



AJ

Home (https://www.thenews.com.pk/)
> Today's Paper (https://www.thenews.com.pk/today)
> Opinion (https://www.thenews.com.pk/print/category/opinion)

Abdul Jalil
(https://www.thenews.com.pk/writer/abdul-
jalil)

Autonomy for the SBP

March 25, 2021



(https://www.thenews.com.pk/print/809347-
u=https://www.thenews.com.pk/%2Fprint%2F809347-

for-the

the-SBP

sbp)

for-autonomy-

the-for-

sbp)

In a significant move, the federal cabinet approved amendments in the State Bank of Pakistan (SBP) Act in the name of central bank autonomy, accountability and price

stability.

(https://www.thenews.com.pk/%2Fprint%2F809347-

If parliament approves these amendments, the SBP will hold more sway to target inflation. In line with global practices, the SBP will have to shift to flexible inflation targeting (FIT). Price stability becomes the overriding objective of monetary policy. The enactment of the SBP Amendment Act is an important milestone in this regard.

Earlier, the SBP was working under the 1956 law 'to regulate the monetary and credit system of Pakistan and to foster its growth in the best national interest with a view to securing monetary stability and fuller utilisation of the country's productive resources'. That is, there was no clarity on the exact role of the SBP pertaining to inflation, credit, employment or economic growth.

The SBP Act will assign the task of price stability and inflation targeting to the SBP. Though it would only be possible to fathom the breadth and width of the amendments after it gets approval of parliament, an educated guess based upon media reports reveals that price stability would be the SBP's primary function while financial stability and support for economic policies will be its secondary and tertiary objectives, respectively.

In order for the SBP to meet these ends, the grant of unprecedented autonomy is in the offing for its banking operations. The move would take the edge off the role of the Ministry of Finance and the government as it entails the abolishment of the Monetary and Fiscal Policies Coordination Board (MFPCEB) to minimize the "risk of undue political influence over the SBP's monetary policy." The MFPCEB show is predominantly run by the finance minister and there is no denying the fact that the ministry plays a defining role in connection with the implementation of the monetary and exchange rate policy. In the wake of the recent developments, the SBP will have the freedom to determine and implement the monetary and exchange rate policy. Nevertheless, the SBP shall be consulted ex-ante on any proposed legislative act related to the Bank.

Furthermore, the SBP shall not extend any direct credits to or guarantee any obligation of the government, or government-owned entity or any other public entity. Earlier, the government borrowed from the SBP to meet fiscal expenses. Besides this, the SBP will abolish the Rural Credit Fund, the Industrial Credit Fund, the Export Credit Fund, the Loans Credit Fund and the Housing Credit Fund. This implies that the SBP will not fund quasi-fiscal operations and economic growth related activities. However, the SBP will provide

refinance facility only to financial institutions, and can provide short-term facility to a troubled commercial bank, provided the federal government acts as a guarantor for the sanction of such a loan.

The governor of the SBP (the governor) shall be appointed by the president of Pakistan for five years with a likelihood of a one-term extension; the federal government will appoint the deputy governors. The external members of the Monetary Policy Committee (MPC) will be appointed by the federal government on the recommendation of the SBP board. Members of parliament or a provincial assembly and members of a political party cannot be members of the SBP board or the MPC. Importantly, the government cannot remove the governor or deputy governor except in certain given scenarios.

An 'executive committee' of the SBP will be set up under the governor and with the deputy governor and executive directors of the SBP. The executive committee will decide any 'residual matter' that has not been explicitly addressed by the new law. The governor shall submit the annual report before parliament regarding the achievement of the SBP's objectives, the conduct of the monetary policy, the state of the economy and the financial system.

There are three important ramifications of these amendments: first, price stability is declared as the prime objective of the SBP. This is significant keeping in view the country's history of sudden jumps in inflation. It goes without saying that inflation erodes the purchasing power of the consumers and the confidence of the investors.

Second, the government cannot directly borrow from the government. It is well documented that government borrowing is inflationary. Furthermore, government borrowing crowds out private investment and, consequently, the country's economic activities bear the brunt. Third, autonomy is given to the SBP by reducing the Ministry of Finance and the government's role. Literature postulates that central bank independence is crucial for the monetary policy's transmission mechanism for price stability.

However, this is not the first time that such autonomy has been bestowed upon the SBP. According to the website of the SBP, "Under financial sector reforms, the State Bank of Pakistan was granted autonomy in February 1994. On 21st January 1997, this autonomy was further strengthened by issuing three Amendment Ordinances..."

The devil lies in the details of how this act is implemented and for what end. If not implemented in its true spirit, then wait for more autonomy of the SBP in the future. In case it does not yield the desired results, this autonomy for the SBP may further be extended and that, no doubt, will have further repercussions for the economy. At present, we can just hold our fire and let things take their due course.

The writer is professor of economics at the Pakistan Institute of Development Economics (PIDE), Islamabad.

Latest News



Prince Harry Not Happy Over His Move To Disgrace Royal Family In Oprah Tell-all

(<https://www.thenews.com.pk/latest/828430-prince-harry-not-happy-over-his-move-to-disgrace-royal-family-in-oprah-tell-all>)

(<https://www.thenews.com.pk/latest/828430-prince-harry-not-happy-over-his-move-to-disgrace-royal-family-in-oprah-tell-all>)



Justin Bieber's Comeback Tour Pushed Back To 2022

(<https://www.thenews.com.pk/latest/828429-comeback-tour-have-been-pushed-back-to>)

(<https://www.thenews.com.pk/latest/828429-comeback-tour-have-been-pushed-back-to>)