

**Coronavirus challenge, SBP responds prudently**

- cuts policy rate by only 75 basis points to 12.50pc
- offers manufacturing sector Rs100bn package in response to anticipated slowdown
- will also refinance banks to provide Rs5bn to health sector

KARACHI: State Bank of Pakistan has cut the key policy rate by 75 basis points and announced two special financing schemes to address the economic and health challenges posed by the spread of coronavirus (COVID-19).

Talking to newsmen after a meeting of Monetary Policy Committee (MPC) on Tuesday at SBP head office, Governor State Bank Dr Reza Baqir said the Committee has decided to cut policy rate by 75 basis points to 12.50 percent. In reaching this decision, the MPC considered key trends and prospects in the real, external and fiscal sectors, and the resulting outlook for monetary conditions and inflation, he added.

The MPC has also emphasized that it stood ready to take further actions, if and when needed as more information becomes available on the outlook for inflation and growth. "We are closely monitoring the entire local and international developments and the SBP will take whatever additional actions that may be necessary to safeguard price and financial stability and for support of economic growth", he said.

In addition to its decision on interest rates by MPC, SBP has announced two special financing schemes. 'Temporary Economic Refinancing Facility (TERF)' will be for businesses to provide important additional support to investment in response to the anticipated slowdown in activity due to the coronavirus pandemic. Secondly, 'Refinance Facility for Combating COVID-19 (RFCC)' will provide cheap financing to hospitals and medical centers for combating the spread of COVID-19.

As per earlier SBP announcement, the governor's press briefing was not scheduled, however, in the wake of recent development due to COVID-19, the governor SBP Dr Reza Baqir decided to have an interaction with media to talk about the recent economic developments.

Governor SBP said the dominant development since the last MPC meeting has been the outbreak of the coronavirus pandemic and this has precipitated a slowdown in the world demand and volatility in global financial markets, as well as a steep fall in global oil prices.

"Together with the domestic deceleration in food prices and a significant decline in consumer price expectations, the outlook for inflation in Pakistan has therefore improved, paving the way for today's rate cut," he mentioned.

He mentioned that the current market volatility being experienced in Pakistan is externally driven and the strengthening in the fundamentals of Pakistan's economy that drove the improvement in Pakistan markets before the Coronavirus outbreak remains intact. As a result, volatility is likely to subside as global risk aversion reduces, he added.

“The overall situation in the wake of COVID-19 is still uncertain and SBP also remained vigilant. This is the first steps not the last and SBP will take more actions and steps, whenever required to support the economy,” he said.

In order to encourage the investors for investment in the country, the SBP has launched ‘Temporary Economic Refinance Facility (TERF)’ and its Shariah compliant version to stimulate new investment in manufacturing.

The Governor SBP said he believed that this scheme will help counter any possible delays in the setting up of new projects that investors were planning prior to the coronavirus outbreak. It will be available for one year only, requiring a letter of credit (LC) to be opened by end-March 2021.

Under this scheme, the SBP will refinance banks to provide financing at a maximum end-user rate of 7 percent for 10 years for setting up of new industrial units. The total size of the scheme is Rs 100 billion, with a maximum loan size per project of Rs 5 billion, he added.

Dr Baqir said the TERF can be accessed by all manufacturing industries, with the exception of the power sector, where an SBP refinance facility for renewable energy projects already exists. In line with the SBP’s other refinancing schemes, the credit risk will be borne by banks and the selection of projects to finance will also be determined by them.

In addition, the Governor SBP also announced a ‘Refinance Facility for Combating COVID-19 (RFCC)’ and its Shariah-compliant version to support hospitals and medical centers in combating the spread of COVID-19.

Under this scheme, the SBP will refinance banks to provide financing at a maximum end-user rate of 3 percent for 5 years for the purchase of equipment to detect, contain and treat the coronavirus, he added.

The SBP will provide this facility to banks at 0 percent. All hospitals and medical centers registered with federal or provincial health agencies and which are engaged in the control and eradication of COVID-19 will be eligible for this facility.

The total size of the scheme is Rs 5 billion, with a maximum financing limit per hospital or medical center of Rs 200 million. This scheme will help contain the spread of coronavirus and reduce its human toll. It is available until end-September 2020.

The Governor SBP said the decision reflected the MPC’s view that the outlook for inflation has improved in light of the recent deceleration in domestic food prices, a significant decline in consumer price expectations, a sharp fall in global oil prices, and a slowdown in external and domestic demand due to the coronavirus pandemic.

Average headline inflation is expected to remain within the SBP’s 11-12 percent forecast in FY20, before falling to the medium-term target range of 5-7 somewhat earlier than previously forecast, he added.

He said before coronavirus, Pakistan’s economy was moving in right direction with some improvement on external account and exchange rate, while Pakistan’s foreign exchange reserves were also surged to a reasonable level.

“Our fundamentals are still strong, however, coronavirus may hit the country’s exports, imports,” he added. On other side, the recent fall in oil prices followed by Coronavirus will help to further reduce the pressure on external account, he mentioned.

Talking about the outflow of 'hot' money, Dr Baqir said that foreign investors worldwide taking precautionary measures and as safety measures they are investing in dollar instead of other instruments as dollar appears to be the most safe investment.

He said that massive investment in government securities has provided sufficient support to the country's foreign exchange reserves in that time, when our reserves were in single digit.

Notwithstanding recent volatility in foreign exchange markets, the SBP's FX reserves have maintained strong growth, driven by the narrowing current account deficit. Pakistan's foreign exchange reserves have increased by \$5.48 billion from \$7.28 billion at end-June 2019 to \$12.76 billion as of end of February 2020.

The actual improvement in the country's external position is much larger, given the sizeable reduction in SBP's forward liabilities of \$ 5.20 billion during the same period. This increase in the net reserve buffers of SBP of \$ 10.68 billion is more than sufficient to cope with any portfolio outflows in an orderly manner, he said.

He said that SBP continues to monitor developments carefully and stands ready to respond effectively to address any disorderly market conditions.

Replying to a question relating to the rate cut, he said that each central bank takes a rate cut decision based on its country's economic situation. "We should realize the difference in emerging markets and developed markets. We can't compare [Pakistan] with the US; they print dollar and we Pak rupee," he added.

Governor SBP said that SBP is also in touch with bank and may take some measures, if bank borrowers will face difficulties in repayment of due to recent economic developments.

Reuters adds: "Since this disease has spread, it has started impacting our economy," said the bank's governor Reza Baqir.

Pakistan's earlier projection of 3.5% growth this year was now likely to slide. "Now we think that it will be around 3%," he said.

The bank has held the 13.25% interest rates steady since July, when it paused after a series of hikes as data started showing the inflation rate stabilising, which lately registered a decline.

The business community said it was expecting a higher cut. However, the central bank governor said Pakistan's economic fundamental would remain strong enough to respond to reforms undertaken before the virus spread.

With sinking foreign reserves and a large current account deficit, Pakistan struck an agreement in April with the IMF for a \$6 billion three-year rescue package.