taken by the State Bank for the benefit of different sectors of the economy. Talking about the agriculture sector, she said agriculture credit disbursement indicative target for FY09 has been enhanced by 25% to Rs 250 billion, which is 18% higher than disbursement in FY08. In addition, the State Bank also developed and launched Crop Loan Insurance Scheme under which the government has agreed to share premium cost of subsistence farmers. The State Bank has enhanced the indicative per acre credit limit for major and minor crops, livestock, orchards, fishing and forestry by an average 70 percent, she added.

Referring to measures taken to boost export and industrial investment, Dr Akhtar said the State Bank has restored 100% refinancing under EFS and LTFF to promote real investment in the country and to mitigate the impact of higher interest rate. Similarly, overall quantum of limits for banks under EFS for FY09 has been enhanced by 25% of the amount outstanding as on 30th June, 2008. She said that under these schemes borrower have to pay a maximum of 7.5% mark-up against 14.4 % prevailing weighted-average rate.

Briefing Senate Committee's members about the recent liquidity crunch, Dr Akhtar pointed out that the SBP provided on a timely basis over Rs350 billion liquidity support besides the regular injection of liquidity through open market operations. The liquidity constraints emerged as a result of excessive public sector borrowings, deposit withdrawal and Eid cash withdrawal, she added.

SBP Governor said that the State Bank launched liquidity support for small banks which provides maximum 3 months liquidity for small banks willing to restructure/inject new capital. This facility is available at SBP policy discount plus 3% and is supported by Government guarantee, she added. Similarly, in order to encourage more sustainable growth in deposit mobilization, SBP has imposed minimum deposit rate and exempted long tenor deposits from reserve ratios, she said.

Dr Akhtar said that despite economic stress faced by the country, the banking system is sound and its risk absorption capacity is 'strong.'

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