

Governor's Message



In the midst of the gradually improving but nevertheless challenging domestic macroeconomic environment and the repercussions, albeit indirect, of the ongoing Eurozone financial crisis, State Bank of Pakistan continued to strive to maintain the delicate balance of achieving price stability without prejudice to growth in 2010-11, while also ensuring the stability of the financial sector. Notably, the focus on monetary tightening saw a pronounced shift in the second half of the year when concerns about economic growth came to the fore and a more cautious view was adopted on the monetary stance. Keeping in view inflation trends and the Federal Government's targets for inflation and growth for 2011-12, a reversal of the monetary stance was initiated from July 2011. Some of the key policy measures undertaken during the year are summarized below:

- **Monetary Policy:** SBP raised the policy rate by 50 bps each on 3 occasions to 14.0 percent in the first half of 2010-11, before deciding to maintain status quo in the second half of the year. A more focused approach to monetary easing has been initiated in FY12; since July 2011, the policy rate has been reduced by 200 bps to 12.0 percent.
- **Soundness of the Financial System:** The soundness and resilience of the Banking System can be gauged by the capital adequacy ratio of 14.1 percent at end-June 2011, comfortably above international minimum requirement of 8.0 percent. Fully cognizant of the concerns for credit risk in the banking system, banks' loan portfolio is continuously being closely monitored by SBP.
- **Liquidity Framework:** Keeping in view the role of liquidity in triggering or mitigating financial crisis, SBP has launched work on developing a framework for monitoring the liquidity risk profile of banks and DFIs on a weekly basis. Besides continuing with the current practice of monitoring banks' and DFIs' compliance with statutory liquidity requirements, the new framework will assist in assessing the developing trends in the liquidity profile of individual banks through a set of newly introduced variables and ratios.
- **Launch of New Banks:** During the year, commercial banking licenses were issued to the Industrial and Commercial Bank of China (ICBC) and Sindh Bank Limited, in addition to allowing NRSP Microfinance Bank to commence business on a nation-wide basis. The entry of ICBC, a top tier global bank, has positive implications for Foreign Direct Investment in the financial sector, as well as for the overall outlook of the country.
- **Exchange Rate:** In addition to the economic factors, SBP's proactive approach also facilitated the smooth functioning of financial markets, by focusing on enabling market forces to play their due role in the determination of exchange rate. In line with this strategy, SBP further increased the maximum cap on aggregate Foreign Exchange Exposure Limit of banks to PKR 2,500

million. This measure significantly enhanced the banks' capacity to smoothly handle large volume transactions without putting any undue pressure on the exchange rate. Consequently, the Pak Rupee showed healthy volatility during the year with movement in both directions reflective of the prevalent demand and supply conditions.

- **Currency Swap Arrangements:** During the year, SBP developed a framework of executing bilateral currency swap arrangements (CSA) with regional central banks in the respective local currencies with the objective of boosting bilateral trade and investment in local currencies. As a result, a bilateral CSA was concluded on 1st Nov 2011 between SBP and the Central bank of the Republic of Turkey (CBRT) in Pakistan Rupee / Turkish Lira amounting to US\$ 1 billion in equivalent local currencies and in December 2011 with the Peoples Bank of China equivalent to US\$ 1.5 billion.
- **Financial Inclusion:** To promote financial inclusion and further enhance outreach of financial services, the Branchless Banking Regulations were revised to cater to the needs of the unbanked population through a provision of efficient and cost effective basic banking services at convenient places. The existing branchless banking deployments have the capacity to cater to the needs of over 10 million potential beneficiaries of G2P payments in Pakistan. Moreover, the branchless touch points have surpassed 20,000 agents across the country whereas throughput value of transactions has exceeded Rs. 196 billion in a short span two years. Over one and a half million monthly average transactions are taking place in branchless banking setup.
- **Protecting Consumers' Interest:** With a view to ensuring enhanced outreach of financial services while protecting the interest of the consumer, SBP implemented necessary policy measures during the year. Banks were restricted from levying service charges on regular saving accounts for maintaining a minimum balance, and were allowed to open dedicated Home Remittance Centers for making payments to the beneficiaries of home remittance.
- **Amendments in Banking Companies' Ordinance:** To strengthen SBP's regulatory role, certain amendments in the Banking Companies Ordinance, 1962 were promulgated during the year, the significant features of which entailed powers to ensure fitness and propriety of sponsors/major shareholders of banks, to increase banks' capital as per their risk profiles, and specific triggers for invoking corrective actions.
- **Consolidated Supervision:** To address the risks arising from conglomeration in the financial sector, a Consolidated Supervision Framework is being developed for which a formal set-up has been established.
- **Payment and Settlement Systems:** A focused approach on enhancing the Payment System infrastructure in the country is starting to pay dividends. During the year, effective and timely measures were taken by issuing instructions and guidelines to commercial banks for better controls on Alternate Delivery Channels ADCs. With a view to provide greater flexibility and wide range of value added services to customers, banks were allowed to launch a number of innovative card products during the year under review. Customer Fund Transfers facility was also launched in February 2011 through Pakistan Real Time Inter-Bank Settlement Mechanism (PRISM) system and Multiple Credit Transfers facility for bulk payments through this system has also passed the testing phase and will be available for banks in the next financial year.

I would like to conclude with a note of appreciation for the SBP's Central Board of Directors for their support in discharging my statutory responsibilities.

Yaseen Anwar
Governor State Bank of Pakistan