RESEARCH PAPER

“Pakistani and Chinese Banking Sector - Readiness for CPEC Project and Comparison of Non-Performing Loans (NPLs)”

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Abstract

This paper provides a brief assessment of the global standing and ranking of major Chinese and Pakistani banks and at the same time analyses the current status of the Non-Performing Loans (NPLs) of the banking industry in Pakistan and China. The purpose of the analysis is to judge the capacity of leading banks in both countries in the perspective of China-Pakistan Economic Corridor (CPEC). The research paper also examines the readiness of Pakistani banks to reposition themselves in the backdrop of various business opportunities emerging from CPEC projects by planning ahead and readjusting priorities. The paper also looks at the preparedness of the Pakistani private sector to expand their capacities to exploit the CPEC opportunities.

Keywords: Non-Performing Loans, NPL ratio, listed banks, scheduled banks, private banks, CPEC, economic corridor, energy, infrastructure, Special Economic Zones (SEZs)

Preamble

The China-Pakistan Economic Corridor (CPEC) is said to be a 'game changer' for Pakistan. The two friendly countries whose friendship is regarded as taller than 'Himalayas' and deeper then 'oceans', have embarked upon a new venture which would bring them more closer to each other and would be a win-win game for both. The economic corridor which is going to be built would link Kashgar in China to Gwadar port in Pakistan. For Pakistan, this venture is expected to resolve energy shortages, stimulate domestic and foreign investment, reduce infrastructure bottlenecks, create massive job opportunities and boost economic growth. With US$ 46 billion investment committed, China is going to surpass UAE to become the top sourcing country for investment into Pakistan.

In addition to this massive Chinese investment of US$46 billion, local financing would also be required to meet the project financing demands of CPEC projects. Do our banks, DFIs and capital market have the capability and capacity to cater to the financing requirements and are they ready and prepared to play a dynamic role to maximize the opportunities that are ahead with the implementation of CPEC. As far as China is concerned, it is more focused on transportation network, whereas Pakistan is more concerned with the generation of more electricity. Do our banks have done the homework?

In this Research Paper, we would be making a comparison of the Chinese and Pakistani banking industry vis-à-vis the past and present trend of the non-performing loans (NPLs). We would also be looking at the readiness and preparedness of the banking sector as well the private sector of Pakistan to embark upon the economic corridor potential and opportunities. Before proceeding, let' have a look at some facts and figures about China-Pakistan Economic Corridor (CPEC).

CPEC : Facts and Figures

The China-Pakistan Economic Corridor (CPEC) encompasses projects from road and rail infrastructure to construction of power plants, financial, industrial and agricultural cooperation, development of free economic zones, educational linkage and technology transfer.

The four main components of the CPEC are as under:

1) Gwadar Port (including development of city around Gwadar)
2) Energy Projects (Coal, Hydel, Wind, Solar, LNG etc)
3) Transport Infrastructure (Road, Rail, Aviation)
4) Industrial Cooperation (Gwadar Free Zone and industrial Parks)

As per CPEC-related information available from government sources, the estimated cost to be incurred on 21 energy projects; 4 transport infrastructure projects and 8 projects for the development of Gwadar port and city would be around US$ 44.43 billion.

Sr.	Sector	No. of Projects		Estimated Cost (USD Billion)
1	**Energy**	24		**34.41**
2	**Transport Infrastructure**			
	Roads	2	6.10	
	Rail Network	2	3.69	
	Gwadar Port	8	0.79	**10.58**
3	**Others** (optical fibre Cable, DTMB)	2		**0.05**
	Total Cost of CPEC Projects			**44.43**

Source: Board of Investment and Planning Commission)

Energy Projects: The main focus of CPEC is on energy which is evident from the fact that out of total CPEC package of US$46 billion, around US$34.41 billion is in private sector, mostly in power generation in IPP mode. These energy projects is estimated to produce 17,045 MW of energy, out of which 6,645 MW energy projects are being actively promoted. Majority of these energy projects, as the government claims, relate to coal and wind and not hydel. One of the coal-based power plants will be installed in Thar to tap the coals reserves in the area and produce around 6,600 MW energy.

The Pakistani government has agreed to grant exemption of withholding tax on interest of loans to those Chinese companies who will be installing power plants as Independent Power Producers (IPPs) under CPEC. These Chinese companies will enjoy all exemptions currently available to IPPs in Pakistan. The modalities would be finalized after signing of treaty between the two countries.

Transport Infrastructure: The Chinese investment of US$ 10.63 billion for transport infrastructure would be made through government to government agreements, including US$6.1 billion for construction of roads; US$3.7 billion for rail networks and US$ 793 million for Gwadar-related projects e.g. construction of Gwadar international airport, Eastbay Expressway etc. The Chinese Exim Bank would be extending assistance to Pakistan at 1.6% interest rate for CPEC infrastructure projects.

Other Projects: The other projects that are part of CPEC-package are construction of cross-border optical fibre cable and Digital Terrestrial Multimedia Broadcast (DTMB) project. DTMB project is in fact belongs to the earlier harvest projects of CPEC and leading Chinese telecom network supplier ZTE has completed this project in March 2016. This project will allow the residents around Islamabad city to receive TV signals once they stall a set-top box. DTMB project signify 'information corridor' that would bring Chinese telecom standards to Pakistan (currently there are 4 telecom standards in the world viz. Chinese, European, Japanese and American)

Industrial Cooperation: A CPEC working group on Industrial Parks / Special Economic Zones (SEZs) have been constituted by the government to identify potential feasible sites for consideration by the CPEC Joint Working Group. BOI Pakistan has already identified potential sites in all Provinces of Pakistan – from Khunjrab to Gwadar – to establish SEZs alongside the Corridor. Each SEZ will target specific products and services based on availability of local raw material, work force and other factors. It is expected that establishment of SEZs will attract domestic and foreign investments and create employment opportunities for both skilled and unskilled workers in Pakistan.

Global Standing and Ranking of Chinese Banks

In August 2015, SNL Financial, a leading global provider of financial information, released its annual ranking of the world's largest banks in terms of their total assets. SNL ranks the largest banks in the world by converting their total assets into US Dollars by using the exchange rate as at end of period measured. This ranking revealed that today China has four out of five top largest banks in the world and overall there are 16 Chinese banks of the top 100 banks of the world (see table-1 and table 2) . USA stands second in the ranking with 11 largest banks out of 100, followed by Japan with 8 largest banks and then UK, France and Germany having 6 banks each in the listing of 100 top banks of world.

Table 1: SNL Financial Ranking of Top Five biggest Banks of the World in 2015 (based in terms of their Total Assets)

Ranking	Name of Bank	Country	Total Assets (USD Trillion)
1	Industrial and Commercial Bank of China Ltd	China	3.452
2	China Construction Bank	China	2.819
3	Agriculture Bank of China Ltd.	China	2.716
4	HSBC Holdings Plc	UK	2.670
5	Bank of China Ltd.	China	2.584

Source: Extracted from SNL Financial's List of top 100 banks of the world

As can be seen from **Table-1**, the Industrial and Commercial Bank of China tops the list with total assets of USD 3.5 trillion, which according to CNN is worth more than the entire value of the British economy. China Construction Bank with total assets worth USD 2.8 trillion ranks second whereas Agriculture Bank of China Ltd. having total assets of 2.7 trillion is at third standing in the list. The only non-Chinese bank in the Top 5 list is HSBC, having its headquarter in London, with ranking of fourth with total assets worth USD 2.67 trillion. The Bank of China is fifth with total assets of USD 2.6 trillion.

Table-2 provides the country-wise strength of all 100 largest banks in the world. As can be observed, 16 of the top 100 banks in the world are in China having total assets worth USD 18.87 trillion. USA ranks second with total 11 banks aggregating total assets of USD 12 billion. Europe, including Russia have 43 out of top 100 banks. If we take individually, Japan comes at 3rd position with 8 banks whereas UK, France and Germany with 6 banks each stands at 4th, 5th and 6th positions.

'The Banker' is a global financial Intelligence magazine and owned by Financial Times Group, UK, and a premier resource for the world's investment, retail and commercial banking sectors. Since 1970, it is regularly publishing world rankings of top 1000, which is a key source of data and analysis for the industry. According to its latest ranking of top 1000 banks 2015, the world's biggest banks continue to lose ground to Chinese rivals and the combined profits of all the Chinese banks in the ranking are almost double than those of USA Banks and ten times bigger than those of UK banks. It is pertinent to mention here that in 2008, both USA and UK banks were more profitable than the Chinese banks.

The 2015 Banker's ranking include 117 Chinese banks, out of top 1000 world banks. It is interesting to note that in 2010, only one Chinese bank could find place in Banker's top 10 banks' rankings, but within a short span of five years, the Chinese banks are now in dominant position, which indicates not only a major shift in global banking industry but also demonstrates the capital strength, improved asset quality and enhanced development potentials of Chinese banks.

Table 2: Country-wise strength of 100 largest Banks of the world- 2015

Sr.	Country	Total number of Banks in List of Top 100 largest Banks	Total Assets of Banks (USD Trillion)
1	China	16	18.865
2	USA	11	11.912
3	Japan	08	9.140
4	UK	06	8.692
5	France	06	8.519
6	Germany	06	4.032
7	Canada	05	3.277
8	Spain	04	2.800
9	Australia	04	2.087
10	Sweden	04	1.776
11	Brazil	04	1.606
12	South Korea	04	1.140
13	Netherlands	03	2.427
15	Italy	03	2.185
16	Belgium	03	0.800
17	Singapore	03	0.856
18	Switzerland	02	2.010
19	Denmark	02	0.764
20	Russia	02	0.631
21	Taiwan	01	0.225
22	Austria	01	0.217
23	Norway	01	0.346
24	India	01	0.432
	Total	**100**	**84.739**

Source: R&P Dept Analysis of SNL Financial's List of top 100 banks of the world

Three Chinese banks are in The Banker's top five slot in 2015 ranking with Industrial and Commercial Bank of China (ICBC) securing first position continuously for the third time. In fact, ICBC with over 460 thousand employees and having over 460 million e-banking and 150 million mobile banking customers, also enjoys the top ranking at the 'Forbes Global 2000' list.

Table-3 shows the list of top 10 banks of the world in terms of their Tier 1 Capital, ranked by The Banker, which includes four banks each from China and USA and one bank each from UK and Japan.

Table 3: The Banker's 2015 Ranking of Top 10 Banks (based in terms of Tier 1 Capital)

Ranking	Name of Bank	Country	Tier 1 Capital (USD Billion)
1	ICBC	China	248.6
2	China Construction Bank	China	202.1
3	JP Morgan	USA	186.6
4	Bank of China	China	184.2
5	Bank of America	USA	168.9
6	Agricultural Bank of China	China	167.7
7	Citigroup	USA	166.5
8	Wells Fargo & Co.	USA	154.7
9	HSBC Holdings	UK	152.7
10	Mitsubishi UFJ	Japan	117.6

Source: The Banker's website: www.thebankerdatabase.com

Global Standing and Ranking of Pakistani Banks

Few large Pakistani banks have been able to get global recognitions and awards from the international financial ratings agencies such as EUROMONEY, The BANKER, The ASIAN BANKER, GLOBAL FINANCE and the ASIA MONEY. Table-4 shows global awards received by Pakistani banks.

Table 4 : Pakistani Banks receiving Global Recognition Awards

National Bank of Pakistan (NBP)

The Bank of the Year in Pakistan	The Banker, UK	2015, 2013, 2012, 2011, 2010, 2008, 2005, 2004, 2002 and 2001
Domestic Retail Bank of the Year	Asian Banking and Finance Magazine	2013
Domestic Technology & Operations Bank of the Year	Asian Banking and Finance Magazine	2013
Best Emerging Market Bank -Pakistan	Global Finance, UK	2006 and 2003
Best Foreign Exchange Bank -Pakistan	Global Finance, UK	2005 and 2004

Name of Award	Global Awarding Agency	Year of Receiving Award
Best Local Trade Finance Bank in Pakistan	Global Trade Review (GTR)	2015, 2014, 2013, 2011
Best Trade Finance Provider in Pakistan	Global Finance Magazine	2014, 2010, 2009
Best Bank in Pakistan	Euro money	2015, 2014, 2013, 2009, 2008
Best Domestic Bank in Pakistan	Asia money	2015
Safest Bank in Pakistan	Global Finance	2015, 2014
Best Investment Bank	International Finance Magazine	2015
The Bank of the Year in Pakistan	The Banker, UK	2014, 2009
No. 1 FX Bank in Pakistan	Euro money	2013
Best Retail Bank in Pakistan	The Asian Banker Magazine	2013, 2012
Best Emerging Market Bank	Global Finance	2012, 2010, 2009
Strongest Bank in Pakistan	The Asian Banker Magazine	2012
Best Foreign Exchange Provider in Pakistan	Global Finance	2009

Muslim Commercial Bank (MCB)

Name of Award	Global Awarding Agency	Year of Receiving Award
Best Bank in Pakistan	Asset Asian Awards (AAA)	2014, 2006, 2003, 2001
Best Domestic Bank in Pakistan	Asset Asian Awards (AAA)	2014, 2013, 2012, 2009
Best of the Best Domestic Bank	Asia money Awards	2014, 2009
Strongest Bank in Pakistan	The Asian Banker Magazine	2014, 2010
Best Bank in Pakistan	Euro money Magazine	2012, 2011
Best Bank in Asia	Euro money Magazine	2008

Allied Bank Limited (ABL)

Name of Award	Global Awarding Agency	Year of Receiving Award
Strongest Bank by Balance Sheet – Pakistan	The Asian Banker Magazine	2014
Best Domestic Investment Bank in Pakistan	The Asset Magazine, Hong Kong	2013, 2009
Best Managed Bank Achievement Award 2013	The Asian Banker Magazine	2013
Best Investment Bank in Pakistan – 2013	Euromoney Magazine, UK	2013
Bank of the Year in Pakistan	The Banker, UK	2011
Best Retail Bank in Pakistan	The Asian Banker Magazine	2011
Best Equity House in Pakistan	The Asset Magazine, Hong Kong	2008
The Banker Deal of the Year – Pakistan	The Banker, UK	2008

Askari Bank Limited

Name of Award	Global Awarding Agency	Year of Receiving Award
Best Bank in Pakistan	Global Finance Magazine	2001 and 2002
Best Consumer Internet Bank	Global Finance Magazine	2002 and 2003

United Bank Limited (UBL)

Name of Award	Global Awarding Agency	Year of Receiving Award
The Bank of the Year in Pakistan	The Banker, UK	2013
Best Domestic Bank in Pakistan	Asia money Awards	2012

Habib Metropolitan Bank (HMB)

Name of Award	Global Awarding Agency	Year of Receiving Award
ADB Leading Partner in Pakistan Award	Asian Development Bank (ADB)	2015
Best GTFP Issuing Bank for South-South Trade	Int'l Finance Corporation (IFC)	2012

Meezan Bank

Name of Award	Global Awarding Agency	Year of Receiving Award
Shariah Authenticity Award	Global Islamic Finance Awards	2015
Best Research & Development in Islamic Finance	Global Islamic Finance Awards	2013
Best Islamic Bank, Pakistan	Asset Triple A Islamic Finance Awards	2015
Best Islamic Retail Bank, Pakistan	Asset Triple A Islamic Finance Awards	2015
Best Islamic Trade Finance Bank, Pakistan	Asset Triple A Islamic Finance Awards	2015
Best Islamic Investment Bank, Pakistan	Asset Triple A Islamic Finance Awards	2015
Best Sukuk House, Pakistan	Asset Triple A Islamic Finance Awards	2015
Best Islamic Trade Finance Deal, Pakistan	Asset Triple A Islamic Finance Awards	2015
The Best Islamic Bank in Pakistan	Global Finance Magazine	2015, 2014, 2013, 2012, 2011, 2010, 2009

Rankings of Pakistani Banks in terms of Total Assets

As per State Bank of Pakistan (SBP), the total assets of all Pakistan banks by end March 2015 stood at Rs. 12,528 billion, showing an increase from Rs. 10,752 billion at end March 2014. In 2008, the total assets of all scheduled banks stood at only Rs. 5,628 billion.

Table 5 : Total Assets of Pakistani Commercial and Specialized Banks (By end March 2015)

Category of Bank	Total Assets (Rs. in Billions)	% share in Total Assets
Commercial Banks (CB)	12,342	98.52%
Specialized Banks (SB)	186	1.48%
Total	12,528	

Table-5 presents the total assets held by commercial and specialized banks in Pakistan by March 2015.

The Research and Publications Directorate conducted a brief analysis of the Balance Sheets of few large and medium-size banks in Pakistan to rank them in terms of highest value of total assets. The analysis reveals that Habib Bank Limited (HBL) tops the ranking with Rs. 1867 billion worth of total assets, followed by National Bank of Pakistan (NBP) with Rs. 1543 billion total assets.

Table-6 shows the Top-5 ranking Pakistani banks in terms of total assets.

Table 6 : Rankings of Pakistani Banks in terms of their Total Assets

Ranking	Name of Bank	Total Assets (Rs. in Billions)
1	Habib Bank Limited (HBL)	1867
2	National Bank of Pakistan (NBP)	1543
3	United Bank Limited (UBL)	1111
4	Muslim Commercial Bank (MCB)	935
5	Allied Bank Limited (ABL)	843

Non-Performing Loans (NPL) of Pakistani and Chinese Banking Industry

The Non Performing Loans (NPL) are those financial assets from which the banks no longer receive interest and/or installment payments. In other words, NPL are called non-performing because the loan ceases to 'perform' or generate income for the bank. High NPLs shrinks the operating margin of the banks and erodes their capital base to advance new loans, often termed as 'credit crunch'. The lower credit supply eventually have a negative on the economic. Normally, Non Performing Loans are the result of economic slowdown, however, these are also due to lack of effective monitoring and supervision on the part of the banks, which do not have any effective debt recovery strategies.

Let's have a look in detail on the Non-Performing Loans (NPLs) of the Chinese and Pakistani banking industry and the policy measures taken by the governments in these two countries.

NPLs of Chinese Banks

The non-performing loans (NPL) of commercial banks in China are continuously on the rise. In fact, it has more than doubled in 2015 from previous year. By the end of 2015, NPL of Chinese commercial banks have soared to 1.95 trillion Yuan (or US$ 296.8 billion) from just 842.6 billion Yuan in 2014. Table-7 shows the volume of Non-Performing Loans of the Listed Chinese Banks since 2008.

The main reason that can be attributed to this huge increase in NPL is overcapacity and slowdown in Chinese economy from 9.5 percent in 2011 to around 7 percent in 2014. This is expected to go down further to 6.5 percent in 2015 and onward. Resultantly, the banks profit also fell down to just 2.3 percent. Majority of these non-performing loans are in manufacturing, wholesale and retail sectors.

According to the data available on the website of China Banking Regulatory Commission (CBRC), both the levels of NPLs and the NPL ratio (defined as total NPLs over total loans) of commercial banks have increased steadily over 16 consecutive quarters, reaching 1.186 trillion Yuan by end September 2015. In the first 9 months of FY 2015, the NPL rose to 343 billion Yuan as against 251 billion Yuan in the corresponding period of last year.

Table 7 : Non-Performing Loans (NPLs) of Chinese Listed Banks

Year	NPL (Billion Yuan)	NPL (Billion USD)	NPL Ratio
2008	476	69.79	2.43%
2009	419	61.35	1.60%
2010	361	54.78	1.16%
2011	351	55.77	0.99%
2012	373	59.87	0.95%
2013	592	97.70	1.00%
2014	843	135.75	1.25%
2015	1950	296.80	1.59%

Table 8: NPL Ratios of Five Big Banks in China (By end September 2015- Q3)

Sr	Name of Bank	NPL Ratio
1.	Industrial and Commercial Bank of China (ICBC)	1.44%
2.	China Construction Bank (CCB)	1.45%
3.	Agriculture Bank of China (ABC)	2.02%
4.	Bank of China (BOC)	1.43%
5.	Bank of Communications (BOCOM)	1.42%

Yuan to USD Exchange rate by end December each year : 6.82 (2008); 6.83 (2009); 6.59 (2010); 6.29 (2011); 6.23 (2012); 6.05 (2013); 6.21 (2014) and 6.50 (2015)

Source: Website of Chinese Banking Regulatory Commission and financial newspapers

As can be seen from **Table-7**, the NPL ratios of the Chinese listed banks are steadily rising since 2012. NPL ratio of listed banks was 1% in 2013 which increased to 1.25% in 2014 and by the end of Q3 i.e. end September 2015, NPL ratio rose further to 1.59%. It is expected that in 2016, the NPL ratio will touch the 2 percent level. It may be mentioned here that in 2001, the NPL ratio of Chinese banks was as high as 29.8%, which fell to 20.4% in 2002 and further to 13.2% in 2004 and then to 6.2% in 2007. Since 2008, the NPL ratio has been drastically reduced to 2.4% as indicated in Table-7.

In **Table-8**, the NPL ratios of the 'Five-big' state-owned Chinese banks have been highlighted. As can be seen, the Agricultural Bank of China (ABC) has the hightest NPL ratio of 2.02%. In 2013, NPL ratio of ABC was only 1.22% which increased to 1.54% in 2014. Similarly, the NPL ratios of Industrial and Commercial Bank of China (ICBC) increased from 0.94% in 2013 to 1.13% in 2014 and 1.44% in 2015. The same was the case with China Construction Bank (CCB). This signfies a concerning trend for these four-big state owned banks of China as it is eroding their operating profit margins. According to figures available from the China Banking Regulatory Commission (CBRC), by end of March 2015, the aggregate amount of NPLs of the three state-owned Chinese banks (i.e. ICBC, CCB, and ABC) stood at 412.8 billion Yuan which accounted for 58% of total NPL balance of 16 listed banks.

Realing the increasing trend of NPL ratio, these banks are now focusing on reducing their amount of unsecured debts on their books. However, there is still inherent risk due to increasing loans to businesses and lack of any risk management systems, covering the entire process of assessment and management, prior to after grant of credit to businesses.

The growing NPLs are a great concern for the Chinese government. In fact, the economic slowdown in China coupled with weakening domestic and overseas demand and overcapacity in steel and other industries has resulted in increasing financial risks and cash flow problems for the businesses. The Central Bank in China has taken various measures to check this increasing trend in NPLs of commercial banks such as cutting the interest rates and Banks' reserve requirement ratios. The regulators have also introduced some additional capital requirements as well on banking industry.

NPLs of Pakistan Banks

The non-performing loans (NPLs) of Pakistani scheduled banks have increased over the years as depicted in Table-9. The NPLs stood at Rs. 359 billion in 2008, which continuously rose to reach the level of Rs. 618 billion in 2012 and by end of June 2015, NPL has climaxed to Rs. 630 billion. On the other hand, the NPL ratio has shown a declining trend, which is indicative of the fact that gross loans of banks has increased manifold, resulting in persistent decline in NPL ratio from 15.7% in 2011 to 12.3% in 2014 and increasing slightly to 12.8% by end of March 2015.

Table 9 : Non-Performing Loans (NPLs) of Pakistani Scheduled Banks

Year	NPL (Billion Rupees)	NPL (Billion USD)	Infection Ratio (%)
2008	359	4.56	10.5%
2009	446	5.28	12.6%
2010	556	6.50	14.9%
2011	592	6.58	15.7%
2012	618	6.35	14.6%
2013	607	5.75	13.3%
2014	595	5.92	12.3%
2015	630	6.00	12.8%

Table 10: NPL Ratios of Five Big Banks in Pakistan (On January 2015)

Sr	Name of Bank	NPL Ratio
1.	Habib Bank Limited (HBL)	2.7%
2.	National Bank of Pakistan (NBP)	3.7%
3.	United Bank Limited (UBL)	2.6%
4.	Muslim Commercial Bank (MCB)	1.2%
5.	Allied Bank Limited (ABL)	1.1%

Pak Rs. to USD Exchange rate by end December each year:78.75 (2008); 84.40 (2009); 85.60 (2010); 89.95 (2011); 97.27 (2012); 105.50 (2013); 100.53 (2014); 104.90 (2015)

Source: Website of SBP, Banks and financial newspapers

Table-10 shows the NPL ratios of 'Five-big' listed banks in Pakistan, according to which National Bank of Pakistan (NBP) has the highest NPL ratio of 3.7% whereas Allied Bank of Pakistan has the lowest NPL ratio of 1.2 percent. From table-6 it can be observed that ABL is ranked 5th among top-5 banks in terms of total assets, whereas NBP is first in ranking, though it is on top with highest NPL ratio.

Now, let's analyse here the bank category-wise and segment-wise position of non-performing loans. As can be observed from Table-11, more than 90 percent of non-performing loans (NPLs) in the banking industry are with local private banks and public-sector commercial banks. The share of local private banks is pre-dominant with almost 62 percent by end June 2015, followed by 31 percent of public-sector commercial banks. The specialized banks have around 6 percent share in total NPLs.

Sr.	Category of Bank	June 2014	%share in Total NPLs	June 2015	%share in Total NPLs
1	Local Private Banks	380,476	63.91	391,272	62.10
2	Public Sector Commercial Banks	171,294	28.77	196,592	31.20
3	Specialized Banks	36, 829	6.19	38,584	6.12
4	Foreign Banks	6,699	1.13	3,582	0.57
	Total	595,298	100%	630,030	100%

Table 11 : Bank Category wise Non-Performing Loans (NPLs) (Value in Million Rupees)

As far as sector/segment-wise distribution of NPLs is concerned, it is evident from Table-11 that the 'Corporate sector' has the highest share in overall NPLs of banks i.e. 70.29% in June 2015, followed by the SME sector with around 14% share. The share of agriculture sector and commodity financing in overall NPLs of banks have shown an increasing trend in 2015 as compared to last year, which reflect high loan advancement by banks to these sectors.

Table 11 : Segment/Sector – Wise Non-Performing Loans (NPLs) (Value in Million Rupees)

Sr.	Sector / Segment	June 2014	%share in Total NPL	June 2015	%share in Total NPL
1	Corporate Sector	415,832	69.85	442,849	70.29
2	SME Sector	89,693	15.07	88,269	14.01
3	Agricultural Sector	36,437	6.12	45,756	7.26
4	Consumer Sector	35,764	6.01	34,066	5.41
5	Commodity Financing	4,649	0.78	6,685	1.06
6	Others (staff loans etc)	12,922	2.17	12,405	1.97
	Total	595,298	100%	630,030	100%

Readiness of Chinese Banks for CPEC

In 2014, the GDP growth rate in China was 7.40 percent, which was the lowest witnessed during the last 24 years. However, despite this slowdown, the Chinese growth was comparatively much better than other economies of the world. In March 2015, the Chinese government adjusted its approach towards growth by lowering the GDP growth target to 7 percent for the first time. According to a research study titled 'The World in 2050: Will the Shift in Global Power Continue", it has been projected that China will continue to maintain GDP growth rate of 6.30 percent annually upto the year 2020 before slowing down. However, China will eventually become the World's largest economy (by market exchange rates) in 2028, surpassing the USA. It would not be out of place to quote here a statement made by the Chinese President Xi Jinping at the G-20 Summit in Turkey in December 2015 that "Despite a recent slowdown, China has still contributed 30 percent of world economic growth, which means China is still a major economic powerhouse".

Notwithstanding pressures on Chinese banking industry due to economic slowdown and competition, the emerging trends indicate that the Chinese banks are likely to get a major fillip in their businesses, as a result of some fresh initiatives undertaken by the Chinese Government under its "New Normal' growth strategy, such as 'One Belt and One Road" initiative; China-Pakistan Economic Corridor (CPEC) project, Silk Road Economic Belt and regional integration among Beijing, Tianjin and Hebei and the Yangtze River Economic Belt. All these macro-economic initiatives and developments would certainly motivate the Chinese banks to redraw their regional and international strategies in order to take maximum benefit from the emerging opportunities in the region.

Sustainable economic growth and development depends much on improved infrastructure networks. China has large capital and strong resources with huge foreign reserves, which coupled with its experience in infrastructure construction, places it in a better position to complete these projects as planned and envisioned. The completion of these projects would not only stimulate the global economy but also benefit China and its neighboring countries, including Pakistan, which need more infrastructure investments, as a launching pad to achieve rapid economic growth.

To meet the financing needs of the above projects, China has also taken a lead to establish the Asian Infrastructure Investment Bank (AIIB) and the New Development Bank for BRICS which includes China, Russian, India, South Africa and Brazil. The Asian Infrastructure Investment Bank would help finance infrastructure construction projects in Asian countries. The AIIB is going to commence operations from January 2016 and already fifty countries have become its members, including developed countries like France, UK and Germany. USA, however, has decided not to join AIIB due to its own reservations that AIIB would undermine the role of World Bank and IMF.

Readiness of Pakistani Banks for CPEC

With the initiation of second phase of CPEC-related projects, the banking sector of both Pakistan and China are expected to play a vibrant role in providing finances and working capital to companies who are going to set up businesses and industries in the Special Economic Zones (SEZs). Many banks in Pakistan, who are already part of consortiums to fund different energy and road construction projects under CPEC, have also started thinking and planning about how to exploit the upcoming business opportunities and economic boom with the establishment of Special Economic Zones (SEZs).

According to the information available to Research Department of ICMA Pakistan, major banks are repositioning themselves; re-orienting their internal systems and upgrading their project financing and business development and intelligence departments to take the lead. For instance, the National Bank of Pakistan (NBP) has set-up a new 'Business Development Unit' whereas UBL, HBL, MCB Bank, ABL and Bank Alfalah are in process of upgrading their project financing and business development cells.

Apart from the above preparatory initiatives undertaken by banks, there are some reservations on CPEC as well which are hindering them to finalize medium and long term future business plan such as:

a) Government's reluctance to provide specific, full and final details of CPEC-related projects
b) Non-clarity of financial make-up of CPEC promised funds i.e. actual amount of debt and equity
c) Grievances of Provinces on execution of CPEC projects

d) Confusion about better projections for forex and interest rate movements
e) Concerns related to volatile political scenario in the Middle East
f) Insufficiency of banks deposits for financing or co-financing big CPEC-projects

There are some apprehensions in the banking as well as private sector in Pakistan about our readiness to meet the challenges and to make the most of the upcoming opportunities under CPEC. One major apprehension is that banks in Pakistan are not sufficiently capitalized to undertake the local currency financing of the domestic component of CPEC- related project which is estimated to be around Rs. 800 billion or more. Therefore, there is urgent need for banks to strengthen their balance sheets by resorting to capital markets so as to meet the local currency financing of CPEC projects. At the same time, the Securities and Exchange Commission of Pakistan (SECP) also need to foresee the expanding role of capital market in the backdrop of CPEC and propose some measures in forthcoming budget.

Another apprehension in the minds of businessmen and bankers is that the current interest rate differential between Chinese and Pakistani banks is likely to render the Pakistani banks uncompetitive against their Chinese counterparts in terms of financing of CPEC projects. For this purpose, the State Bank of Pakistan should come forward with a special policy to enable the Pakistani banks to compete with Chinese banks to provide funds to private sector so that they can take up mega projects under CPEC. The capacity of banks also need to be enhanced as even the Chinese banks would also be requiring local financing in Pakistan to compensate their equity cost.

The Government also need to consider establishing a new "Infrastructure Development Bank' to provide rupee components for the projects to be undertaken under CPEC. This is important because China has hitherto not committed to finance CPEC projects from either the 'Asian Infrastructure Investment Bank (AIIB) or its 'Silk Road Fund'. Therefore, all financing is to be done by both sides. In this context, the Pakistani government should allocate sufficient funds under Federal PSDP in the budget 2016-17 as there were no allocations for CPEC in the 2015-16 PSDP financing.

The Pakistani banks need to invest in human and technological resources to become effective partners of banking consortia and syndicates that would be making project financing in CPEC projects. Unlike previous experience of banking consortia which comprised mostly of local and Pakistani-based foreign banks, the CPEC project financing banking syndicates would comprise of local , Chinese and foreign banks not operating from Pakistan. Hence, this would altogether be a new experience for the Pakistani banks and for this they need to invest smartly in their human and technological resources.

Another area which need to be improved by Pakistani banks is to enhance expertise in appraisal of credit proposals and product development. So far, the banks have been making easy money through investment in debt market that brought their advances to deposit ratio to around fifty percent.

Readiness of Private Sector in Pakistan for CPEC

If we look at the preparedness of private sector and industry in Pakistan on CPEC, we observe that they are anticipating great business potential and opportunities. The business confidence is rising as the implementation of CPEC projects is under progress. This is evident from the fact that some , major business groups have even started investing in expanding their production capacities, especially in raw materials to be used in construction such as cement, steel, glass, electric cables etc.

According to research conducted by ICMA Pakistan, Nishat Group is planning to set-up a cement plant in Balochistan whereas Lucky cement is going to install a cement plant in Punjab. Similarly, Younus Brothers, owners of Lucky Cement are contemplating a 'coal power plant' in Karachi. There are other companies dealing in steel, cables and other sectors who are also expanding their production capacities. There are indications that many foreign companies have contacted their Pakistani counterparts to establish joints venture projects in Pakistan to cater to demand of items to be required under the different CPEC-related power and construction projects. There are also news that several Pakistani businessmen and industrialists from Karachi and Lahore have approached the banks to explore the possibility of long term financing in medium and large projects that they intend to launch to exploit the business opportunities emerging from CPEC.

These positive developments will be opening up avenues for our banks to increase their lending to private sector so that they have sufficient working capital available to prepare themselves to meet the impending demands of these products as soon as the work on CPEC is expedited in second phase. ■

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