

Money, Prices & Fiscal Policy Section
Ministry of Planning, Development & Special Initiatives

**Review of
Monetary Developments**

July-June FY20

Broad money (M2) expanded by Rs. 2824.4 billion (15.87% growth) during 1st July 2019 to 26th June 2020 as compared to its expansion of Rs. 1808.5 billion (11.31%) during the corresponding period of last year.

Net Foreign Assets (NFA) of the banking system expanded by Rs. 863.8 billion during the period under review as compared to their contraction of Rs. 1,299.5 billion during the corresponding period of last year. During this period, Net Domestic Assets (NDA) of the banking system expanded by Rs. 1,960.6 billion as compared to their expansion of Rs. 3,108.1 billion during the corresponding period of last year. Currency in circulation expanded by Rs. 1,242.1 billion as compared to Rs. 583.4 billion during the corresponding period last year. Provisional data on monetary aggregates is given in the table below:

Overview

(During 01-07-2019 to 26-06-2020)

- Broad money expanded by 15.87% as compared to its expansion of 11.31% during the corresponding period of last year.
- NFA expanded by 0.06% as compared to its contraction of 0.6% during the corresponding period of last year.
- NDA expanded by 10.16% as compared to its expansion of 19.18% during the corresponding period of last year.
- Credit to private sector increased by Rs. 186.4 billion as compared to an increase of Rs. 681 billion during last year.
- For budgetary financing, government net borrowing from SBP was Rs. 37 billion as against retirement of RS. 301.4 billion up to May 2020. The borrowing from scheduled

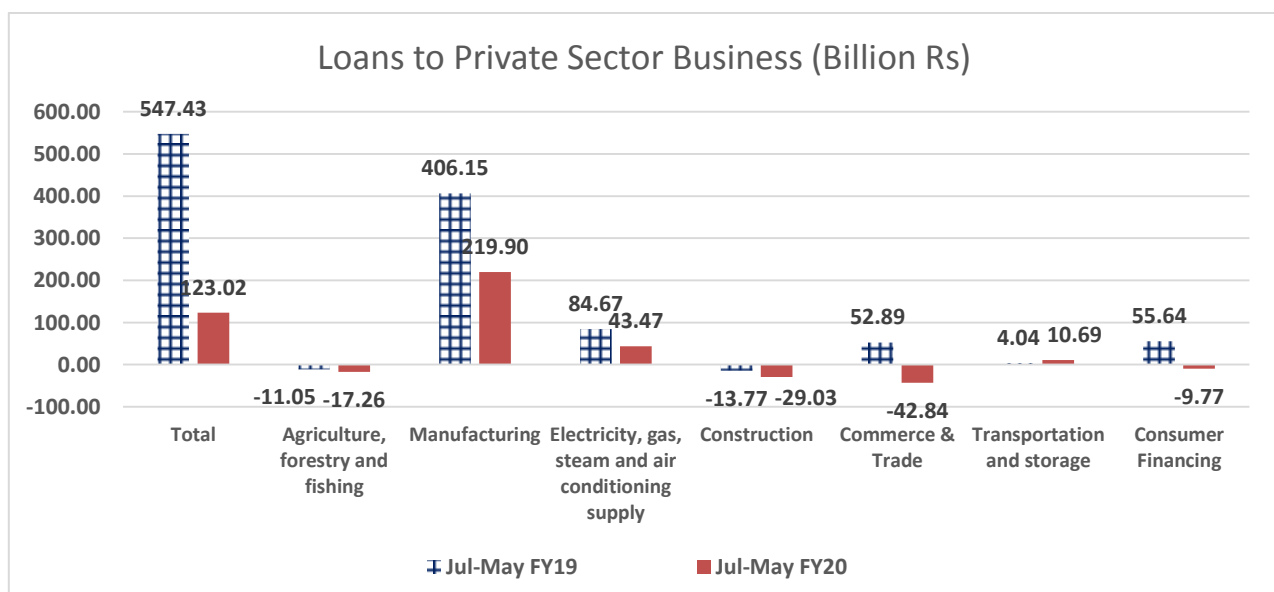
Monetary Aggregates (Rs Billion)			
Factors Affecting Broad Money (M2) Growth	Stocks at End Jun-19	Monetary Impact since 1st July to	
		26-Jun-20	28-Jun-19
A. Net Foreign Assets of the Banking System	-1,507.1	863.8	-1,299.5
<i>Growth</i>		<i>-0.06</i>	<i>0.6</i>
B. Net Domestic Assets of the Banking System (1+2+3)	19,305.6	1,960.6	3,108.1
<i>Growth</i>		<i>10.16%</i>	<i>19.18%</i>
1. Net Government Sector Borrowing (a+b+c)	12,336.7	2,448.8	2,213.3
a. Borrowings for Budgetary Support	11,596.5	2,400.9	2,279.8
i. From SBP	6,691.9	37.0	3,156.6
ii. From Scheduled Banks	4,904.6	2,363.9	-876.8
b. Commodity Operations	756.4	44.3	-63.3
c. Others	-16.2	3.6	-3.2
2. Credit to Non-Government Sector (a+b+c+d)	8,072.8	306.3	1012.9
a. Credit to Private Sector	6,666.5	186.4	681.0
b. Credit to Public Sector Enterprises (PSEs)	1,394.2	117.5	329.7
c. PSE Special Account-Debt Repayment with SBP	-24.2	0	0
d. Credit to Non-Banking Financial Institutions (NBFIs)	36.3	2.4	2.2
3. Other Items (Net)	-1,103.9	-794.5	-118.1
Broad Money (M2) (A+B)	17,798.5	2824.4	1808.5
<i>Growth</i>		<i>15.87%</i>	<i>11.31%</i>

Analysis of Factors Affecting Broad Money (M2)

Liquidity in the banking system is generated by changes in NFA and NDA. The expansion in NFA of the banking system indicates improvement in external sector as current account deficit stood at US\$ 3.3 billion during Jul-May FY20 as compared to US\$ 12.4 billion during last year.

NDA of the banking system consists broadly of (i) government sector borrowings, (ii) credit to non-government sector, and (iii) other items. Under these heads, an expansion was registered for government sector borrowings and credit to non-government sector; while there was contraction in other items. For budgetary support, net government sector borrowings from the banking system stood at Rs. 2400.9 billion. Government borrowed Rs. 37 billion from SBP and Rs. 2363.9 billion scheduled banks. Last year, government borrowed Rs. 3156.6 billion from SBP and retired Rs. 876.8 billion to commercial banks. During July-May, government retired Rs. 301.4 billion to SBP. It means that during June government borrowed Rs. 338.4 billion from SBP Rs. 438.0 billion and Rs. 129 billion from commercial banks. Borrowing from SBP was because of financing of COVID-19 relief packages and to bridge the financing gap due to lower revenue collection.

Under commodity operations, government borrowed Rs. 44.3 billion from the banking system as compared to retirement of Rs. 63.3 billion during the corresponding period of last year. However, during June 20, government retired Rs. 22.0 billion as outstanding stock decreased to RS. 44 billion from Rs. 64.0 billion. Pace of credit to Private sector remained slow due to high policy rate before COVID-19 and after COVID-19 due to slow down in economic activities despite of reducing policy rate from 13.25% to 7.0%. The expansion in private credit squeezed during June when compared with last month as the credit expansion up to end of May, 20 was Rs. 288.0 billion whereas during June, 20 it was Rs. 186.4 billion. Within credit to private sector, private sector businesses during Jul-May FY20 borrowed Rs. 123.02 billion as compared to their borrowing of Rs. 547.43 billion during the same period of last year. Sector-wise loans are shown in the following graph.



During this period, credit to Public Sector Enterprises (PSEs) expanded by Rs. 117.5 billion as compared its expansion of Rs. 329.7 billion. Credit provision to Non-Banking Financial Institutions (NBFIs) increased by Rs. 2.4 billion as compared to last year's credit of Rs. 2.2 billion.

Conclusion

During the year 2019-20, money supply recorded a better growth as compared to last year due to expansion in Net Foreign Assets (NFA) of the Banking System which is attributed to improvement in external account. On the other hand, Net Domestic Assets (NDA) of the banking system registered low growth due to low credit and intake by non-Government Sector. Within NDA, Government borrowing of budgetary support and commodity operations remained the dominating factors. The Government relied on borrowing from both SBP and Commercial Banks. It is important to mention here that up to May, 2020 government was opting policy of zero borrowing from SBP as agreed with IMF, thereby borrowed from Commercial Banks, however, during June 20 it borrowed Rs 338.4 billion from SBP, thus become net borrower of Rs 37.0 billion instead of net retiring of Rs. 301.4 billion.

commodity operations borrowing during July-May 20 stood at Rs. 64.34 billion as compared to retirement of Rs. 60.17 billion mainly due to net borrowing for procurement of wheat (Rs. 58.2 b) and sugar (Rs. 8.5 b) billion during July-May, FY 2020.

In case of private sector credit, there was comparatively less expansion which also owes to deterioration of manufacturing sector growth and decline of economic and business activities as well as the lagged impact of earlier higher policy rate and pandemic COVID-19.

The Monetary Policy Committee (MPC) decided to reduce the policy rate by 100 basis points to 7 percent. This decision reflected the MPC's view to boost economic activities to mitigate the effect of COVID-19. The inflation outlook has also improved which at end June registered and increase of 10.74%. It implies a negative real interest rates, at least in the short run. It will keep borrowers on gain side while lenders will be losers in real terms. So there is need to divert cheap funds towards real investment ends. On the other hand, decreasing the policy rate exerts pressure on exchange rate as low interest rates discourage portfolio investors and they seek other destinations for higher returns. During June outflow of foreign portfolio investment was US\$ 43.2 million. Capital flight may get further momentum in uncertain circumstances as the ones originated by the pandemic. It is therefore expected that the central bank may keep existing policy rate intact during next meeting of MPC to increase economic activities.

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