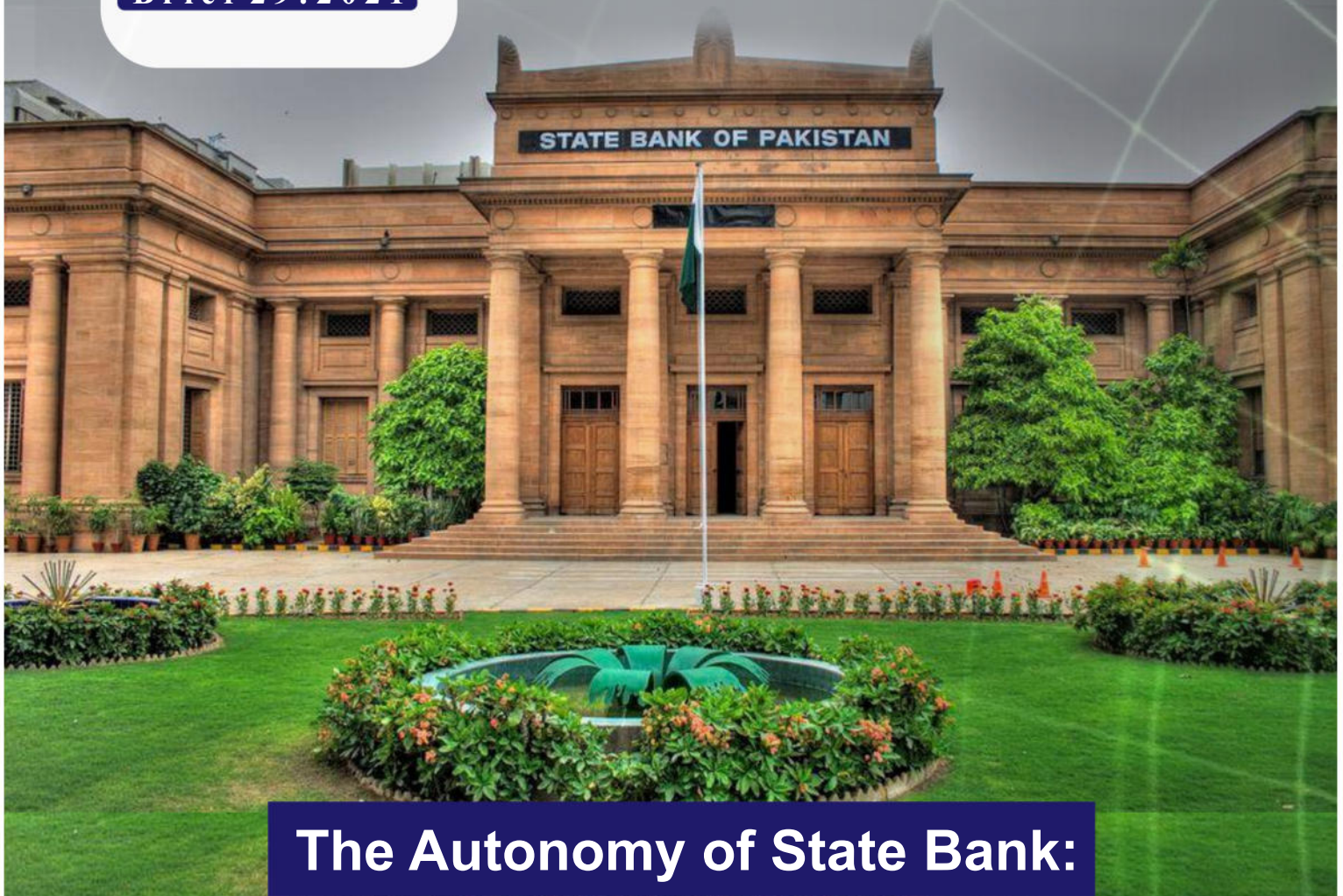


  
**Webinar**  
Brief 29:2021



## The Autonomy of State Bank:

### A Fresh Look at Central Bank Independence



**Pakistan Institute of  
Development Economics**



PIDE WEBINAR ON

# PAKISTAN DAY

MARCH 23 - START ARM  
PART-1

## THE AUTONOMY FOR SBP: A FRESH LOOK AT CENTRAL BANK INDEPENDENCE

In a significant move, the federal cabinet approved amendments in the State Bank of Pakistan (SBP) Act in the name of central bank autonomy, price stability and accountability. The benefit of central bank independence is well documented in the literature. However, there is a dire need to evaluate several important questions:

- Why is autonomy so important? Should every institution be autonomous?
- Is Pakistan is prepared for the complete autonomy of the central bank?
- Can only SBP manage inflation given the constraints of the supply side and governance?
- What will be the implications for economic growth?
- What will be the implications for financial stability?
- How will the institution be accountable?

### SPEAKERS



**Riaz Riaduddin**  
Former Deputy Governor,  
State Bank of Pakistan



**Syed Salim Raza**  
Banker, Financier and  
Former Governor of  
State Bank of Pakistan.



**Dr Salman Shah**  
Advisor to the CM of  
Punjab on Economic  
Affairs and Planning  
& Development



**Dr Pervez Tahir**  
Former Chief Economist  
Planning Commission  
Government of Pakistan

### MODERATOR

**Dr Nadeem ul Haque**  
VC, PIDE



PIDE Islamabad



PIDEpk



PIDEpk



PIDE Official



PIDE Islamabad



# Part-I

## Setting the stage

The Moderator of the webinar Dr. Nadeem ul Haque opened the floor for debate with his views about IMF programs to Pakistan that we have had an IMF program every five years which indicates that we have outsourced our policy to foreign donors. But the IMF has been experimenting with our economy diverting its program focus from one failure to another that is from emphasizing the opening up of capital account to closing it down and from targeting the policy rate to SBP independence. Unfortunately our policymakers and economic intellectuals don't talk about it. Neither Ministry of Finance nor the SBP economists have any say in framing policy so our economic policies have been leased out to the IMF.

Dr. Nadeem ul Haq stressed that Pakistan is not a high inflation country but IMF has made it extremely inflation abuzz. There has been 20% inflation only twice in our whole history and the average inflation rate is 10 %. It is not that high. A brief review of empirical evidence across the world shows that inflation convergence is happening across countries. However, long-term growth is on a declining trend, and investment in Pakistan is also declining. Currently in Pakistan there are three objectives on macro policy fore-front: Growth, Inflation, and Balance of Payments. But growth is hardly taken that much seriously as the hullabaloo about inflation.

Sharing a recently published article "The role of IMF conditionality on Central Bank Independence" Dr. Nadeem argued that IMF has motives to stress in promoting Central Bank independence (CBI). The motive of IMF in stressing the promotion of Central Bank Independence is to insulate the Central Bank from political interference and shield loan disbursement from government abuse.

## Key Messages

### What is central bank Independence?

It refers to the freedom of monetary policymakers in the conduct of money monetary policy, free of any political interference. There are so many indicators and indexes used for measuring Central Bank Independence; a few more important and more widely used indicators are GMT (1991) and CWM (1992) these are the two most widely used indexes in Literature.

Empirical evidence shows that:

- Central Bank Independence doesn't have a significant negative impact on inflation.
- No relationship between Central Bank Independence and growth exists. Most recent literature shows that there is a negative relationship between Central Bank independence in economic growth in the long run in the advanced countries.
- Central Bank Independence leads to adopting policies that increase inequality.
- What is new in the new SBP bill?

SBP Act 1956 doesn't clarify the primary objective whether it is stabilization or fostering economic growth or regulating the monetary and credit system of Pakistan. According to the proposed bill Central bank's primary objective is to achieve domestic price stability and to regulate the monetary and credit system of the country. The secondary objective is the stability of the financial system of the country and the tertiary objective is supporting the economic policies of the Government of Pakistan without undermining the primary and secondary objectives.

The actual draft of the proposed bill is not publicly available for debate yet following are some points that are known to be recommended for amendment in the bill:

- To abolish the Monetary and Fiscal Policies Coordination Board proposed to eliminate the meddling of the Ministry of Finance in central bank matters.
- To abolish Rural Credit Fund, Industrial Credit Fund, Export Credit Fund, And Loan Credit Fund, SBP shall not extend any direct credit or guarantee any obligation to the government of Pakistan.
- SBP Governor shall be appointed by the President of Pakistan for five years and his term can be extended for another five years.
- Government cannot remove the Governor or Deputy Governor.
- The executive committee of SBP shall be set up under the Governor, Deputy Governor, and executive directors to oversee the residual matters that the proposed action doesn't cover.

## **Why is autonomy so important? Should every institution be autonomous?**

SBP autonomy is a welcome development as it brings with it more responsibility to SBP. Also, this move is the one long over-due to insulate SBP from political interference. But the important thing to bear in mind is that SBP isn't getting goal independence. The independence it is getting is only for utilizing all the available instruments for the conduct of its policy. Institutional designs in Pakistan need to be redefined. First, we need to look at SBP's institutional design. What is it meant for? Is it appropriate to meet the goals that it is supposed to serve? It is very essential to pin-down the ultimate objective and function of SBP. Targets need to be defined by the national economic committee or Parliament. Only then provide independence. Independence should include the ultimate autonomy in using all the available instruments without any clash among other institutions of the economy. Next comes the idea of, after using all the requisite instruments, financial independence to achieve these goals.

## **Can only SBP manage inflation given the constraints of the supply side and governance?**

All the mania about inflation in Pakistan is directionless. Inflation targeting and not just price stability should be the objective. Although Inflation targeting has nothing to do with autonomy, it is just one of many instruments of monetary policy. Most of the countries around the world have chosen a range for inflation targeting rather than targeting a number. For example, India has chosen a range between (3%-7%). So we need to choose a range like 4-9 % and set a target period as well, say two years, for monitoring the progress and over time monitor it with data from market and SBP statements.

Supply-side factors like energy imports and BOP fluctuations should not be reacted to while targeting inflation because these are transient factors.

## **Is Pakistan prepared for the complete autonomy of the central bank?**

SBP autonomy is the first and not the final thing. Just like SBP, all other economic institutions need to be revitalized. The whole system of economic governance needs up-gradation to perform well within the defined perimeter. In a system that is already inefficient and crumbling down if we only focus on one particular institution and ignore the rest, it will only perpetuate inefficiency and institutional disparity. For example accountability of SBP is hinged on parliament but in the case of a dysfunctional parliament, parliamentary accountability seems not like a viable option.

The autonomy of SBP is inevitable. But autonomy should not come at the cost of transparency. There should be more transparency in the whole process of bringing in autonomy. Another reservation is that there is a tendency of concentration of power in the institutions and the notion of performance is tied to that power like we have an extremely powerful institution that delivers at best. If SBP is going to get this kind of power and autonomy then there are more chances of clash of institutions than coordination.



## **What will be the implications for economic growth?**

In the current scheme of things, SBP has a focus on long-term growth as well as price stability. The macroeconomic analysis has a direct focus on all the long-term indicators including growth. So the argument that inflation targeting or price stability objective will get the growth on the back burner doesn't make much sense. Notwithstanding, framing the growth policy is not the domain of SBP and we cannot blame SBP for the neglect of other institutions of their job.

Having said that, experts believe that it will be before time to foretell any growth implications as the actual provisions of the proposed bill are not available for debate yet.

Opponents of the amendment argue that there is a clash of interest among institutions and different tiers of govt. when it comes to price stability. Central Bank alone cannot singlehandedly control or stabilize prices as only core Inflation falls in the domain of SBP, administering prices is the subject of the Federal government and similarly, another pricing is done by the provinces. So in this state of affairs, whether there is autonomy or not, SBP cannot stabilize prices.

## **How will the institution be accountable?**

There is no performance evaluation as per the current provisions of law. The Governor of the central bank is appointed by the President of Pakistan. He's dismissed by the President. There is no observation in the current law about his performance evaluation. Making price stability as the primary objective has put SBP in a tough place to perform. Because now SBP will have to effectively communicate if it fails to do so. The old blame game and finger-pointing at the Ministry of Finance are not going to help. The door to all the quasi-fiscal items will be completely closed and SBP will have to do all the important public communication. With greater autonomy, there will be higher accountability of the governor of SBP. The current law has put SBP in a better place to perform than ever before.

## **Conclusion**

SBP autonomy is an important development but it should not bring any institutional disparity in the system. Economic growth is a more critical issue than SBP autonomy but unfortunately, this issue is not being discussed much as we are seeing almost all the vital indicators on a downward trajectory.

## PIDE WEBINAR

**FRIDAY, MARCH 26 - START 3PM**

# The Autonomy for SBP: A Fresh Look at Central Bank Independence

## PART - II

In a significant move, the federal cabinet approved amendments in the State Bank of Pakistan (SBP) Act in the name of central bank autonomy, price stability and accountability. The benefit of central bank independence is well documented in the literature. However, there is a dire need to evaluate several important questions:

- Why is autonomy so important? Should every institution be autonomous?
- Is Pakistan is prepared for the complete autonomy of the central bank?
- Can only SBP manage inflation given the constraints of the supply side and governance?
- What will be the implications for economic growth?
- What will be the implications for financial stability?
- How will the institution be accountable?

## SPEAKERS



**Dr. Hafiz A Pasha**  
Renowned Economist  
and Former Federal  
Minister for Finance,  
Government of Pakistan



**Dr. Shahida Wizarat**  
Chairperson, Aam Awam  
Takmeele Pakistan, &  
President, IEPP



**Dr. M. Khawaja**  
Senior Research  
Economist, PIDE



**Dr. Atiq ur Rehman**  
Associate Professor,  
Director, KIE,  
University of Azad  
Jammu and Kashmir

## MODERATOR

**Dr Nadeem ul Haque**  
VC, PIDE



PIDE Islamabad



PIDEpk



PIDEpk



PIDE Official



PIDE Islamabad



# Part-1I

## Key Messages

- Dr. Nadeem ul Haq opened the floor for debate inviting Dr. Shahida. According to her viewpoint, institutional autonomy is not a good thing for countries that are still in the colonial mode because of this way we are bringing in foreign dictation and agendas. The provision regarding the legislation for SBP makes it mandatory for the government to consult with SBP for any legislation regarding SBP, and SBP is going to act upon IMF's advice. This is a dangerous provision because SBP will be taking advice from the IMF directly. Another reservation is that there are going to be hefty salaries for Governor and Deputy Governor but no mention of penalties for underperforming staff. Similarly, the provision that makes SBP immune from NAB and FBI jurisdiction is one of the so many serious reservations. Dr. Shahida concludes that the SBP act will have very grave implications for Pakistan's economic, social political and strategic environments.
- Talking about the concept of Central Bank Independence and how this concept came into life one of the speakers mentioned that the concept dates back to the 1970s and early 1980s when developed countries were facing higher inflation due to the oil crisis so they came up with this notion of Central Bank Independence and inflation targeting. Most of those developed countries had per capita incomes, at that time, that were much higher than today's Pakistan's level of per capita income. Definitely one thing to be noted is that there was some threshold level of economic development and growth before those countries at that time could afford to exclusively focus on inflation.
- The proponents of Central Bank Independence are of the view that we need autonomy for all the Institutions of Pakistan economy so we have to start somewhere. But the thing is that SBP autonomy is not a bad thing at all until it doesn't create an imbalance of power among various institutions. Some provisions are very questionable for example accountability mechanism is not straightforwardly given while the staff is being given immunities is questionable.
- There was a question among the speakers among the participants of the debate that what would Central Bank do if there is some kind of accident or exceptional circumstances for example if there is some nuclear disaster or if there is some kind of natural calamity and in that scenario, the government needs borrowing and according to the constitutional provisions and according to the SBP act government cannot borrow from Central Bank or the commercial banks then what Central Bank can do to help the government or what will be the way forward with SBP? The proponents of Central Bank autonomy are of the view that in any such case Central Bank can violate these provisions because the exceptions are always there as in the past so in the future.
- Those in favor of Central Bank autonomy are of the view that the current scheme of things doesn't suggest the central bank is going to be accountable to none Central banks around the world are autonomous but that doesn't make them unaccountable.
- Autonomy and Independence are the instruments of social and economic development and cannot be enforced over-night. It only happens overtime after the economy has developed but in the case of Pakistan giving autonomy to the Central Bank of Pakistan only is just like putting the horse before the cart.
- The political independence of bureaucracy is more important than the constitutional independence of the State Bank. SBP is already autonomous in so many operational matters for example SBP is fully autonomous in interest rate determination as time and again it is proved that SBP has maintained a high interest rate despite the opposition from the Ministry of Finance.

- Resultant governance structure and institutional design after autonomy are important and it is the only thing that matters. Until the original draft law comes out, nothing could be said with certainty.
- Will autonomy boost financial stability or not? One of the speakers argued that the Central Bank on purpose supports larger banks and companies than smaller ones because they affect the Indexes and rankings so SBP can kill, at will, smaller banks and companies and supports bigger capitalists. Banks are the major components of market capitalization. When the interest rate goes up it is good for banks. So the practice is that no one is concerned about financial stability.
- One argument presented was that Independence is a culture it brings with it transparency and openness as well but it seems that SBP is not ready for openness and transparency right now because SBP has a culture of confidentiality in practice. In this environment of uncertainty and ambiguity, SBP should have come forward to provide some clarification on the burning debates about autonomy and its implications but it seems that it wants to keep it confidential and close to its chest.
- SBP autonomy is considered to break the begging bowl of government because when the channel from which easy money is going to the government is broken only then is it possible to force govt. to focus on its revenue targets and spurring growth.

### Conclusion

The conclusion of this webinar like the previous one was the same: autonomy is not a bad thing there should be greater autonomy, not for only one institution but the autonomy should be given to all the Institutions on equal footing so that there would be no disparity. There should be greater autonomy not only for SBP but for all the independent entities like universities, Planning Commission, all the regulatory authorities, and other key economic institutions. Another conclusion is that autonomy and Independence are a question of institutional architecture as well. There could be two possible implications of SPB autonomy the one is with greater SBP autonomy interest rate might shot up real internal rate will also follow the suit but with increased interest rate the economy will have to go through very troubled waters as it will experience a very painful adjustment and our government is rushing into this painful adjustment without considering its repercussions. The second implication could be that there will be only de jure autonomy and no de-facto autonomy like it was earlier done in the past. Whatever happens, remains to see but one thing is certain that Pakistan's economy cannot fare well with any such disparate autonomy.



## PIDE WEBINAR

TUESDAY, MARCH 30- START 7PM

# The Autonomy for SBP: A Fresh Look at Central Bank Independence

## PART - III

In a significant move, the federal cabinet approved amendments in the State Bank of Pakistan (SBP) Act in the name of central bank autonomy, price stability and accountability. The benefit of central bank independence is well documented in the literature. However, there is a dire need to evaluate several important questions:

- Why is autonomy so important? Should every institution be autonomous?
- Is Pakistan is prepared for the complete autonomy of the central bank?
- Can only SBP manage inflation given the constraints of the supply side and governance?
- What will be the implications for economic growth?
- What will be the implications for financial stability?
- How will the institution be accountable?

## SPEAKERS



**Muhammad Yaqub**  
Former Governor of the State  
Bank of Pakistan



**Shahid Hafeez Kardar**  
Former Provincial Finance  
Minister and Former  
Governor of the State  
Bank of Pakistan

## MODERATOR

**Nadeem ul Haque**  
VC, PIDE



PIDE Islamabad



PIDEpk



PIDEpk



PIDE Official



PIDE Islamabad

# Part-III

## • **Mr. Muhammad Yaqoob standpoint on the Autonomy of SBP**

M. Yaqoob started by presenting a brief account of the history of SBP autonomy. He divided the subject of autonomy into three categories:

1. Administrative autonomy
2. Regulatory autonomy
3. Monetary policy autonomy

Before 1993, SBP was completely subservient to the Ministry of Finance administratively. The finance secretary was completely at the helm of affairs in SBP. SBP was an extension of the ministry of finance and monetary policy was the extension of fiscal policy at that time. The autonomy ordinance was drafted and passed in 1993 and Dr. Yaqoob, therefore, was one of the committee members who drafted the law. He put forth that the current law has more emphasis on the administrative autonomy of the State Bank of Pakistan for securing the tenure of functionaries. It is more akin to providing protection to individuals and granting immunities against prosecution to functionaries.

Before reforms, Pakistan Banking Council was a parallel setup run by the government to control commercial banks. In 1997, banking reforms were introduced and SBP was made the sole regulatory authority of the banking sector in Pakistan. It was authorized to issue licenses to commercial banks. The new law proposes nothing for the regulatory amendments to the State Bank of Pakistan.

In the context of monetary policy autonomy, two new articles were proposed in amended law in 1997. These articles were meant to empower SBP to make it a formulator and executor of monetary policy. The fiscal and monetary coordination board was set up and there was a provision for submission of quarterly reports to Parliament for accountability as well as for knowledge of the parliamentarians. Shedding light upon what has happened since then; Dr. Yaqoob maintained that the government has been borrowing massively from the State Bank of Pakistan while on the other hand there has been greater IMF intervention in the financial affairs of the country. In the current provisions of the amended bill, there should be no direct borrowing by the government from the State Bank of Pakistan, and all the concessional loans or the concessional lending programs that the government designs would not be funded or subsidized by the State Bank of Pakistan. The finance secretary will be kicked out of the board and abolition of the fiscal and monetary board is also one of the provisions of the amended bill. According to Dr. Yaqoob's proposals, there should not be any individuals' interference instead there should be institutional channels for coordination and cooperation between the State Bank of Pakistan and the Ministry of Finance.

In the new scheme of things, the State Bank of Pakistan will be responsible for inflation targeting set up through its considerations while readily there are no predefined criteria for inflation targeting. Notwithstanding, inflation in Pakistan cannot be controlled by monetary policy alone because it is not exclusively a monetary phenomenon in Pakistan. It is a mix of supply-side fluctuations and so many structural factors so it cannot be controlled single-handedly by monetary policy. He suggested that the developmental role of monetary policy should also be minimized. There is a need for integration of monetary policy with other policies e.g. exchange rate policy and fiscal policy through institutional arrangements like monetary and fiscal coordination boards. He remarked that there should be a difference between autonomy and anarchy. The ground reality of Pakistan is that there are so many laws that are written in the books but they never get to see the light of the day. This act could be one of the IMF conditionality only to please the IMF and the law may become redundant as soon as the program is over.

Is there any urgency for the new law or is the existing law good enough? The common practice has been that a monetary policy is formulated based on growth and inflation targets. State Bank only determines the safe limit of money supply expansion in a given period. The foreign reserves position and potential implications are taken into account then the scope for government borrowing is examined. There is a macroeconomic framework put in place to examine all these aspects while framing monetary policy. This framework ensures that monetary policy is market-based and according to best international practices, so in essence, there was no urgency for autonomy. It was already there in papers but not in fact. The need for amendment originated under the compulsion of IMF conditions the government is forced to do this amendment against its will.



## · Mr. Shahid Kardar viewpoint on the Autonomy of SBPT

The operational aspect of any institution's autonomy should not compromise the key objectives of the institution. The new law has assumed that objectives and functions of the 1956 Act, which was essentially a reflection of the economic structure of that era, should continue to be performed by the State Bank of Pakistan.

Due to the **potential conflict between objectives and functions**, SBP continues to perform certain functions which it shouldn't. For example, a component of debt management is being performed as safe deposits, deposits from other Central banks and Roshan digital accounts, etc. are managed by SBP needlessly. Similarly, injections into the economy are not encouraged. On Average, there is an injection of 1 trillion Rs. every year. In March there was an injection of Rs. 1.6 tr. which is almost 3.3% of GDP keeping the cost of government borrowing lower than it would be without injection. The decision of keeping interest rates high to squeeze the demand was also not welcome. It is akin to keeping the PKR overvalued; it also has implications for the stability of the financial system of the country.

**The new law proposes the primary objective to be price stability but it is not clear** what price stability means in the new scheme of things. There is a need to clearly define what price stability means and what is the extent of prices that will be controlled by the State Bank of Pakistan. There need to be well thought out and craftily set target rates of inflation. The criteria for inflation targeting should also be defined. It is also worth mentioning that we have never had that much high rate of inflation as Zimbabwe or Nigeria etc.

If SBP in the last 25-30 years has not been unable to exercise the autonomy under the existing law in performing its functions relating to the conduct of monetary policy and ensuring the stability of the whole financial system, it will likely fail in the future as well under the new law. Because **De jure autonomy has always been there it is only the de facto autonomy that has been lacking**. In the case of effective management of the exchange rate regime, there was a period when the State Bank of Pakistan itself kept the exchange rate overvalued, so the question is essential of de facto autonomy. CPI which gives 58% weightage to food and energy, anchoring CPI as an inflation indicator, and giving the task of price stability to SBP doesn't make any sense. There are un-accounted demand-side factors that need to be taken care of.

**Multilateral donor assistance** also leads to a major stir to GDP. Today barely 20% of bank borrowing is by the private sector. There is the matter of the output gap when the growth rate is nearly 3% it doesn't reflect the potential of the economy. This aspect should be considered seriously.

**How should we appoint the governor?** According to Dr. Kardar, the draft bill is poor on this aspect. Appointing authority is the President of Pakistan and the board of directors will be chosen by the Ministry of Finance from the list of individuals given by the State Bank of Pakistan. If such sweeping powers are granted to this body, then there will be consequences for the whole economy and the decision in prospects of growth and employment will be seriously undermined.

**Who should set targets?** Certainly neither the board nor the SBP management. According to the draft bill, the National Economic Committee is to set targets/parameters. And criteria for monetary policy should be assessed for performance evaluation. The SBP governor should not only be submitting the annual report in the parliament but he should also be quizzed by the finance committee and if needed by experts twice a year and details should be made public. There should be coordination and cooperation between various economic Institutions of the country but according to the draft will there is no provision for such coordination.

In the current law financial system and financial stability are being confused. Parameters should be set to define the meaning of financial stability so that performance could be assessed later on. There should be a balancing act through the fiscal coordination board. Growth and employment cannot be ignored as objectives it should be a combined effort.

## PIDE WEBINAR

**MONDAY, APRIL 5 - START 3PM**

# **The Autonomy for SBP: A Fresh Look at Central Bank Independence**

## **PART - IV**

In a significant move, the federal cabinet approved amendments in the State Bank of Pakistan (SBP) Act in the name of central bank autonomy, price stability and accountability. The benefit of central bank independence is well documented in the literature. However, there is a dire need to evaluate several important questions:

- Why is autonomy so important? Should every institution be autonomous?
- Is Pakistan prepared for the complete autonomy of the central bank?
- Can only SBP manage inflation given the constraints of the supply side and governance?
- What will be the implications for economic growth?
- What will be the implications for financial stability?
- How will the institution be accountable?

## **SPEAKERS**



**Dr. Hamza Ali Malik**  
Director, Macroeconomic Policy, UNESCAP



**Ashraf Janjua**  
Former Deputy governor at State Bank of Pakistan



**Dr. Ahmed Jamal Pirzada**  
Assistant Professor, University of Bristol, UK

## **MODERATOR**

**Dr Nadeem ul Haque**  
VC, PIDE



PIDE Islamabad



PIDEpk



PIDEpk



PIDE official



PIDE Islamabad



# Part-IV

## • **Mr. Ashraf Janjua's viewpoint**

Governor SBP is empowered to make any decisions independently without the fear of an explanation or accountability, so the new law is not needed for autonomy as SBP already has enough independence. What is needed is that the Governor should be competent enough and qualified for the job while at the same time accompanied by an efficient team of macroeconomists and researchers who update him about every economic development regarding policy implications and future policy conduct. He, however, expressed his concern that in current law the primary objective of SBP is monetary stability which is not just price stability and is a very comprehensive term that should be understood fully.

## • **Mr. Hamza Ali Malik's View point**

**Autonomy has already been here but the central bank was not exercising it.** Now when objectives have been clearly defined and inflation targeting is solely the responsibility of the State Bank of Pakistan this should make SBP more accountable for inflation but unfortunately, there is no accountability process defined in the new law. It should be clarified and strong measures of accountability are put in place only this way we can justify the new amended act. However, it was clearly expressed that this step is not going to define our long-term prosperity and development prospects. It needs other institutional and regulatory reforms.

He rejected the opinion that inflation isn't a serious problem in Pakistan. He said that it is fundamentally a serious issue in Pakistan. Inflation has impeded the long-term growth perspectives of Pakistan and there is lots of empirical evidence present in this regard. The average inflation for Pakistan in the year 2020 is 10.8% while the average inflation in most of the countries of the Asia-Pacific region is around 3-4% so in Pakistan inflation is around three times higher than the other countries in the region. By controlling inflation means that SBP is trying to give purchasing power to the piece of currency that the government is issuing. Among so many economic variables going to be influenced by this inflation are wages.

Quoting examples of direct government intervention in SBP, Dr. Hamza disclosed that there has been an erratic, volatile, and announced borrowing by the government directly from SBP especially after 2007-08, which kept on going up and up limitlessly since then. This practice of government entails a huge injection of liquidity even if it is in a controlled manner.

The conflict of interests is another issue. The finance secretary as a representative of the Ministry of Finance has been influencing monetary policy sitting in the monetary policy decision-making processes and keeping interest rate unnecessarily low for longer periods against all the empirical evidence produced by the State Bank of Pakistan. Exchange rate intervention is another case. It not only affects inflation but also has caused a balance of payment crisis in the country. Overvaluation of currency that we have seen in the past is due to dictation coming from the Ministry of Finance and it was the SBP's weaknesses in not sticking to its legal framework. whenever there has been opposition, the SBP governor had to lose the job. Therefore, the proposed law is right in setting up the objective straight and giving more job security to the governor but without accountability, it will make no difference if SBP chooses not to go operational on these lines.

Another point is that macroeconomic policies including the monetary policy of the country need effective coordination thus abolition of monetary and fiscal coordination boards is not advocated at any level. The proposed law says that the Governor as an individual and the finance secretary as an individual will coordinate in policy matters which is a very foolish idea and it leads to a non-transparent way of working. There should be institutional channels for institutional coordination.

There should be a formal institutional mechanism with proper minute taking records and those records need to be made public over time so people understand what is being discussed by policymakers that facilitates the accountability over time of all the macro institutions concerned so the law will only give you some direction the whole idea is actually whether you exercise what is already in the law or not. Dependence on the Ministry of Finance creates difficulties for the central bank to set its policy instruments.

Responding to a question about the role of SBP in the growth of the financial system, he advocated the positive role of SBP in the financial system. How Pakistan braved the financial crisis of 2008 without much harm to the economy was because the central bank regulated the financial market. SBP facilitated the development of the foreign exchange market and now we, fortunately, see that the exchange rate is pretty much market-determined.

***What is the optimal inflation target for Pakistan and who will define it? What is the normal anchor in Pakistan, what is the normal anchor the central bank has been pursuing up till now and what is the nominal anchor going forward and has that nominal income anchor been fixed by the central bank or by the ministry of finance?***

Responding to this question he stressed that SBP has been in inflation targeting mode since the early 2000s. The inflation target used to be set by the government and SBP would try to meet this target. And Inflation has been the nominal anchor in Pakistan. SBP research shows that 4-5% inflation is the threshold level of inflation that is neutral for the economy. Beyond this level, any upward deviation has negative consequences for the economy. So SBP is concerned about inflation targeting.

#### · **Mr. Ahmed Jamal's Viewpoint**

He concurred with Dr. Nadeem about the autonomy argument. However, he expressed his views regarding inflation targeting as the primary objective of monetary policy. He asserted that there is no rule to set the normal level of inflation in a country. Theoretically, there might be some principles but empirically it is proved that setting such threshold levels for inflation leads to unrealistic results. More important than inflation targeting is that SBP sets its objectives right. Instead of wandering between various policy regimes and policy instruments, SBP should set the anchor and work for it. It will ensure the stability of the system.

Dr. Ahmed remarked that if there is going to be enough autonomy and clarity of objectives for the central bank to work then instruments to be used specifically by SBP should also be defined particularly. And in that whole process government should be taken on board.

#### · **Conclusion**

Central Bank autonomy is not a bad thing. But in a country like Pakistan where institutions are the colonial residue, giving perfect autonomy to one institution alone, ignoring the autonomy of the rest of all institutions is not advisable. It will only create imbalance and institutional clash in the economy.

Secondly, it is very important to ensure an institutional framework for the across-the-board accountability of central bank staff, starting with defining qualification criteria for the selection of governors and deputy governors. Without across-the-board accountability, autonomy will not improve the economic conditions of the economy.

Lastly and most importantly, there should be open and transparent discussions on the subject between various stakeholders. There is no need to hide the law from the public; it should be open to debate before landing in parliament. Regarding the objectives and instruments of monetary policy, there should be a consensus among all the economic institutions to avoid any future clash of interests. The culture of informed opinion and debate is all that we need in Pakistan for all kinds of socio-economic problems. One can hope for sanity to prevail, the sooner the better.





**Prepared by**  
Aqsa Gul, MPhil  
Scholar PIDE

**Edited by**  
Hafsa Hina

**Design by**  
Afzal Balti

🌐 [www.pide.org.pk](http://www.pide.org.pk)  
✉ [policy@pide.org.pk](mailto:policy@pide.org.pk)  
☎ 92-51-924 8051  
📠 92-51-942 8065

📍 PIDEIslamabad

🐦 PIDEpk

📺 PIDE Official

🌐 [pide.org.pk](http://pide.org.pk)