Chapter 5

Money and Credit

The financial liberalization and development of new financial instruments has raised the efficacy of monetary policy for a sustainable economic growth. Over the years, it has not only contributed towards maintaining price stability but also played a stabilizing role in affecting the economic growth through number of channels. Moreover, a suitable approach of monetary policy has also been recognized for a well-functioning financial system in particular during the recent global financial crisis with a growing consensus that for a sustainable economic growth, a country must ensure the stability of financial system because the downfall of financial system leads to the failure of economic system as it happened in the global financial crisis 2007-08.

The financial crisis that has gone through a number of phases since 2008,have witnessed an appreciable improvement since October, 2012 onwards with a significant reduction in near term stability risks in Euro area thus providing further support to the economies along with enhancing the confidence together with positive economic outlook. Similarly, there is also an improvement in funding conditions in the markets for sovereign, bank and corporate debt. Nevertheless, the elevated funding costs, deteriorating asset quality and weak profits still reflects the significant challenges for many banks in the Euro area.

Financial system in Pakistan proved to be more strong and resilient during the global financial crisis due to its limited exposure and the basic nature of exports, as Pakistan's exports are largely low value added cotton products, intermediate cotton products and primary commodities. Nevertheless, the economic resilience was tested several times owing to numerous challenges the country has faced into the period of five years. On one hand the country confronted the issue of less external inflows due to volatile security situation, while on the other hand power crisis along with massive floods and rains and global economic slowdown further aggravated the situation. Consequently, there was a significant decline in investment rate, increase in the debt burden and a sharp reduction in foreign exchange reserves. Furthermore, substantial fiscal borrowing in the absence of sufficient external inflows exerted a significant pressure on monetary management. Despite a significant reduction in interest rates, deceleration in accumulation of Non Performing Loans (NPLs) and an improvement in deposit growth, there was a low utilization of credit by the private sectors as banks were more comfortable to invest in government papers. In spite of all this, most of the macroeconomic indicators performed well as inflation was successfully brought down to single digit during 2012-13. Year on Year inflation reduced to 5.8 percent in April, 2013 as compared to 11.3 percent last year. Fiscal deficit contained at 4.6 percent of GDP during July-March, 2012-13. Current account posted a deficit of $1.0 billion against $ 3.0 billion during the same period last year. The improvement during the year is primarily attributed to $1.8 billion received under the Coalition Support Fund (CSF). Still the risks to external current account and its financing cannot be overruled due to projected shortfalls in financial and capital inflows and scheduled repayments of IMF loans that would result in further depletion of foreign exchange reserves, leading to increased pressures on exchange rate. Equally, the economy is confronting with the challenge of containing the inflationary pressures. Keeping in view all these developments, SBP responded cautiously to further improve the current economic situation.

Monetary Policy Stance

Central banks generally use the monetary policy as an important tool to achieve certain objectives that are crucial for economic growth and stability. However, the effectiveness of monetary policy is contingent upon improvements in the fiscal and the balance of payment position.

Recently monetary policy in Pakistan has undergone substantial changes in tandem with volatile economic conditions within the country. In particular, relentless inflationary pressures, global economic downturn , heavy reliance on domestic borrowing in the absence of diversified financial sources and consequently low credit to private sector resulted in the policy stance that has been largely supportive of the dual objective of promoting economic growth and price stability along with the revival of credit to private sector.

Table 5.1: Policy Rate	
w.e.f	**Policy Rate**
Nov-10	14.0
Aug-11	13.5
Oct-11	12.0
Nov-11	12.0
Feb-12	12.0
Apr-12	12.0
Jun-12	12.0
Aug-12	10.5
Oct-12	10.0
Dec-12 until date	9.5

Source: State Bank of Pakistan

SBP has adopted relatively an expansionary policy stance for the past two years as the policy rate has been reduced by cumulative 400 basis point from 13.5 percent in August 2011 to 9.5 percent in December 2012.It is pertinent to mention that during the first half of current fiscal year 2012-13, the policy rate was slashed by cumulative 250 basis point to 9.5 percent on account of positive inflationary outlook together with a retirement of fiscal borrowing from SBP and improvement in the external current account deficit in October 2012. While keeping in view the major risks to medium term inflation outlook owing to high growth in monetary aggregates, upward adjustments in administered prices and risks to the balance of payment position in the remaining months of 2012-13, SBP has decided to keep the policy rate unchanged at 9.5 percent on 12th April, 2012-13.

Recent Monetary and Credit Development

During July –3rd May2012-13, money supply (M_2) increased by 9.2 percent (Rs.705.8billion) against the growth of 8.7percent (Rs. 581.2 billion) in the comparable period last year. The growth in M2 during July-3rd May2012-13 is mainly contributed by the improvement in Net foreign assets (NFA), rise in Net domestic assets (NDA) and credit off take by the Public Sector Enterprises (PSEs).The reserve money grew at much faster pace of 13.1 percent against the expansion of 9.6 percent in the comparable period of last year.

Table: 5.2- Profile of Monetary Indicators (Rs. Billion)

	Jul-3May 2012-13	Jul-4May 2011-12
1.Net government sector Borrowing(a+b+c)	**874.0**	**962.0**
a .Borrowing for budgetary support	988.0	1,051.6
b. Commodity operations	-115.1	-90.0
c. Others	1.3	0.4
2.Credit to Non-government Sector (d+e+f+g)	**185.0**	**117.9**
d. Credit to Private Sector	142.0	251.8
e. Credit to Public Sector Enterprises (PSEs)	43.3	-134.6
f. PSEs Special Account-Debt repayment with SBP	-0.2	0.0
g. Other Financial Institutions(SBP credit to NBFIs)	-0.1	0.7
3.Other Items(net)	**-171.6**	**-241.6**
4.Net Domestic assets (NDA)	**887.4 (12.5%)**	**838.4 (14.2%)**
5.Net Foreign Assets (NFA)	**-181.6**	**-257.2**
6.Monetary Assets(M2)	**705.8 (9.2%)**	**581.2 (8.7 %)**

Box 1:
Monetary Policy stance in South Asia

The combine growth rate of South Asian region (Afghanistan, Bangladesh, Bhutan, India, Maldives, Nepal, Pakistan and Sri lanka) stood at 4.7 percent in 2012 and it is expected to increase up to 5.5 percent in 2013 with continuing efforts to create fiscal space and boost private investment. The countries of the region are at risk to various external shocks such as widening of current account deficit, low level of foreign direct investment and medium term risks to inflationary outlook. Fragile economic prospects have thus limited the ability for central banks to use monetary policy in order to overcome the economic slowdown. Moreover, some countries have witnessed the sharp decline in foreign exchange reserves like Maldives and Pakistan.

Keeping in view all these economic development, the monetary policy stance within the region has been accommodative as it is evident that with the exception of Srilanka and India, real interest rates remain negative for other countries in the region. Recently, Reserve Bank of India adopted easy monetary policy stance by reducing its repo rate by 25 basis points in January and March, 2013, down to 7.5 percent. The policy stance since January, 2012 was to address the risks to growth.

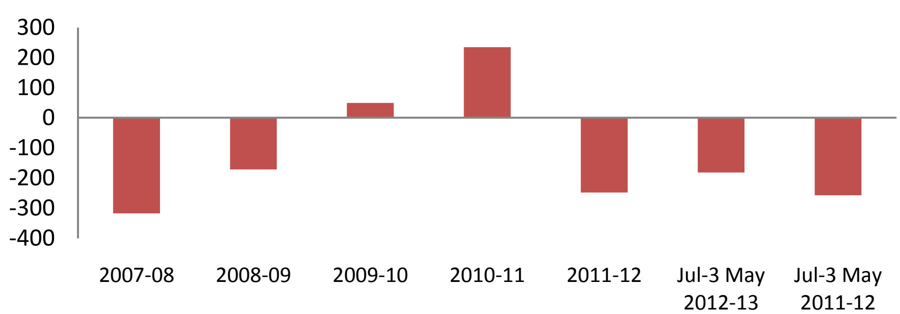
Srilanka has also followed accommodative policy stance by shifting from tight policy stance. The policy stance was broadly due to falling growth rates and the low inflation. The central bank had raised policy interest rates in February and in April, keeping them steady until making a small downward adjustment in December. The policy rate was reduced from 9.75 percent to 9.50 percent in December 2012.

Similarly, Bangladesh's monetary policy stance during fiscal year 2013, contributed to ensure the external sector stability achieved along with attaining maximum economic growth. Central bank of Bangladesh slashed the policy rate since 2009, keeping in view the risks to economic situation of the country from uncertain global economic outlook. Policy rate has been lowered to 7.25 percent from existing 7.78 percent.

Source: South Asia Economic Focus: The World Bank, Spring 2013.

Net Foreign Assets (NFA) witnessed some improvement during the period under review as it reduced to Rs. 181.6 billion as compared to the net contraction of Rs. 257.2 billion last year. The improvement in NFA however, is mainly on account of realization of $1.8 billion under the Coalition Support Fund (CSF) during the first half of 2012-13.

Fig: 5.1- Net Foreign Assets of the Banking System



Despite some improvement, NFA remained under great pressure due to decline in foreign exchange reserves on account of debt repayment to IMF since February 2012 and drying up of external financial inflows. The pressure on foreign exchange reserves is likely to remain owing to another payment of $561.3 million to IMF in the coming months. Till 10th May, 2013 Pakistan has repaid $ 3.7 billion to IMF.

NDA of the banking sector increased by 12.5 percent (Rs. 887.4 billion) as compared to net expansion of 14.2 percent (Rs. 838.4 billion) in the same period last year. The PSEs borrowed Rs. 43.3 billion during July- 3rd May, 2012-13 against the retirement of Rs. 134.6 billion during the same period last year.

During July-3rd May, 2012-13, Credit to public sector enterprises (PSEs) witnessed an expansion of Rs. 43.3 billion against the retirement of Rs. 134.6 billion in the comparable period last year on account of high credit demand by the loss incurring PSEs. During the period under review Pakistan Steel Mills Limited, Pakistan International Airline and a Power sector holding company borrowed significantly from banks to repay their long term loans. Going forward, Net retirement during 2011-12 was largely due to the one-off payment in order to reduce the circular debt in energy related PSEs and the receivables of procurement agencies.

Government Bank Borrowing

The government borrowing from the banking system for budgetary support and commodity operations stood at Rs. 874.0 billion during July-3rd May, 2012-13 as compared to Rs. 962.0 billion in the comparable period last year. The decline in borrowing for budgetary support during the period under review was primarily due to one-off settlement of Rs. 391 billion in the first half of fiscal year 2011-12 and containment of fiscal deficit at 4.6 percent of GDP during July-March, 2012-13.

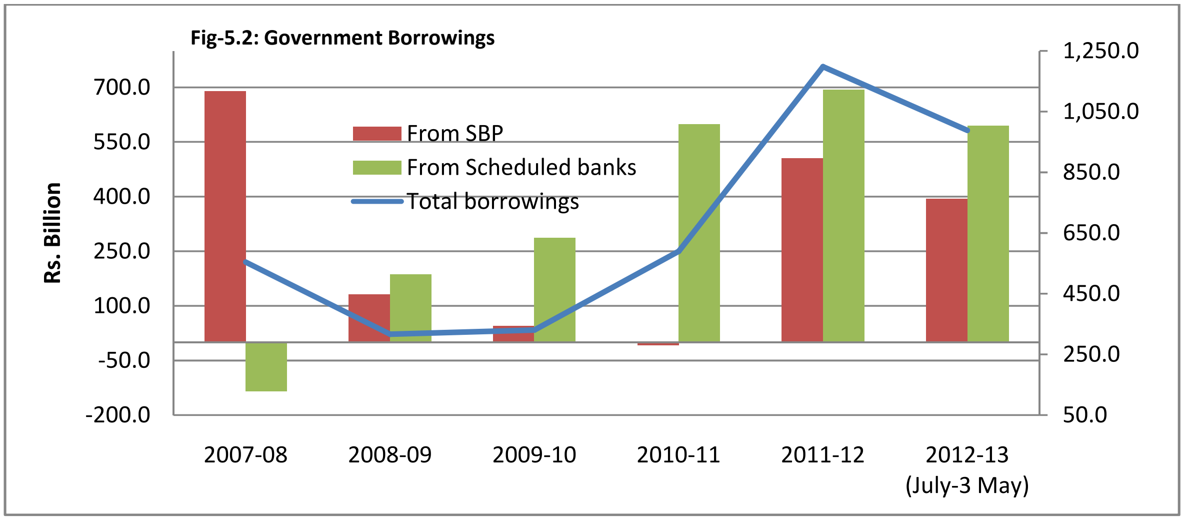


Fig-5.2: Government Borrowings

Additionally, the government borrowing has been declining gradually as the SBP has reduced the injection of liquidity into the money market. Government borrowing for budgetary support stood at Rs. 988.0 billion during July-3rd May, 2012-13 against Rs. 1,051.6 billion in the same period last year. Within banking system, large part was financed by commercial banks as it stood at Rs. 595.0 billion as compared to Rs. 615.8 billion last year. Low borrowing from the scheduled banks during the year was due to bank's low appetite for investment in government papers. On the other hand borrowing from the SBP remained at Rs. 392.8 billion lower than the previous level of Rs. 435.8 billion recorded in the same period of fiscal year 2011-12. Nevertheless, shift in government's borrowing from commercial to central bank is worrisome as it is more inflationary in nature.

Commodity Finance

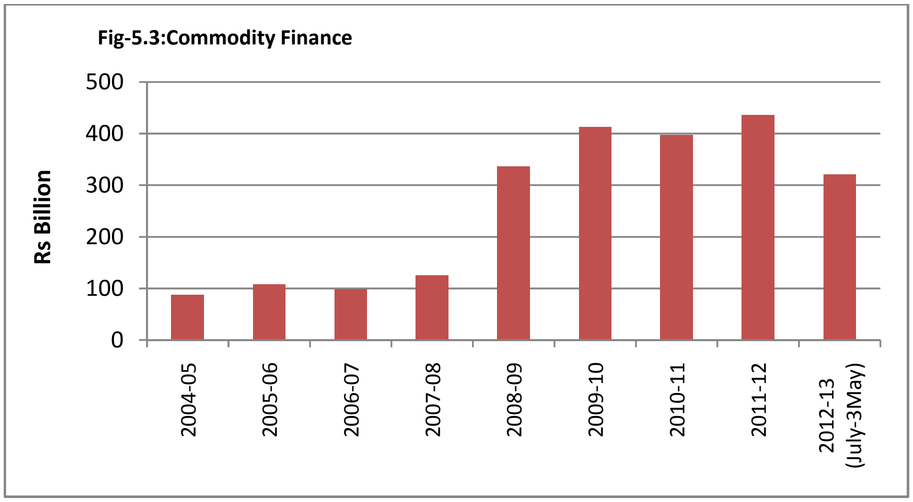
Commodity financing recorded a significant increase since 2009 owing to relatively higher support price for major food crops. In 2012-13, the support price of wheat for next crop has been increased from Rs. 1,050 per 40 kg to Rs. 1, 200 per 40kg.

During July-3rd May, 2012-13 loans for commodity operations registered a net retirement of Rs. 115.1 billion as against the retirement of Rs. 90.0 billion during the same period last year. Rise in net retirement during the period under review was mainly on account of retirement of Rs. 144.9 billion borrowed for wheat finance as compared to the net retirement of Rs. 82.5 billion in the comparable period last year.

The government`s financing requirements for its commodity operations peaked to Rs. 436.1 billion (grew by 9.7 percent) in June 2012 mainly on account of record wheat procurement of 9.2 million tons by different federal and provincial departments, despite the release of Rs. 78 billion to procurement agencies by the government for the settlement of accumulated subsidies. Whereas the stock of commodity finance increased to Rs. 321.0 billion during July-3rd May, 2012-13 against the stock of 307.5 billion recorded in the same period last year. The rise in stock during the current fiscal year was primarily attributed to increased borrowing needs for the import of fertilizer. On the other hand, the outstanding loans to wheat procurement agencies declined as the Punjab Food Department offloaded its wheat stocks in October and onwards.

Credit to Private Sector

Credit to private sector increased to Rs. 142.0 billion during July-3rd May2012-13 as compared to the expansion of Rs. 251.8 billion in the comparable period of last year. Whereas year on year growth has shown an increase of 4.2 percent up to July-3rd May, 2012-13 (Fig: 5.4). During fiscal year 2011-12, credit to private sector witnessed a highest YoY growth of 7.5 percent since 2008which was primarily driven by non-bank finance companies (NBFCs).



Despite the decline of 250 bps in policy rate during 2012-13 credit to private sector could not gain the momentum as it was expected. The muted growth was attributed to the severe energy shortages, and law and order situation. Additionally, rising trend in government borrowing for budgetary borrowing from the commercial banks have also restricted the expansion of credit to the private sector. Consequently banks rather than extending credit to the private sector preferred to invest in government papers despite a significant deceleration in Non Performing Loans (NPLs) and an improvement in their deposit base.

Nevertheless, the cumulative decline of 250 basis points in the policy rate during the first half of current fiscal year although contributed towards the revival of private sector credit; still it is lower than the previous level recorded during the same period of FY12. Private sector witnessed a highest flow of credit during the second half of 2012-13, as it stood at Rs. 189.5 billion as compared to the retirement of Rs. 84.9 billion in first quarter and Rs. 35.2 billion of expansion in the third quarter.

Sectoral Analysis

According to the Sector wise growth in credit to private sector business, 0.8 percent growth was recorded during fiscal year 2011-12, whereas, during July-March, 2012-13 private sector business registered a growth of 6.7 percent against 1.8 percent recorded in the same period last year.

Table: 5.3 - Credit to Private Sector **(Rs. Billion)**

Sectors	End June Stocks		July-March (Flows)		Growth Rates	
	Jun-11	Jun-12	2011-12	2012-13	2011-12	2012-13
Overall Credit (1 to 5)	2,918.2	2,922.0	41.6	188.7	1.4	6.5
1. Loans to Private Sector Business	2,431.8	2,450.1	42.9	165.1	1.8	6.7
A. Agriculture	180.5	198.4	10.5	14.3	5.8	7.2
B. Mining and Quarrying	17.9	15.9	-2.8	5.9	-15.7	37.1
C. Manufacturing	1,385.4	1,389.9	65.0	145.5	4.7	10.5
Textiles	514.7	491.0	16.4	74.9	3.2	15.3
D. Electricity, gas and water supply	269.4	278.1	-12.2	-0.8	-4.5	-0.3
E. Construction	67.7	53.5	-9.5	-1.2	-14.0	-2.2
F. Commerce and Trade	213.7	210.0	-4.3	1.8	-2.0	0.8
G. Transport, storage and communications	106.2	111.3	-2.5	-8.7	-2.3	-7.8
I. Other private business n.e.c	29.4	30.0	-1.4	8.8	-4.8	29.2
2. Trust Funds and NPOs	18.0	18.0	-1.0	-0.9	-5.4	-5.2
3. Personal	294.0	285.0	-7.8	13.0	-2.6	4.6
4. Others	16.4	15.6	-0.1	-4.0	-0.6	-25.7
5. Investment in Security & Shares of Private Sector	158.0	153.2	7.5	15.6	4.7	10.2

Source: State Bank of Pakistan

The downward revision of the interest rate, rise in working capital requirement, along with the expansion in fixed investment and trade financing has contributed towards the revival of private sector business. Working capital loans gathered momentum from October 2012 onwards, with seasonal demand from textile, rice and sugar processing industries. Large part of working capital loans were used to overcome the energy shortages in the industrial sector as well as expansion in cement sectors. As on March, 31 2013, banks provided Rs. 172.4 billion working facility to the companies under the category of small loans, whereas Rs. 1136.7 billion was borrowed under the category of "others". Similarly the sectors, such as manufacturing, textile, electricity, gas and water supply, construction, and trade and commerce sectors have also witnessed a growth in working capital loans.

In flow terms credit expansion to private business stood at Rs. 165.1 billion during July-March, 2012-13, as compared to Rs. 42.9 billion recorded in the same period last year. The growth in all the major sectors registered an increase when compared to last year. The manufacturing sector availed 88 percent of private sector loans (Rs.145.5 billion), followed by textile (45.4 percent or Rs. 74.9 billion), agriculture (8.7 percent or Rs. 14.3 billion), mining and quarrying (3.6 percent or Rs. 5.9 billion).

Fig: 5.4- Consumer Financing (Rs. Billion)

Description	July-March(flows)		Growth (%)	
	2011-12	2012-13	2011-12	2012-13
Consumer Financing	-8.5	8.5	-3.9	4.2
1) For house building	-5.2	-2.4	-10.9	-5.7
2) For transport i.e. purchase of car	-5.6	2.3	-11.0	5.1
3) Credit cards	-1.7	-1.9	-7.0	-8.2
4) Consumers durable	0.1	-0.1	37.1	-40.3
5) Personal loans	2.7	10.2	3.0	11.5
6) Other	1.2	0.4	27.0	7.0

Source: State Bank of Pakistan

Consumer loans registered a modest growth during July-March, 2012-13, as it stood at 4.2 percent against the negative growth of 3.9 percent recorded in the same period last year. The decline in consumer financing during the last four years was mainly due to the increase in policy interest rate by the SBP.

Expansion of loans has been witnessed in auto and personal loans, as it stood at 5.1 percent and 11.5 percent respectively. The disbursement of personal loans increased significantly during July-March, 2012-13, as it was amounted to Rs. 10.2 billion against Rs. 2.7 billion recorded in the comparable period last year. The rise in personal loans was mainly after one public sector bank doubled the limit of its advance salary loan scheme, from Rs. 0.5 million to Rs. 1.0 million in September, 2012.

Table-5.5 Targets and Actual Disbursement of Agriculture Loans

Name Of Banks	Target		Flows July-March	
	2011-12	**2012-13**	**2011-12**	**2012-13**
5 Big Comm. Banks	141.0	153.5	107.6	123.7
ZTBL	70.1	72.0	37.8	38.0
DPBs	54.1	66.7	37.3	51.0
PPCBL	7.6	9.0	6.0	5.4
MFBs	12.2	13.8	8.5	13.0
Total	285.0	315.0	197.4	231.0

Source: State Bank of Pakistan

In agriculture, overall credit disbursement amounted to Rs. 231.0 billion during July-March, 2012-13 against the target of Rs. 315.0 billion as compared to the disbursement of Rs. 197.4 billion against the target of Rs. 285.0 billion during the same period last year, posted a growth of 17 percent year on year basis. Whereas five major commercial banks disbursed Rs. 123.7 billion against Rs. 107.6 billion disbursed during the corresponding period last year showing a growth of 15 percent.

Monetary Assets

The components of monetary assets (M2) consist of currency in circulation, demand deposit, time deposit and resident's foreign currency.

Currency in Circulation

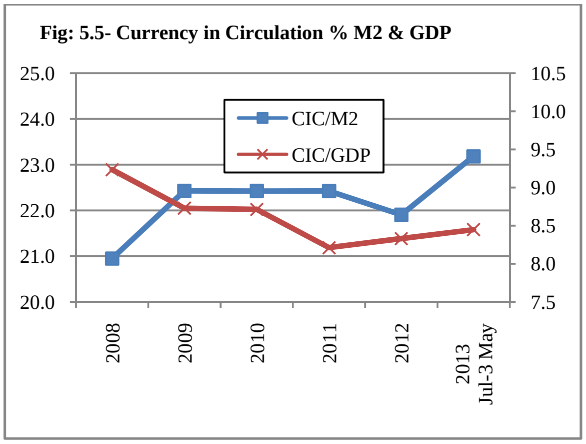
During July-3 May, 2013 currency in circulation (CIC) in flow terms amounted to Rs. 261.5 billion as compared to Rs. 170.5 billion in the same period of fiscal year 2011-12. Similarly, the currency in circulation (CIC) as percent of money supply (M2) has increased to 23.2 percent as against 23.0 percent during the period under review. YoY growth in currency in circulation has registered a significant increase of 15.6 percent. The rise in CIC is mainly due to higher cash demand geared up by relatively stronger growth in agriculture sector and higher cash transfers through Benazir Income Support Program (BISP).

Table-5.6 Monetary Aggregates (Rs. Million)

Items	**End June**		**July-3May**	
	2011	**2012**	**2011-12**	**2012-13**
A. Currency in Circulation	1,501,409	1,673,746	1,671,894	1,935,248
Deposit of which:				
B. Other Deposits with SBP	10,145	8,899	12,031	10,738
C. Total Demand &Time Deposits incl. RFCDs	5,183,640	5,959,150	5,592,433	6,401,614
of which RFCDs	374,945	440,130	412,240	505,960
Monetary Assets Stock (M2) A+B+C	6,695,194	7,641,795	7,276,358	8,347,600
Memorandum Items				
Currency/Money Ratio	22.4	21.9	23.0	23.2
Other Deposits/Money ratio	0.2	0.1	0.2	0.1
Total Deposits/Money ratio	77.4	78.0	76.9	76.7
RFCD/Money ratio	5.6	5.8	5.7	6.1
Income Velocity of Money	2.9	2.9	2.7	2.7

Source: State Bank of Pakistan

Broad money (M2) grew by 9.2 percent during July -3rd May, 2013 as compared to an increase of 8.7 percent in the same period last year. The increase in money supply came from the increase in currency in circulation and deposit money.



During July-3rd May, 2013 demand and time deposits stood at Rs. 442.5 billion against Rs. 409.0 billion during the same period last year. The year on year growth in overall deposits at 7.4 percent was due to an increase in demand deposits. It appears that SBP's policy decision of May 2012 to increase the minimum payable rate on saving deposits from 5 to 6 percent appears to have played its role in this increase. Similarly the increase in Residents foreign currency deposits (RFCDs) to Rs. 65.8 billion as compared to Rs. 37.3 billion in the same period last year have also contributed to overall deposit growth.

Monetary Management

Rising trend in government borrowing for budgetary support due to weak fiscal position and less than expected external financing during 2012-13 posed significant challenges for monetary management. However the SBP has followed a cautious policy stance over the years keeping in view lower than targeted growth in tax revenues, risks to inflationary outlook on account of faster growth in reserve money, inability of banks to reduce their costs of operations, low growth in national savings and investment and irregular trend in international prices of oil.

In order to meet the rising liquidity demand due to high government borrowings from the banks, SBP increased its liquidity injections during 2012-13. In the present scenario this act was necessary to evade the liquidity shortage through base money creation in the absence of strong financial inflows. The outstanding net injections through Open Market Operations (OMOs) increased to Rs. 510.0 billion at the end of March, 2013 from a meager Rs. 80 billion at the end of fiscal year 2011-12. However, net injections are continuously on decline as it reached to Rs. 250.7 billion at the end of April, 2013. This implies that government borrowing is on gradual decline.

The SBP mopped up Rs. 146.5 billion during July-March 2012-13 against the injections of Rs. 19,821.1 billion (Table: 5.7) whereas in the comparable period of last year absorption of Rs. 27 billion against the injections of Rs. 9,357.4 billion has taken place.

Table :- 5.7 Summary of OMO's **(Rs. billion)**

	Injections		Absorptions	
	2011-12	2012-13	2011-12	2012-13
July	408.5	1,058.6	-	-
August	640.4	2,090.1	-	-
September	1,025.1	2,095.6	-	-
October	1,058.7	2,505.1	-	-
November	1,381.5	2,633.2	-	-
December	1,418.9	2,404.4	24.0	39.5
January	969.2	2,480.2	-	107.0
February	1,244.4	2,231.6	-	-
March	1,210.9	2,322.5	3.0	-
Total	**9,357.4**	**19,821.1**	**27.0**	**146.5**

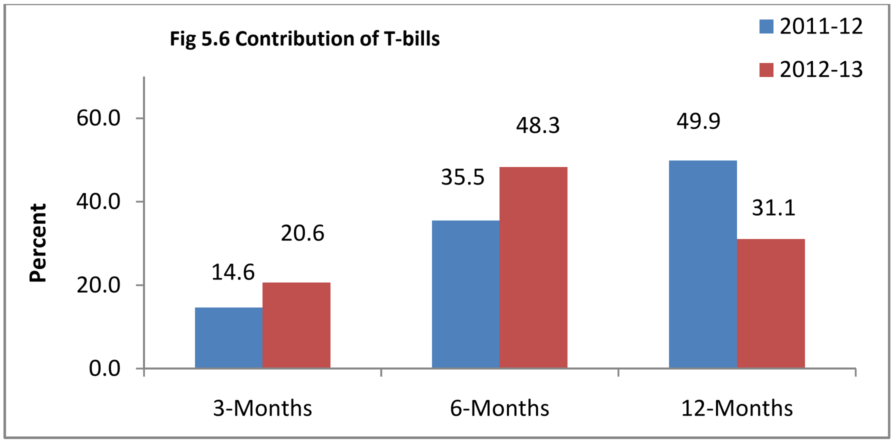
Source: State Bank of Pakistan

Most of the government borrowings consist of T-bills having maturity of one year or less. The rise in short term debt is due to the increase in roll over requirement by reducing the average tenor of overall government debt securities. SBP accepted Rs. 4,253.5 billion from the primary market of T-bills during July-March, 2012-13 as compared to Rs. 2,486.2 billion during the same period of fiscal year 2011-12. The market offered the total amount of Rs. 6,509.5 billion during July-March, 2012-13 against the offer of Rs. 4,258.9 billion in the same period last year. During the first nine months of current fiscal year, 6-months T-bills accounted for 48.3 percent of total accepted amount followed by 31.1 percent in 12 months.

Table 5.8 Market Treasury bills Auctions (Rs. Million)

	July-June			July-March					
	FY2011-12			Offered		Accepted		W.A.Rate*	
	Offered	Accepted	W.A Rate*	2011-12	2012-13	2011-12	2012-13	2011-12	2012-13
3-Months	1,658,923	1,114,157	12.5	671,490	1,266,989	363,478	878,175	12.5	10.5
6-Months	1,719,456	1,058,185	12.7	1,501,433	3,147,453	883,012	2,053,367	12.7	10.5
12-Months	2,154,137	1,283,676	12.8	2,086,003	2,095,012	1,239,758	1,321,928	12.8	10.6
Total	**5,532,516**	**3,456,018**		**4,258,926**	**6,509,454**	**2,486,248**	**4,253,470**		

Source: State Bank of Pakistan
Average of maximum and minimum rates



During the current fiscal year, the borrowers typically prefer raising long term debt whereas the government rather focused more on short term debt. SBP mopped up Rs. 191.0 billion during July-March, 2012-13 against Rs. 159.2 billion in the same period of last year.

Table-5.9 Pakistan Investment Bonds Auctions (Rs. Million)

	July-June			July-March				W.A Rate	
	Offered	Accepted	W.A Rate	Offered		Accepted			
PIBs	2011-2012			2011-12	2012-13	2011-12	2012-13	2011-12	2012-13
3 Years	98,271	72,207	12.8	74,171	206,729	50,607	82,224	12.8	11.4
5 Years	74,798	55,897	12.8	57,277	128,227	41,938	64,362	12.6	11.9
10 Years	149,418	92,049	12.8	108,032	118,349	64,370	39,239	12.8	12.4
15 Years	2,446	2,262	13.5	2,446	0.	2,262	0	13.5	0
20 Years	4,890	3,680	13.3	200	6,211	0	5,197	0	13.4
30 Years	210	0	0	210	0	0	0	0	0
Total	**330,033**	**226,095**	-	**242,336**	**459,516**	**159,177**	**191,023**	-	-

Source: State Bank of Pakistan

Market offered a total amount of Rs. 459.5 billion during the first nine months of 2012-13 as compared to Rs. 242.3 billion in the same period last year. Heavy investment was occurred in 3 years PIBs which constituted 43 percent of the total accepted amount.

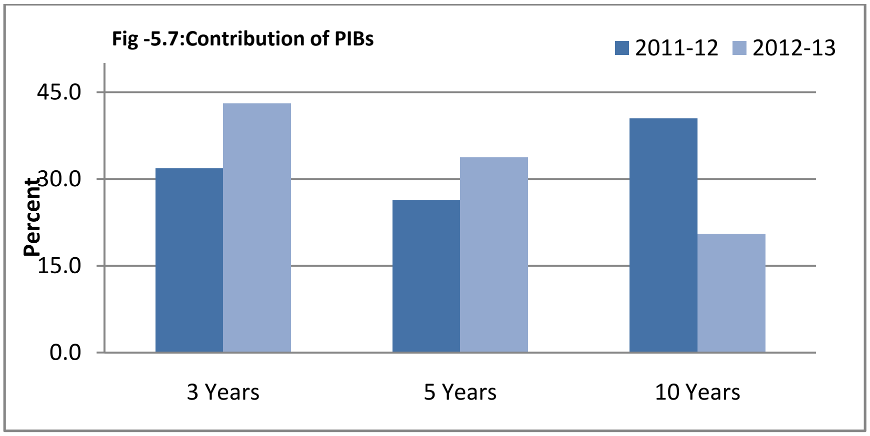
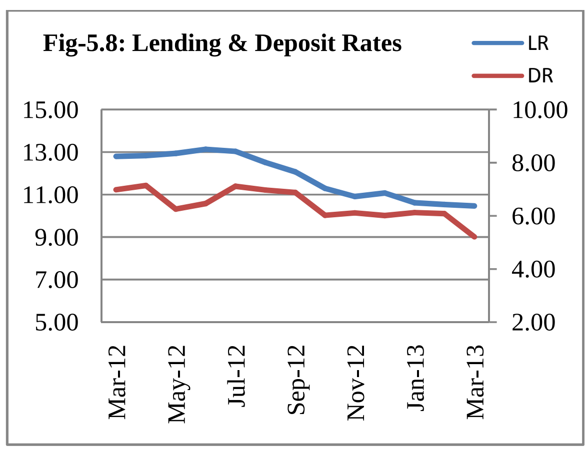


Table-5.10 Lending & Deposit Rates(W.A)	LR	DR	Spread
Mar-12	12.80	6.98	5.82
Apr-12	12.83	7.14	5.69
May-12	12.94	6.25	6.69
Jun-12	13.13	6.46	6.67
Jul-12	13.03	7.11	5.92
Aug-12	12.51	6.97	5.54
Sep-12	12.07	6.88	5.19
Oct-12	11.29	6.02	5.27
Nov-12	10.91	6.11	4.8
Dec-12	11.07	6.01	5.06
Jan-13	10.61	6.12	4.49
Feb-13	10.53	6.08	4.45
Mar-13	10.46	5.21	5.25

During the current fiscal year, following a decline policy rate by 250 bps points, weighted average lending rates of commercial banks also reduced by 267 bps points to 10.5 percent by March, 2013 against 13.1 percent in June, 2012.

Weighted average lending rate (including zero mark-up) on outstanding loans stood at 10.46percent, while weighted average deposit rate (including zero mark-up) stood at 5.21percent.The lending rates have declined since July, 2012 onwards owing to easy monetary policy stance. Banks have also cut the deposit rates from its peak level of 7.11percent in July, 2012 to 5.21percent in March 2013, in order to avoid fall in their profits.

A declining trend has been witnessed in the banking spread, as it reduced to 4.45 percent in February, 2013, while it rose to 5.25 percent in March, 2013. Lending rate is expected to reduce further owing to low level of investment and fresh disbursements by the banks. On the other hand, deposit rate is likely to increase from April, 2013 onwards, because the banks will start paying interest on average balance of saving accounts instead of minimum as per directives issued by the SBP.



Pakistan's Financial Sector

The effective implementation of monetary policy is consistent with well-organized financial system which is crucial for the appropriate functioning of the transmission mechanism. Deep and stable financial system exerts a powerful impact on economic development, poverty alleviation and economic stability. Moreover it also ensures that the central bank's policy rates are effectively transmitted to the financing conditions of households and firms and affect their saving and investment decisions. Recent global financial crisis has highlighted the importance of a resilient financial infrastructure for financial stability. It has led to a discussion about the role of the central banks and regulators, particularly ensuring stable systems for large-value financial transactions.

Pakistan financial system remained resilient against the back drop of global economic downturn due to less developed financial institutions and markets when compared with other emerging countries in Asia and around the world. Despite a substantial growth in the financial sector over the years, less exposure (lack of depth) (**Box-II**) implies that much of the financing needs cannot be met and still there is huge potential to grow with an aim to play its consequential role in the economic development of the country.

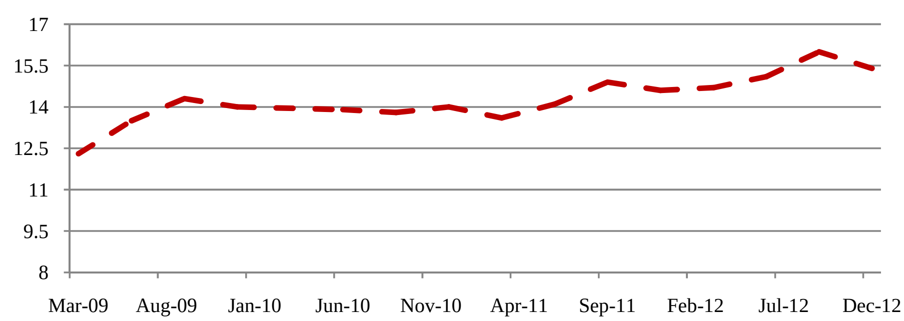
Table- 5.11: Highlights of the Pakistan's Banking System (Rs. Billion)

	CY07	CY08	CY09	CY10	CY11	Mar-12	Jun-12	Sep-12	Dec-12
Total Assets	5,172	5,628	6,516	7117	8171	8,386	8,653	9,109	9,761
Investments (net)	1,276	1,087	1,737	2157	3055	3,188	3,275	3,769	4,009
Advances (net)	2,688	3,173	3,240	3358	3429	3,429	3,573	3,549	3,760
Deposits	3,854	4,218	4,786	5451	6244	6,315	6,803	6,744	7,301
Equity	544	563	660	695	784	787	808	855	882
Profit Before Tax (ytd*)	107	63	81	105	170	48	99	142	187
Profit After Tax (ytd)	73	43	54	65	112	31	64	92	121
Non-Performing Loans	218	359	446	556	592	609	635	617	607
Non-Performing Loans (net)	30	109	134	185	182	192	214	185	171
Capital Adequacy Ratio (all banks)	12.3	12.2	14.0	13.9	15.1	14.7	15.1	16.0	15.4

Source: State Bank of Pakistan, *: year to date

The asset base of the banking system and its key elements posted a strong growth particularly in terms of deposit base. During December, CY12, assets of the banking system grew by 19.5 percent year on year basis to reach Rs. 9.8 trillion. Total assets have grown primarily because of investments in government papers. Deposits increased by 16.9 percent year on year basis, on the back of significant inflows of workers' remittances.

Fig-5.9: Capital Adequacy Ratio (percent)



Capital adequacy ratio (CAR) can also be used to test the strength of the banking system as it ensures that banks are strong enough to meet the credit, market and operational risks. In December, 2012 capital adequacy ratio (CAR) dropped by 0.6 percentage points and stood at 15.4percent against 16percent in September 2012. Non Performing Loans (NPLs) continue to grow as it reached to Rs. 607 billion in December, 2012 as compared to Rs. 592 billion in CY11largely due to security situation, energy shortage and slowdown in macroeconomic situation. However, during the fourth quarter of CY12 witnessed a decline after reaching at Rs. 635 billion in June 2012.

Box: 2
Financial development

Financial depth approximated by M2-to-GDP ratio is considered to be the most comprehensive measure as M2 as a proxy for the size of the financial sector includes not only credit to private sector, but also credit to government as well as bank assets other than credit. A rising M2/GDP ratio specifies that in nominal terms the financial assets are growing faster than the non-financial assets. As an important indicator of financial development M2/GDP has shown a declining trend in Pakistan since 2007-08, as it reduced from 44.1 percent to 38.0 percent in 2011-12. During July-3rd May 2012-13, M2/GDP ratio has increased to 36.4 percent as compared to 36.2 percent during the same period last year. Low financial depth reflects the need for more structural reforms in addition to the one implemented earlier in order to achieve potential level for sustained economic development.

Years	M2/GDP
2006-07	44.0
2007-08	44.1
2008-09	38.9
2009-10	38.9
2010-11	36.6
2011-12	38.0
July-3 May, 2012-13	
2011-12	36.2
2012-13	36.4

Islamic Banking

Islamic banking industry (IBI) in Pakistan witnessed significant growth due to local demand for Shariah complaint financial services.

Table 5.12 Islamic Banks (Rs. Billion)

	CY05	CY06	CY07	CY08	CY09	CY10	CY11	Dec 12*
Assets of the Islamic banks	71.5	119.3	205.9	276.0	366.3	475.1	641.0	836.5
Deposits of the Islamic Banks	49.9	83.7	147.4	201.6	282.6	390.1	521.0	706.5
Share in Banks Assets	1.95%	2.79%	3.98%	4.90%	5.60%	6.70%	7.80%	8.60%
Share in Bank Deposits	1.75%	2.62%	3.82%	4.78%	5.90%	7.20%	8.40%	9.70%

Source: Islamic Banking Department, State Bank of Pakistan
*: Provisional data

The assets and deposits of the Islamic banking industry grew by 30.5 percent and 35.6 percent (YoY) respectively. Asset base of Islamic banking Industry reached to Rs. 836.5 billion by end December, 2012 from Rs. 641 billion in 2011 while deposits reached to Rs. 706.5 billion against Rs. 521 billion in the same period last year. The share in bank assets increased to 8.60 percent at the end of 2012 as compared to 7.80 during the same period last year whereas share of deposits increased by 9.70 percent as against the share of 8.40 percent recorded in 2011. On the other hand profit of Islamic banking industry remained Rs. 10 billion during the last quarter of CY2012. As a positive development, both Non Performing Finances (NPFs) to financing ratio as well as Net non performing assets to total capital ratio witnessed decline during the last quarter of 2012.

Two major components of assets i.e investment and financing, registered positive growth during the last quarter of CY12 though growth in financing was higher than the growth in investment.

Table 5.12 (a) Financing Products by Islamic banks (%age)

Mode of Financing	CY06	CY07	CY08	CY09	CY10	CY11	CY12
Murabaha	48.4	44.5	36.5	36.5	40.8	43.8	39.7
Ijara	29.7	24	22.1	15.1	8.9	10.4	9.2
Musharaka	0.8	1.6	2.1	3.4	1.9	2.4	0.8
Mudaraba		0.3	0.2	0.4	0.2	0.1	0.2
Diminishing Muskaraka	14.8	25.6	28.9	29.7	29.7	32.0	35.7
Salam	1.9	1.4	1.8	1.2	1.5	2.4	3.0
Istisna	1.4	1.0	2.9	6.0	6.1	4.4	7.2
Others	3.0	1.6	5.4	7.8	10.9	4.4	4.3

Source: State Bank of Pakistan

All modes of financing except Musharaka witnessed increase in the last quarter of 2012. Whereas in CY12, Murabaha continued to have the highest share in overall financing followed by Diminishing Musharaka, Ijara and Istisna.

Microfinance

Microfinance sector has been experiencing growth and making progress towards profitability despite facing various external challenges. Due to favorable market environment both existing and new investors continue to invest substantially in microfinance banks (MFBs). Growth has been witnessed in almost all areas. Lending which was adversely affected due to devastating floods in 2010-11, has now started to rise again. Another substantial development is mobile phone banking which has been adding vast, low-cost and easy-to-access distributional channels in the sector. In recognition of its effective role and sustained commitment, the State Bank of Pakistan (SBP) has earned international recognition for its regulatory role in microfinance and branchless banking.

Presently, ten privately owned MFBs are operating in Pakistan. Three out of five telecoms have ownership stakes in MFBs. Two global MFIs, ASA and BRAC are also operating in Pakistan since 2008 and now have their operations spread across the country. Recently, Advance SA & FMO has established Advance SA Microfinance Bank.

Microfinance sector (MFBs and MFIs) witnessed a 13.7 percent growth in its aggregate loan portfolio which grew by Rs.5.2 billion in the third quarter of fiscal year 2012-13, reaching to Rs.43.5 billion against a total of 2.5 million borrowers. At the close of third quarter of 2012-13, the total loan portfolio of MFBs grew by 41 percent, reaching to Rs.23.7 billion as compared to Rs.16.8 billion in the corresponding period last year. The number of borrowers served also registered a growth of 9.8 percent, increasing from 807,986 in March, 2012 to 889,986 in March, 2013. Encouragingly, the NPLs of MFBs were restricted to around 1.92 percent as of end March, 2013. The deposit growth remained impressive with a total of Rs.9.1 billion (63 percent) added to the sector’s deposit base which stood at Rs.23.6 billion as of end March, 2013 compared to Rs.14.4 billion in corresponding period last year. The progress of the industry remained satisfactory despite macroeconomic challenges facing the country. The sector was able to expand its branch/service center network to 1,970 adding 52 new business locations across the country over the last quarter.

SBP Policy Initiatives during the Year FY13

- To foster market development, State Bank of Pakistan (SBP) has established a Consultative Group on Branchless Banking, comprising of key stakeholders. The group is currently examining critical challenges and developing recommendations to overcome the identified challenges.
- To further expand access of financial services, commercial banks have been advised to improve the coverage ratio of ATMs (the number of ATMs per branch) effective from CY 2013 onwards. All banks shall add one ATM in their network against each new branch to be opened in during a calendar year. The banks having less than 1:1 ATM per branch ratio shall cover their existing gap in 5 years starting from CY 2013 @ 20% each year.
- Rozgar microfinance bank has been converted into a nation-wide microfinance bank. Its name has also been renamed as U Microfinance Bank after its acquisition by Paksitan Telecommunication Limited. Like Tameer and Waseela, the MFB also plans to launch branchless banking platform for offering financial services.
- The pionner MFB i.e. Khushhali Microfinance Bank has been acquired by UBL led consortium while Kashf Microfinance Bank is in advanced stage of acquisition by M/s. FINCA Microfinance Holding Company.
- Advans SA has been licensed, and has commenced business as a province-wide MFB. Advans SA is operating in Sindh. The MFB is sponsored by Advans Group which is a network of financial institutions providing financial services to micro and small enterprises.
- Tameer Microfinance Bank has been allowed to undertake microenterprise lending on a pilot basis. The development came after SBP allowed higher loan limits to MFBs for undertaking microenterprise lending in March, 2012 with prior approval of SBP. Other MFBs have also demonstrated interest to undertake microenterprise lending.
- In order to further facilitate micro-enterprises, the scope of SMEs credit guarantee scheme has been extended to include microfinance banks as eligible participating financial institutions (PFIs); whereby, they would be able to access the guarantee facility for extending loans from above Rs. 150,000 up to Rs. 500,000 to micro-enterprises for a tenor not exceeding 5 years.

Box-3: Program Initiatives

To complement policy measures & promote financial inclusion, SBP also undertakes implementation of government and donor funded programs. The updates on government programs and SBP market interventions are as follows:

To promote financial inclusion in the country, SBP has been implementing the DFID-funded Financial Inclusion Program (FIP) with the aim to promote inclusive growth and to improve income and livelihoods opportunities for poor and marginalized groups in Pakistan. The progress and details on account of different interventions of FIP are given below:

a) Microfinance Credit Guarantee Facility: The £10 million MCGF is a credit enhancement facility launched by SBP in December 2008 under FIP to cover partial risks against the loans extended to microfinance providers by the commercial banks. The facility has helped develop the market and introduce poor borrowers to mainstream financial institutions. So far 25 guarantees have mobilized Rs.7.075 billion from commercial bank for onward lending to around 350,000 new micro borrowers. The scope of the facility has been enhanced to mobilize non-bank financing from capital markets, further diversifying sources of financing for micro borrowers.

b) Institutional Strengthening Fund (ISF): In December 2008, SBP launched £10million ISF facility with the objective to provide grants for strengthening the institutional and human resource capacity of the microfinance providers (MFPs). Up till now, Rs.638 million have been approved for 13 MFPs which cover 20 projects addressing institutional strengthening needs of the grantee institutions for Capacity Building/ HR Training, IT development, Business Plan/ Strategic reviews, Market Research, Branchless Banking, Corporate Governance, Credit Ratings, Remittances, and Treasury functions etc.

c) Credit Guarantee Scheme for small and rural borrowers (CGS): CGS worth £10million was launched in March 2010 to facilitate credit to small and rural businesses for greater outreach. Under CGS, limits worth PKR 4.830 billion have been assigned to 12 banks for 2012 and the Guarantees of Rs. 1,231 million have been issued against sanctioned loans of Rs. 2,923 million for providing new loans of 4,861 to Agri. & Small Enterprises

d) Financial Innovation Challenge Fund (FICF): a £10 million facility that aims to foster innovations and test new markets, lower cost of delivery, enable systems and procedures to be more efficient and provide new ways of meeting the unmet demand for financial services. The first round of the Fund which was held on Government to Person (G2P) Payments has now been successfully concluded by deciding to award Rs. 505 Million to six applicant institutions. The 2nd FICF Round would be held on Rural Financial services including agricultural finance and broad based Financial Services Projects using telecommunication infrastructure to promote micro payment for people who are not part of financial services

e) Technical Assistance (TA) worth £10 million was launched for providing support to improve market Information and Infrastructure, such as

I) Support to Systemic Areas

- National Microfinance Credit Information Bureau
- Anti-Money Laundering: Strengthening of FMU’s information systems and analytical capabilities
- Pakistan Remittance Initiative (PRI)
- Third party transparency initiative for MF industry
- Strengthening Consumer protection monitoring vis-à-vis global benchmarks

II) Surveys and Assessments such as G2P payments, Islamic: KAP Survey, SME Cluster Surveys, Hybrid Value Chain financing study, Branchless Banking Survey and development plan Access to Finance survey -2, Agriculture Finance Study etc.

Lack of financial literacy has been a major constraint to enhance financial inclusion in the country. In order to address this challenge, SBP launched Pakistan's first-ever Nationwide Financial Literacy Program (NFLP) on 20th January 2012 to assist financial inclusion and poverty alleviation efforts to facilitate economic growth and stability across the country

The dissemination of the pilot program has now been completed successfully. The program focused on disseminating basic education about financial concepts, products and services to masses focusing on Budgeting, Savings, Investments, Banking Products and Services, Debt Management and Consumer Right and Responsibilities etc. As a way forward, the program will further be scaled up based on the evaluation of the pilot project to reach out to more than 500,000 poor and low income beneficiaries

Farmers Financial Literacy & Awareness Programs on Agricultural Financing, Grass-root level Training Programs for Credit/Loan Officers of Microfinance Banks/Microfinance Institutions (MFIs), and likewise SME Finance Grass Root Cluster Training Programs were arranged by SBP with the ultimate of broadening financial inclusion.

Insurance Sector

The insurance industry in Pakistan is relatively small compared to its peers in the region. The insurance penetration and density remained very modest as compared to other jurisdictions while the insurance sector remained underdeveloped relative to its potential. As of December 2011, the industry's total premium revenue stood at over Rs. 124 billion or US$1.29 billion.

The market is fairly liberalized as 100 percent foreign ownership and control of insurance companies is permitted with paid up capital requirements at US$4 million, with the condition of bringing in at least a minimum of US$2 million in foreign exchange and raising an equivalent amount from the local market. The minimum capital requirements have been increased in a phased manner, though they still remain modest by international standards, at Rs. 300 million for non-life and Rs. 500 million for life insurers.

Currently there are 39 non-life insurers operating in the market, including three general Takaful operators and one state-owned company. Approximately, 65 percent of the market share in gross written premium rests with the top three players. In the CY2011, the sector grew by 16 percent, whereas the total premium of non-life insurance sector stands at Rs. 54 billion. In addition, a government owned reinsurer continues to benefit from a mandatory minimum 35 percent share in the treaties of non-life insurers.

There are nine life insurers, including two family Takaful operators and one state-owned corporation in the life insurance sector. In CY2011, the life insurance market grew by 30 percent, whereas the total premium stood at Rs. 70 billion.

There are two dedicated health insurance companies in the market along with two foreign life insurance companies and two non-life foreign companies. The market has witnessed introduction of new products in the lines of health, crop and livestock insurance. New distribution channels such as Bancassurance, websales and Telesales are also growing rapidly.

Achievements

During the period under review, in its quest to meet its primary objectives of protecting the interests of policyholders and facilitating orderly development of the insurance industry, including takaful segment, the Insurance Division is focused in various areas which are as follows:

i. Micro insurance

SECP is working with the World Bank, under a project sponsored by the FIRST Initiative, to create an enabling environment for the provision of micro insurance in the country. Three high-level missions by the senior staff and consulting experts of the World Bank were carried out during the period under review. A diagnostic study has also been completed and published, depicting the state of micro insurance in Pakistan with the demand and supply-side analysis.

iii. Development of crop and livestock insurance

SECP has been an active member of the Presidential Task Force and working to formulate a framework on NAIS, a National Agriculture Insurance Scheme. A draft scheme has also been prepared which includes the latest estimates of cropping area, cost of production, estimated cost of premiums and various proposals on the sharing of premium subsidies by the federal and provincial governments. This scheme would be available to all farmers of the country involved in the cultivation of five major crops namely wheat, rice, sugarcane, cotton and maize and will provide coverage from sowing to harvest. It will be mandatory in nature and all farmers in the country will be automatically insured, whether they take the loan from the banks or not. Indemnity will be based on the per acre input cost estimates of Agriculture Policy Institute and the sum insured will be determined on the estimated cost of cultivation. Simultaneously, a similar task force has been formed by the State Bank of Pakistan for the development of a Livestock Loan Insurance Scheme (LLIS).

iv. Insurance industry reform committee

It is imperative to promote a robust and financially sound insurance industry to diversify the inherent systemic risk and to enhance the resilience of the financial system by increasing its outreach and penetration. To accomplish this challenging task, SECP constituted an Insurance Industry Reform Committee comprising of industry experts, professionals and members from within SECP.

vi. Insurance Companies (Sound and Prudent) Management Regulations, 2012

To safeguard the interests of stakeholders, the Commission, after the approval of SEC Policy Board notified the Insurance Companies (Sound and Prudent Management) Regulations, 2012, which are applicable to the Chief Executive Officers/Principal Officer, Directors and the relevant key officers of insurance companies. The regulations have been prepared after thorough consultation with stakeholders and insurance industry experts and are in line with the international best practices prescribed by the International Association of Insurance Supervisors (IAIS).

vii. Introduction of risk based solvency regime

In January 2012, the SEC Policy Board signaled its nod for notifying revisions in the solvency regime thereby modifying the SEC (Insurance) Rules, 2002 vide Gazette Notification SRO16(I)/2012 dated 9 January 2012. The salient features of the amendments are:

- Rationalization of admissibility limits for certain assets;
- Enhancement of Minimum Solvency Requirement for non-Life insurers and shareholders' fund for life insurers; and
- Enhancement of Statutory Fund requirement by introducing Risk Based Margin above the current policyholders' liabilities.

ix. Takaful Rules, 2012

In 2007, a Committee was tasked to review the Takaful Rules 2005. The committee focused on areas such as ensuring consistency with accounting provisions of the SEC (Insurance) Rules 2002, prescribing of percentages in respect of various modes of the Shariah complaint investments for the purpose of determining solvency, maintaining separate solvency for each Participants' Takaful Fund which will ultimately strengthen the solvency of the Waqf Pool, introduction of a comprehensive Shariah Governance Framework. In other words, the takaful operator would ensure that their operations are managed in a sound and prudent manner. In this regard, the SECP is, also, in the process of establishing a Shariah Advisory Board. One of the prominent features of the Takaful Rules 2012 is that in line with a policy decision of the GoP, the rules contain requirements for allowing conventional insurance companies to commence Takaful business through specialized "window" operation. Proposed rules shall allow conventional insurance companies to apply for permission to commence window operations enabling them to offer shariah compliant products and conventional insurance products simultaneously provided that the accounts are segregated and reported separately. The Rules were subsequently approved by the Policy Board.

x. Directions for insurance companies to combat money laundering

While taking appropriate steps to address the gaps related to the threat of money laundering in the insurance industry, SECP has issued a Directive for the Insurers on the Anti-money Laundering (AML) regime including the Customer Due Diligence/ Know Your Customer (CDD/KYC) Policies and Designation of Compliance Officers. Such regulatory directions are prescribed and implemented by Regulators globally in the financial sector so as to promote the anti-money laundering practices which helps to protect the interest of all stakeholders. The directive is applicable to all public and private sector insurers.

xi. On-line Insurance Companies Return Submission System (ICRS)

To facilitate the insurance industry for submitting the regulatory returns required under the applicable insurance laws, the Commission has introduced an online regulatory returns submission system, the Insurance Companies Return Submission (ICRS) system, which has been implemented since the beginning of July 2012 for both life and non-life insurers.

Box: 3
WAY FORWARD

- SECP is actively working with stakeholders to develop innovative solutions for the delivery of micro insurance. Certain technology-driven models have been prepared for local indigenous solutions and it is expected that with the support from international and multilateral agencies, modern intermediary models shall soon be introduced for the provision of micro insurance to the remote and rural populations.

- While the crop insurance has recently taken off in Pakistan, SECP is working to develop comprehensive guidelines for the industry enabling it to develop this product and cater to the huge demand in the market. Certain pilot projects have been designed by the stakeholders and planned to be executed during the current year, for which SECP has been providing supervisory advises.
- The Insurance Division has been encouraging the insurers to do a pilot project on health insurance in partnership with contemporary distribution channels, with emphasis on the need of creating innovative business models and leveraging the use of technology. Stakeholder dialogues have been initiated and guidelines for health insurance are also being developed in consultation with the industry.
- SECP is working to help the stakeholders for developing catastrophic insurance schemes and participated in various forums organized by the stakeholders including National Disaster Management Authority (NDMA), Pakistan Poverty Alleviation Fund (PPAF), Lead Pakistan and Climate Development Knowledge Network (CDKN), etc. A national level scheme is in the process of development for which SECP is committed to provide full support.
- Under the provisions of the SECP Act 1997, the SECP is considering to form the Shariah Advisory Board. The members of the Board shall comprise of, other regulatory surveyors, renowned Islamic scholars, with expertise in the fields of accounting, law and the insurance industry. The primary goal of the Board will be to ensure compliance of regulated entities with the Islamic covenants such as portfolio purification, selection of investment & product design, monitoring and management of strategies and ensuring compliance to Islamic guidelines.

Conclusion

Pakistan's financial sector continued to grow and remained vibrant during the global financial crisis. However internal factors were more dominating in affecting the macroeconomic environment of the country particularly less than expected external inflows and acute power shortages posed multifaceted challenges. Moreover, repayments to IMF since February 2012 onwards exerted tremendous pressure on BOP due to dwindling foreign exchange reserves at the critical level. On the other hand substantial fiscal borrowings from the banking system further jeopardized the situation as the banks were more comfortable in investing government papers rather than extending credit to the private sector. Keeping in view the macroeconomic situation of the country and declining inflationary pressures, SBP followed an accommodative policy stance since the beginning of current fiscal year in order to support the economic growth through the revival of credit to private sector. Recent estimates on monetary aggregates indicate the shift in government borrowings from the scheduled banks to the central bank, which itself is inflationary in nature. Hence there is a medium term risk to the inflation outlook, at the same time the credit to private sector is also expected to increase.