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Private sector credit drops 53pc to Rs265bln in July-May

KARACHI: Private sector credit sharply fell 53.3 percent to Rs265 billion in almost 11 months as high interest rates made funds largely unattractive amid downside risks to growth, the central bank's data showed on Monday.

The State Bank of Pakistan's (SBP) data showed that banks lent Rs567 billion to private businesses from July 1, 2019 to May 15, 2020. Analysts said the demand for bank financing, such as working capital loans and fixed investment loans, remained low due to decade-high interest rate, which only recently moved down to stimulate economy upended by the lockdown after the coronavirus outbreak. "The growth of the private sector credit remained slow, pointing to weakness in the economy even before the economic impact of the coronavirus pandemic," an analyst said. The central bank has significantly cut the borrowing costs to help the economy withstand the coronavirus crisis and taken measures to support liquidity and credit conditions since the beginning of the crisis. Lockdown went into the effect in the last week of March. The SBP slashed the policy rates cumulatively by 525 basis points to 8 percent and expanded refinancing schemes, announcing new facilities to support employment and allowing banks to defer loan repayments for one year.

"Recent monetary easing measures seem to have little impact so far on credit growth that requires further rate cuts in future," an analyst said, requesting anonymity. "The easing cycle is likely to be nearing its end."

The economic fallout from the COVID-19 is expected to increase the level of bad loans in banks' balance sheets, given that businesses have scaled down their activities, despite the easing of lockdown restrictions in the country. Furthermore, in the worst case scenario many small and medium-sized firms would be forced to close or to struggle to repay their debts.

"Banks may have the highest exposure to credit risk from the aviation, tourism, oil and gas exploration and the textile sectors in the coming months," said an analyst. "However, the appetite for the bank credit can emerge from the construction sector owing to the support package provided by the government to this sector." Economic growth is expected to contract 1.5 percent this fiscal year before recovering to around 2 percent over the next fiscal. Since the start of this fiscal year, many big and small firms and households were reluctant to borrow due to weak demand and high interest rates. This trend was also linked to subdued industrial production and decline in imports. Large scale manufacturing saw a steep fall of 23 percent year-on-year in March. The SBP said the successive policy rate cuts and sizeable cheap loans provided through the SBP's enhanced refinancing facilities have helped maintain credit flows, bolster the cash flow of borrowers, and support asset prices. "This has contained the tightening of financial conditions that would otherwise have amplified the initial necessary contraction in activity," it said in the latest monetary policy statement.