DAWN

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Private-sector lending: a tricky business

Between July 1, 2019 and Jan 10, 2020, banks' net fresh lending to the private sector slumped to Rs138 billion — or less than one-third of Rs495.6bn lent in the year-ago period — according to the State Bank of Pakistan (SBP).

Why are banks not lending to the private sector? More importantly, can they actually accelerate lending in the remaining part of the fiscal year?

Despite a big decline in the GDP growth rate from 5.5 per cent in 2017-18 to 3.3pc in 2018-19, banks' private-sector lending remained robust, falling to just Rs693bn from Rs775bn. During this fiscal year, it seems that Pakistan is again headed towards an even lower growth rate — 2.4pc, according to the projection by the International Monetary Fund (IMF).

Unlike in the past fiscal year, banks' private-sector lending has also plunged. Can banks start lending aggressively now if, for the argument's sake, they choose to do so?

The SME sector has huge credit demand and tapping it at a time when the overall private-sector appetite is low makes sense

The recently created Pakistan Corporate Restructuring Company (PCRC) may help revive sick industrial units through the restructuring of their overdue bank loans and that, in turn, may create room for banks to lend more to the private sector. Ten commercial banks — HBL, NBP, UBL, MCB Bank, ABL, Meezan Bank, Bank Alfalah, Bank Al Habib, Habib Metropolitan Bank and Faysal Bank — that have jointly set up the company are the biggest lenders of the private sector and the government.

One reason for the banks' low lending to the private sector is that bad loans have recently ballooned and the loan infection ratio has shot up. Banks certainly need to take care of this issue before they can improve private-sector lending.

Borrowing from banks

	By the private sector	By the government
2014-15	Rs223.8bn	Rs1.323tr
2015-16	Rs460.6bn	Rs1.278tr
2016-17	Rs747.9bn	Rs179.4bn
2017-18	Rs775.5bn	Minus Rs152.4bn
2018-19	Rs693.5bn	Minus Rs874.6bn

Source: SBP

Credit and economic growth

	Net lending to private sector	GDP growth
2014-15	Rs223.8bn	Rs1.323tr
2015-16	Rs460.6bn	Rs1.278tr
2016-17	Rs747.9bn	Rs179.4bn
2017-18	Rs775.5bn	Minus Rs152.4bn
2018-19	Rs693.5bn	Minus Rs874.6bn

Source: SBP

The volume of non-performing loans or NPLs swelled to Rs758bn in September 2019 from about Rs637bn in September 2018, showing an increase of Rs121bn or 19pc in a year, according to the SBP. This situation is attributable primarily to the ballooning of bad loans of sugar and energy sectors, though the problem persisted across all sectors. Large-scale manufacturing is still in recession. Its output is down about 6pc year-on-year in the first five months of this fiscal year on top of a 3.4pc slump seen in the last fiscal year. This leaves little hope for boosting private-sector credit through higher corporate lending, which seems too difficult for banks because of the increase in the corporate loan infection ratio from 8pc in September 2018 to 9pc in September 2019.

The silver lining is in the small and medium enterprises (SME) sector, although its loan infection ratio is quite high — 18pc to be exact. But it is not the rise. The ratio was a bit higher — 18.4pc a year earlier. But the problem with our banks is that they don't seem willing to increase exposure to the SME sector. As of September last year, lending to SMEs was still 5.5pc of total advances. Some 3.2 million SMEs are contributing 30pc to GDP, employ more than 80pc of non-agricultural workforce and account for one-fourth of our export earnings. Do they deserve this treatment? Should their share in the total pie of bank advances remain 5.5pc?

The SBP must goad banks into boosting their lending to the SME sector. The SME sector has huge unmet credit demand and tapping it at a time when the overall private-sector credit appetite is low makes sense.

The low appetite for private-sector credit is undeniable but so is the fact that banks have long become concentrating this credit in corporate and consumer sectors. Hoping for an increased credit appetite in the consumer sector during this fiscal year is unwise amidst sliding growth in GDP and growing unemployment.

Two powerful drivers of consumer finance — house building and automobile industries — are already in deep trouble. In fact, in the first half of this fiscal year, the off-take of auto loans has seen no growth while loans for house building rather declined by Rs2.7bn on a year-on-year basis.

Banks continue to lend to the agriculture sector, but one must remember that agricultural lending is done mostly against last-year recovery. That is why, in spite of hundreds of billions worth of agricultural loans in a year, its impact on overall private-sector credit off-take remains minimal. Flows of private-sector credit cannot be thickened much even if banks lend more aggressively to the agriculture sector in traditional ways. But if they reach out to new loan seekers in agriculture and lend to them or if they lend to existing borrowers more than the recoveries made during a year, only then higher agricultural lending can enhance the overall private-sector credit flow, making some impact on economic growth as well.

But why on earth will banks come out of their comfort zone and make efforts to boost private-sector credit? They will not do this unless government borrowing from banks is reduced. Under immense fiscal pressure and in order to reduce the stock of its borrowing from the central bank, the government is borrowing heavily from commercial banks these days. And the trend cannot be reversed anytime soon.