

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

**Review of
Monetary Developments (M2)**

July-June FY20-21

Introduction

M2 is the measure of money supply in an economy. It plays an important role in forecasting issues like inflation which in turn affects the economy in general, in terms of consumer spending and business etc. Volume of money supply or liquidity in the banking system is generated by changes in Net Foreign Assets (NFA) and Net Domestic Assets (NDA). NFA shows whether a country is a creditor or debtor nation by measuring its external assets and liabilities. In other words, it depicts cumulative change in its current account balance. NDA of the banking system consists broadly of (i) government sector borrowings, (ii) credit to non-government sector, and (iii) other items.

Provisional data on monetary aggregates is given in the table below:

Monetary Aggregates (Rs. Billion)			
Factors Affecting Broad Money (M2) Growth	Stocks at End Jun-2020^P	Monetary Impact since 1st July to	
		25- June - 21	26-June- 20
A. Net Foreign Assets (NFA) of the Banking System	-516.153	1008.080	858.588
B. Net Domestic Assets of the Banking System (1+2+3)	21,424.1	1851.095	1942.191
1. Net Government Sector Borrowing (a+b+c)	14,547.2	1785.930	2430.701
a. Borrowings for Budgetary Support	13,748.3	1,687.006	2,382.796
i. From SBP	6,538.8	-1,268.208	37.006
ii. From Scheduled Banks	7,209.5	2,955.214	2,345.789
b. Commodity Operations	813.4	96.710	44.296
c. Others	-14.5	2.214	3.610
2. Credit to Non-Government Sector (a+b+c+d)	8,372.4	549.579	306.415
a. Credit to Private Sector	6,862.8	594.611	186.509
b. Credit to Public Sector Enterprises (PSEs)	1,490.5	-52.540	117.459
c. PSE Special Account-Debt Repayment with SBP	-24.2	0	0
d. Credit to Non-Banking Financial Institutions (NBFIs)	43.3	7.507	2.448
3. Other Items (Net)	-1,495.5	-484.414	-794.926
Broad Money (M2) (A+B)	20,908.0	2,859.175	2,800.779
<i>growth</i>		13.68%	15.74%
<i>Source: State Bank of Pakistan</i>			

Analysis of Factors Affecting Broad Money (M2)

i. Net Foreign Assets

The Broad Money supply witnessed a growth of 13.68% on account of improved NFAs of the banking sector. There has been an increase in the NFA of both central and scheduled banks where volume for the former is higher i.e. 908.171 billion as compared to Rs 99.909 billion for the latter. During this period, the NFAs mainly improved due to the inflow of the remittances of around US\$ 29.370 billion. However, the Current Account witnessed a deficit of US\$ 1852 million as compared to deficit of US\$ 4.449 billion during corresponding period of the last year.

During July to June, FY 21, the remittances stood as the main factor contributing to growth in NFA. The workers' remittances reached to US\$ 29.370 billion during Jul-June FY21 that is significantly higher than the reference period during previous year (\$23.131 billion). The Initiatives taken by the SBP to increase and facilitate the remittances through official channels, especially after the COVID outbreak have proved to be very supportive. The introduction of 'Roshan Pakistan Digital Account' has facilitated financial inflow of US\$ 1.8 billion since September, 2020. Further, SBP has encouraged the banks and exchange companies to process the higher number of remittances which include doubling the rate of reimbursement for Telegraphic Transfer (TT). The use of digital channels for sending and receiving remittances and launch of 'M-Wallet Scheme' and 'Asaan Remittance Account' that is attributed to continuous efforts by Government and SBP to attract inflows through official channel, limited cross border travel amid second wave of COVID-19 and flexible exchange rate regime.

Highlights (During 01-07-2020 to June, 2021)

- Broad money expanded by 13.68% as compared to its expansion of 15.74% during the corresponding period of last year.
- Net Foreign Assets (NFA) of the banking system expanded by Rs. 1,008.080 billion during the period under review as compared to their expansion of Rs. 858.588 billion during the corresponding period of last year.
- NDA expanded by Rs. 1851.095 billion as compared to its expansion of Rs. 1942.191 billion during the corresponding period of last year.
- Credit to private sector extended by Rs. 594.611 billion as compared to its expansion of Rs. 186.509 billion in last year.
- The borrowing for budgetary financing by the government from SBP contracted by Rs. 1,268.208 billion (debt retirement) as compared to its expansion by Rs. 37.006 billion during reference period last year. For budgetary support, Govt. borrowed from scheduled banks to Rs. 2,955.214 billion as compared to Rs. 2,345.789 billion borrowed last year in the same period.

ii. Net Domestic Assets

The expansion was also registered in NDA where government sector borrowings, credit to non-government sector and other items observed an increase. For budgetary support, net government sector borrowings from the banking system stood at Rs1,785. 930 billion during July- June FY21. Government retired Rs. 1,268.208 billion to SBP and borrowed Rs. 2,955.214 billion from scheduled banks. Last year, during this period government net borrowing was Rs 2,430.701 billion where Government borrowed Rs 37.006 billion from SBP and Rs. 2,345.789 billion from commercial banks. Under commodity operations, government borrowed 96.710 billion from the banking system as compared to the borrowing of Rs. 44.296 billion during the corresponding period of last year.

Credit to private sector expanded by Rs. 594.611 billion during July-June FY21 compared to last year expansion of Rs. 306.415 billion. Due to accommodative monetary policy stance, the private sector credit expanded and the same is expected to grow during FY22 (SBP, July 21). An outlook of Stock of Loans to Private Sector Business during June 2020 and June 2021 and their variation are shown in the following table:

CREDIT/LOANS CLASSIFIED BY BORROWERS

S.No	Description	Rs. In Million		
		June-20	June-21	Difference
	PRIVATE SECTOR (BUSINESS)	5,271,037	5,712,430	441,393
1.	Agriculture, forestry and fishing	280,216	292,274	12,058
2.	Mining and quarrying	82,989	67,175	-15,814
3.	Manufacturing	3,290,273	3,548,472	258,199
4.	Electricity, gas, steam and air conditioning supply	491,843	558,695	66,852
5.	Construction	129,561	154,443	24,882
6.	Wholesale and retail trade; ...	429,343	452,581	23,238
7.	Transportation and storage	119,607	113,666	-5,941
8.	Information and communication	159,242	185,367	26,125
9.	Real estate activities	29,439	30,892	1,453

Loans to Mining and Quarrying and Transport and Storage declined during the reference period whereas for the rest of the sectors loans increased, especially a significant increase can be observed for manufacturing and Electricity, gas, steam and air conditioning supply.

Credit to public sector Enterprises (PSEs) contracted by around Rs.52.540 billion during July-June, 2021 as compared to its expansion of Rs.117.459 billion for the same period. during the last year. A significant increase in credit provision to Non-Banking Financial Institutions (NBFIs) has been observed. It increased by Rs.7.507 billion as compared to last year's credit expansion of Rs.2.448 billion.

Conclusion

The growth 13.68 % in Broad Money has been recorded during July - June 2021. The growth owes to the expansion in Net Foreign Assets (NFA) of the banking system by Rs. 1008.080 billion during the period under review. The NDA also recorded an expansion of Rs.1851.095 billion during the reference period, compared to the expansion of Rs. 1942.191 during the reference period last year.

SBP has announced to maintain the policy rate at 7 % in the backdrop of the domestic recovery, improved inflation outlook following the recent decline in food prices and core inflation. The consideration has also been given to the uncertainty arising out of the fourth wave of the pandemic. The latest MPC expects the policy rate to remain unchanged in the near future and any change in the stance will be gradual depending on the demand led pressure on inflation or current account vulnerabilities.

Inflation declined from 11.1 percent (y/y) in April to 9.7 percent in June 2021. Food prices declined in June (month on month basis) owing to the administrative measures taken by the government and import of wheat and sugar. According to SBP, this trend confirms the supply side nature of inflation. The key risks for upward trends in inflation include the resurgence of pandemic, higher than expected global prices, domestic energy tariffs and fiscal slippages.

The accommodative monetary policy stance has proven to be supportive in the wake of uncertain situation arising out of the pandemic. The business confidence is high coupled with credit expansion to the private sector. The current monetary policy stance may be supported in the wake of continued domestic recovery with a gradual and measured resumption towards normalization.
