2 Currency Management

Currency Management is one of the core operational areas of SBP BSC as it deals with distribution, management and withdrawal of banknotes and coins. Further, SBP BSC is also entrusted with operational management of Prize Bonds and government savings certificates. These functions are undertaken through 16 SBP BSC field offices and 224 NBP Chest branches.

2.1 Overview

SBP BSC strives to ensure implementation of policies and guidelines relating to currency management and government savings schemes issued by the State Bank of Pakistan (SBP) and Central Directorate of National Savings (CDNS) respectively. The primary objective of Currency Management is to undertake end-to-end management and distribution of good quality notes in circulation while timely ensuring disposal of soiled banknotes. SBP BSC endeavors to match its operational management and currency processing / cash handling procedures in the country with international best practices to set a benchmark for the industry to evolve and employ globally trusted technologies for managing currency operations in Pakistan.

Accordingly, SBP BSC endeavors to:

i. Build and maintain public confidence in the currency by preserving its value and integrity by ensuring adequate availability of good quality banknotes in the market to meet the demand for currency, which is essential for the proper functioning of the economy.

ii. Arrange for timely printing and effective stock management of currency notes and prize bonds in coordination with Pakistan Security Printing Corporation (PSPC).

iii. Ensure swift withdrawal of soiled notes from the market and their subsequent destruction with enhanced control environment, so as to improve the overall quality of the notes in circulation.

iv. Issue comprehensive instructions to its 16 field offices for effective implementation of SBP's Currency Management Strategy (CMS) through rigorous on-site examinations and monitoring by Cash Monitoring Hubs (CMHs) across Pakistan.

v. Propose new developments to align existing currency management function with international best practices.

vi. Ensure effective operational management of Government Savings Schemes and winning prize arrangements for National and Premium Prize Bonds in coordination with CDNS.

vii. Strengthen Anti Money Laundering and Combatting Financing of Terrorism (AML & CFT) regime in government savings operations performed by SBP BSC.

2.2 Key Stakeholders

- Commercial Banks
- Pakistan Railways
- Central Directorate of National Savings
- Pakistan Security Printing Corporation
- Pakistan Mint
- Law Enforcement Agencies (LEAs)
- State Bank of Pakistan

2.3 Key Performance Highlights during the Year

Box 2.1: Key Performance Highlights during FY20

Currency Operations

- Ensured uninterrupted supply of fresh notes across the country, with 29 % YoY increase in total issuance of fresh notes in FY20
- Conducted 1,203 cash monitoring examination by CMHs during FY20 showing an increase of 17% from previous year
- Formed centralized destruction hub of lower denomination banknotes at SBP BSC North Nazimabad

Efforts to Combat COVID-19 Pandemic

- Released fresh notes worth Rs. 89 billion to commercial banks for Ehsaas Emergency Cash Program announced by the Federal Government
- Facilitated supply of disinfected re-issuable notes to banks in replacement of quarantined cash
- Balance sheet relief of Rs.9.1 billion for banks with regards to quarantined cash
- Managed uninterrupted supply of fresh notes while ensuring minimum public dealing
- Issued detailed guidelines to SBP BSC offices and banks to curb the spread of COVID-19 pandemic

Government Savings Operations

- Successful withdrawal of Rs.236 billion worth of Rs.40,000 bearer National Prize Bonds (NPBs), amounting to 99% of the outstanding value in circulation
- Payment of prize money and face value on National Prize Bonds through direct credit and Branchless Banking Accounts
- Claim of prize money from commercial banks for facilitation of general public

AML &CFT

- Implementation of system-based screening of proscribed / designated persons in July 2019 to comply with Anti Money Laundering 2010 Act, the National Counter Terrorism Authority (NACTA) guidelines and United Nations Security Council Resolution (NSCRS) & Financial Action Task Force (FATF) Recommendation R-6.

2.4 Operational Performance

2.4.1 Circulation of Banknotes

Pakistan is a highly cash centric economy with presence of informal markets / businesses that mostly rely on cash. Hence, the value of Notes-in-Circulation (NIC) has been increasing, despite increase in usage of online and point-of-sale banking and alternative payment channels. During FY20, NIC witnessed an annual growth of 22.0%, with the NIC as a percentage of Gross Domestic Product (GDP) standing at 15.6%, highlighting the cash centricity of Pakistan's economy. The increasing trend of cash has been more pronounced in FY20, with COVID-19 pandemic being the major driver. **(Table: 2.1).**

Table 2.1: Comparison of GDP and NIC in FY20 ***Rupees in millions***

Year	Nominal GDP	Notes in Circulation (NIC)	NIC as % of GDP	NIC Change over previous year
FY19	37,972,310	5,319,186	14.0%	13.4%
FY20	41,726,683	6,492,272	15.6%	22.0%

2.4.2 Currency Management

SBP BSC's main focus area is ensuring availability of good quality banknotes across the country. The distribution of fresh notes is ensured through active and timely coordination with SBP BSC's 16 field offices, NBP Chest and commercial banks' branches across the country. The issuance of fresh notes in FY20 exhibited significant deviation from previous years' trends **(Table: 2.2 below)**.

Table 2.2: YoY Comparison of Fresh Notes Issuance *(No. and value of pieces in millions)*

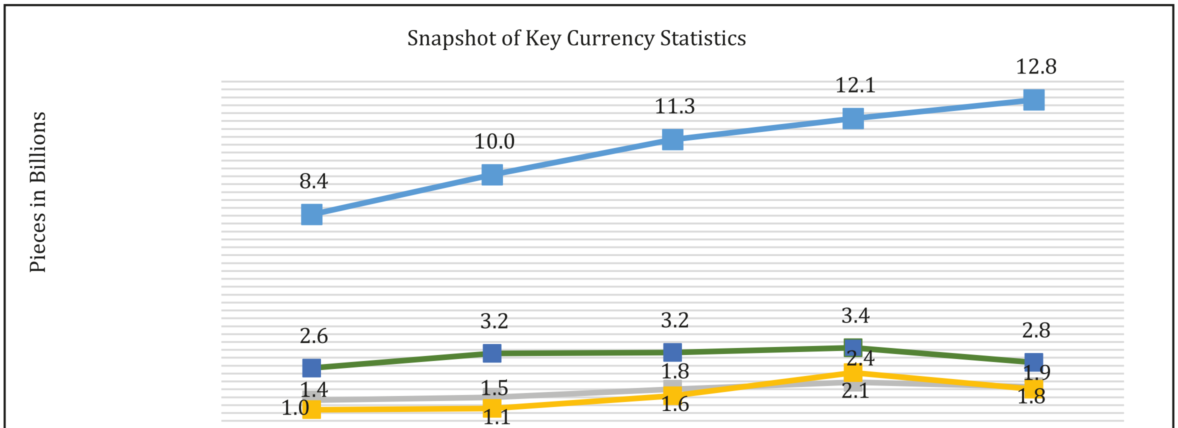
Year	Lower Denomination (Up to Rs. 100)				Higher Denomination (Rs. 500 & Above)			
	Pieces	% Increase	Value	% Increase	Pieces	% Increase	Value	% Increase
FY19	2,473	5.6	77,301	7.5	880	5.1	1,226,150	8.7
FY20[2]	1,667	-32.6	64,014	-17.2	1,175	33.5	1,611,167	31.4

[2] T-24 Currency Data as of 30 June 2020

The primary reasons for the record increase in demand of higher denomination fresh banknotes were the increased issuance emanating from mandatory requirements for quarantine of infected cash, general public's reliance on cash as the preferred medium of exchange during emergencies, ATM feeding through disinfected/fresh cash and cash payments for government's Ehsaas Program. The same is elucidated in detail in Section 2.4.7.

Meanwhile, in view of the lockdown across the country and the risk of non-compliance of social distancing measures at commercial bank branches, the 8877 service (for issuance of fresh notes to the public), remained suspended for both Eid occasions. Resultantly, the issuance of lower denomination banknotes in FY20 saw a YoY decline of 33%.

The Currency in Circulation (CIC) saw an increase of 6% YoY in terms of pieces. Meanwhile destruction of banknotes saw a decline of 25% on YoY basis, due to halting / suspension of examination and destruction at SBP BSC offices as a COVID-19 pandemic measure. **(See Figure: 2.1)**



	FY16	FY17	FY18	FY19	FY20
CIC	8.4	10.0	11.3	12.1	12.8
Soiled Receipt	1.4	1.5	1.8	2.1	1.9
Notes Destroyed	1.0	1.1	1.6	2.4	1.8
Fresh Issued	2.6	3.2	3.2	3.4	2.8

Figure 2.1: Snapshot of Key Currency Statistics

2.4.2.1 Counterfeit reporting / confiscation

The increase in counterfeits reported by banks to SBP BSC offices and the lower number of counterfeits detected during examination at SBP BSC's end reflects an improvement in banking system's counterfeit detection capability with mandatory machine processing and stronger reporting mechanism at commercial banks. Meanwhile, the lower number of counterfeits detected in examination can also be attributed to suspension of examination procedures in March 2020, due to COVID-19 pandemic.

2.4.3 Monitoring of Currency Operations

2.4.3.1 Cash Monitoring of Commercial Banks

Currency Management Strategy (CMS) was rolled out in 2015, primarily to ensure the circulation of good quality banknotes and curb the increasing spread of counterfeits in the economy. To materialize the objectives of CMS, it was of utmost importance that the banks meticulously comply with the CMS guidelines. For the purpose, three (03) dedicated Cash Monitoring Hubs (CMHs) were established at Karachi, Lahore and Rawalpindi in October 2018.

During FY20, the monitoring of commercial banks was further strengthened after the implementation of CMS on countrywide basis. Despite the spread of COVID-19 pandemic in the second half of the financial year and lockdowns across the country, the CMHs undertook 1,203 examinations of commercial bank branches, including 208 Cash Processing Centers, 189 Cash Feeding Branches, 530 Standalone and 276 Linked branches. In comparison, 1,027 examinations of commercial bank branches were conducted in the previous year. Cumulative penalties imposed amounted to Rs. 21.59 million during FY20 as compared to Rs. 40.5 million in FY19, highlighting implementation of a stronger compliance regime by commercial banks and effectiveness of the cash monitoring exercise.

The CMH teams also conducted over 45 classroom and online awareness sessions regarding machine sorting, banknote packing and allied instructions under CMS for capacity building of the cash officers at commercial banks to further improve their compliance.

2.4.3.2 NBP Chest Examination

During FY20, on-site examination of NBP Chest branches was decided to be carried out twice in a financial year. The first cycle was timely completed whereby all 224 chest branches were visited with rigorous follow-up to get the irregularities/ observations rectified. A comprehensive report highlighting the non-compliant aspects and higher risk NBP branches was put up to the senior management. The second cycle was initiated in second half of FY20 with focus on high-risk branches, which were carrying balances in excess of their holding capacities. However, due to the outbreak of COVID-19 pandemic, the same could not be completed.

2.4.4 Automation of Currency Management Operations

In pursuance of SBP's strategic goal to maintain good quality banknotes in circulation as well as to ensure effective implementation of CMS, SBP BSC is gradually transforming its currency operations from manual to automated environment in line with international standards. During FY 20, 4 Banknote Disintegration Systems (BDS) were installed at Lahore, Faisalabad, Peshawar and North Nazimabad offices. The installed machines allow for bulk shredding of banknotes, thereby, making the process more efficient and secure, while also improving health & safety standards. These facilities will be added in three more SBP BSC offices during the next year.

Further, a contract for 9 Banknote Processing and Authentication Systems (BPAS) was awarded in October, 2019 and their phased installation is expected to be completed by December, 2021. BPAS machines are capable of high-speed processing[3], authentication and online destruction of banknotes providing 100

[3] Approx.30 banknotes per second

percent counterfeit detection, processing accuracy, standardization, and significant HR savings in comparison to its manual counterpart.

It is expected that with the successful installation of 11 BPAS, SBP BSC's yearly capacity for processing and online shredding of higher denomination (Rs. 500 & above) banknotes will increase to 1.4 billion pieces. In addition, with the implementation of BDS, SBP BSC will be able to disintegrate more than 2.5 billion pieces of lower denomination (Rs.100 & below) banknotes on a yearly basis in a safe and secure manner.

SBP BSC has also installed 141 Countertop & Desktop Banknote Sorting Machines (CNS & DNS) across 16 field offices for counter operations and as a stopgap arrangement for back end processing until the installation of BPAS & BDS machines across SBP BSC offices is completed. These machines are playing a pivotal role in ensuring that only good quality and machine-authenticated banknotes are issued over counters at SBP BSC's field offices.

2.4.5 Government Savings Schemes

The management of Government Savings Schemes on behalf of Central Directorate of National Savings (CDNS) is another major area of SBP BSC's operations. SBP BSC is focused on modernizing the operations of these schemes to achieve operational efficiency in terms of time, cost and HR needs. A brief overview of various Government Savings Schemes is given as under:

2.4.5.1 National Prize Bonds

National Prize Bonds (NPBs) are bearer instruments available in seven denominations. The holder of these bonds is eligible for a prize in draws held on quarterly basis. Winning prize bonds are drawn by special children in presence of draw committee and general public attending the draw ceremonies.

The sale and encashment of these bonds is carried out by all SBP BSC field offices, authorized commercial bank branches and National Savings Centers across Pakistan. The draws of NPBs are held at nine (09) SBP BSC offices on quarterly basis as per schedule announced by the CDNS at the start of each year.

During FY20, decreasing trend in sale of prize bond and prize money payment was witnessed as various functions, such as sale of Government Savings Schemes was temporarily suspended as a precautionary measure to combat the COVID-19 pandemic.

Additionally, withdrawal of Rs.40,000/- denomination NPBs from circulation was another major factor for the decreasing trend. As on June 30, 2020, prize bonds of Rs.40,000/- denomination worth Rs. 236 billion (99%) have been successfully converted / encashed. Data pertaining to National Prize Bonds is elaborated in (**Table: 2.3)**

Table 2.3: Total NPB Sale & Encashment at SBP BSC field offices *(Rupees in millions)*

Denom	FY19				FY20				Outstanding Value Held by Public FY2020
	Sale	Encash-ment	Prize Money Payment	Net Sale	Sale	Encash-ment	Prize Money Payment	Net Sale for FY20	
100	1,256	307	841	949	467	370	731	97	10,286
200	2,600	1,021	2,426	1,579	953	1,205	1,746	(251)	29,340
750	14,514	2,733	8,957	11,781	6,492	2,596	7,356	3,896	107,344
1,500	15,763	3,308	9,468	12,455	18,054	2,971	9,009	15,083	123,248

7,500	23,568	4,784	9,063	18,784	6,609	2,784	8,611	3,825	106,457
15,000	34,704	12,669	15,489	22,035	13,009	16,575	13,969	(3,566)	172,554
25,000	27,501	13,476	14,894	14,025	15,824	12,404	13,760	3,420	164,048
40,000	34,446	76,417	25,858	(41,971)	-	191,403	9,018	(191,403)	2,398
Total	**154,352**	**114,715**	**86,996**	**39,637**	**61,409**	**230,307**	**64,200**	**(168,899)**	**715,676**

During last year, commercial banks were entrusted with the responsibility to accept prize money claims from general public on the behalf of SBP BSC to make the claim process convenient and efficient. The cited facility has received overwhelming response from general public as a total of 36,511 prize money claims valuing Rs.3.7 billion were received through commercial banks.

Moreover, in order to encourage low-income individuals to use digital payment modes and enhance financial inclusion, the SBP BSC has also introduced facility for payment of prize money and face value on National Prize Bonds (NPBs) through Branchless Banking Accounts.

Additionally, initiatives taken by SBP BSC such as direct credit of prize money and face value not only significantly improved the efficiency of public debt operations managed by SBP BSC, but also reduced dependency on cash.

2.4.5.2 Premium Prize Bonds (PPBs)

Premium Prize Bonds (Registered) Scheme is another savings scheme that is managed by SBP BSC. The PPBs are registered in nature and issued against Computerized National Identity Cards (CNIC) of the investor. This scheme is a step towards increasing documentation of economy as maintaining a bank account is mandatory for investment in this scheme. The Premium Bonds are eligible for both prize money (as admissible in the scheme) and profit payment as per rates notified by Government of Pakistan. The bi-annual profit and prize money (if any) are credited directly into the bank accounts of the investor and do not require personal visit for collection of profit or prize money. PPBs can also be purchased from six authorized commercial banks i.e. NBP, HBL, UBL, MCB, ABL & BAFL. A snapshot of the business conducted for Rs. 40,000/- PPBs in FY20 is given in chart below.

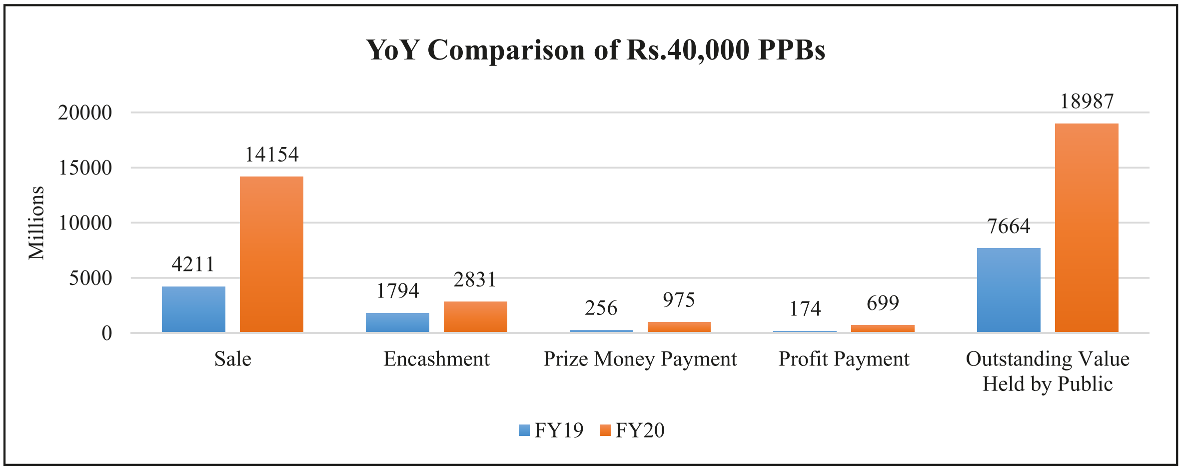
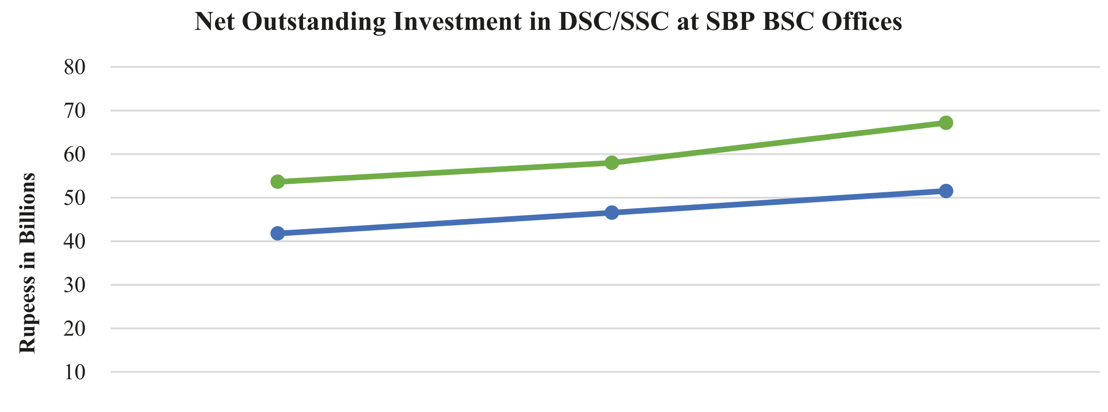


Figure 2.2 : Total PPB Sale & Encashment at SBP BSC field offices

2.4.5.3 Special and Defence Savings Certificates

Special Savings Certificates (SSC) Scheme, introduced by CDNS in 1990, has mainly focused on lower to middle-income investors who are in need of a steady income. These certificates are available in various denominations, starting from Rs. 500/- and going up to Rs. 1 million with a maturity period of three years. Defence Savings Certificates (DSC) Scheme, introduced in 1966 by CDNS, is a long-term investment option with a maturity period of 10 years. DSCs are available in various denominations, starting from Rs. 500/- with a maximum denomination of Rs. 1 million.

During FY 20, the net outstanding investment grew 11% YoY against SSC and 16% YoY against DSC to Rs. 51.5 billion and Rs. 67.2 billion respectively.



	FY 18	FY 19	FY 20
DSC	53,630,110,912	57,979,709,942	67,185,802,482
SSC	41,775,090,488	46,523,960,488	51,546,962,988

Figure 2.3: Net Outstanding Investment in SSC/DSC at SBP BSC Offices

2.4.6 Anti-Money Laundering and Combatting the Financing of Terrorism (AML & CFT) Compliance

In order to ensure mitigation of risks emanating from the menace of money laundering and terrorism financing, and ensure compliance of prevailing rules & regulations, SBP BSC has put in place a comprehensive AML & CFT regime in its dealing with external stakeholders. For this purpose, a dedicated AML & CFT Compliance Division was established in SBP BSC that is tasked with implementation of requisite actions stemming from the local and international regulatory requirements.

During the year, significant progress was made in strengthening AML & CFT regime in Government Savings Scheme operations. A comprehensive AML & CFT framework has been implemented in the operations of SBP BSC. The compliance regime includes customer identification, pre-screening under the United Nations (UN) Targeted Financial Sanctions Regime such as UNSCR 1267, 1373 etc., record keeping guidelines and reporting Currency Transaction Reports (CTRs) and Suspicious Transaction Reports (STRs) to the Financial Monitoring Unit (FMU).

In compliance with the NACTA guidelines and UNSCR & FATF Recommendation R-6, Sanction Screening has been implemented in core-banking system (T-24 system) for screening of proscribed / designated persons. All walk-in-customers are screened based on their unique national identification number i.e. CNIC / NTN which is checked against various sanctions lists issued by UN, NACTA, etc.

Additionally, all SBP BSC offices and HOK have been registered as reporting entities on FMU's goAML portal, whereby STRs and CTRs are being reported by concerned offices/departments to FMU.

Furthermore, SBP BSC is also currently working on enhancing the scope of the in-house developed Transaction Monitoring System (TMS) to assist concerned SBP BSC officials in monitoring the transactions and generation of alerts on the basis of pre-defined red flag indicators. On the customer identification / verification front, additional checks are being introduced to ensure a more robust and comprehensive system-based Know Your Customer (KYC) module. This shall enable SBP BSC to timely update customer profiles and carry out ongoing Customer Due Diligence (CDD) / Enhanced Due Diligence (EDD) exercise.

In addition to the above, SBP BSC is also taking the lead in procurement of an automated off-the-shelf targeted financial sanction screening solution, in line with international best practices

2.4.7 Initiatives to Tackle Spread of COVID-19 Pandemic

2.4.7.1 Policy Initiatives

As a socially responsible institution, SBP BSC took numerous special measures in response to the COVID-19 pandemic. In order to ensure business continuity in times of uncertainty, only critical currency management functions were carried out to ensure uninterrupted provision of services to government departments and commercial banks, whereas direct public dealing was minimized. In line with guidelines issued by Government of Pakistan (GoP) & World health Organization (WHO), detailed advisories were issued to SBP BSC Offices, commercial banks and Cash-in-Transit companies regarding:

- Maintaining social distancing protocols.
- Use of face masks, disposable gloves, disinfectants, hand sanitizers, etc.
- Ensuring minimal staff deployment.
- Screening for symptoms of all persons entering bank premises including employees, public, and representatives of banks/ Cash in Transit (CIT) companies.

Further, following initiatives were taken as a precautionary measure to curb community spread of COVID-19 pandemic through banknotes:

- Mandatory quarantine of banknotes received over counters by commercial banks and BSC Offices. Alternatively, disinfection of banknotes by commercial banks through Pakistan Council of Scientific and Industrial Research (PCSIR) certified cabinets/ machines.
- Feeding of ATMs with either fresh or ATM-fit re-issuable notes taken from BSC Offices.
- Disinfection and sealing of banknotes received from hospitals, clinics and pharmacies in commercial banks' own vaults. A total of Rs. 10.8 billion worth of same day balance sheet relief was provided to commercial banks by SBP BSC to facilitate banks in meeting these requirements.
- Suspension of 0.12% service charge on deposit of re-issuable banknotes to SBP BSC offices until June 2021, to facilitate banks in fulfilling quarantine requirements.

- Mandatory standardized packing with shrink-wrapping of bundles vide Banknote Packing Instructions for all denominations, as compared to previous instructions which only mandated the same for Rs. 100 and above denominations.
- Uninterrupted receipt of soiled banknotes from commercial banks and NBP Chests.

As is often observed during times of uncertainty, general public's reliance on cash remained high. As such, the currency in circulation witnessed a significant increase during the corona virus pandemic. The CIC increased by Rs. 635 billion (10.8%) from March 24 to June 30, 2020, compared to same period last year. Moreover, due to the quarantine requirements, commercial banks increasingly relied on SBP BSC offices for depositing their excess cash and withdrawing fresh/ re-issuable banknotes. Re-issuable balances deposited by commercial banks during the same period increased by 95 million pieces (194%) and Rs. 122 billion in value (168%). Similarly, payments of fresh & re-issuable balances to commercial banks increased by 37 million pieces (65%) and Rs. 290 billion in value (46%) compared to same period last year.

2.4.7.2 Ehsaas Cash Program

Complete support was also extended to ensure seamless cash disbursements through the Ehsaas Emergency Cash Program and cash payments of Rs. 89 billion were made to commercial banks specifically for the purpose.

2.5 Development Initiatives

2.5.1 Government Savings Operations

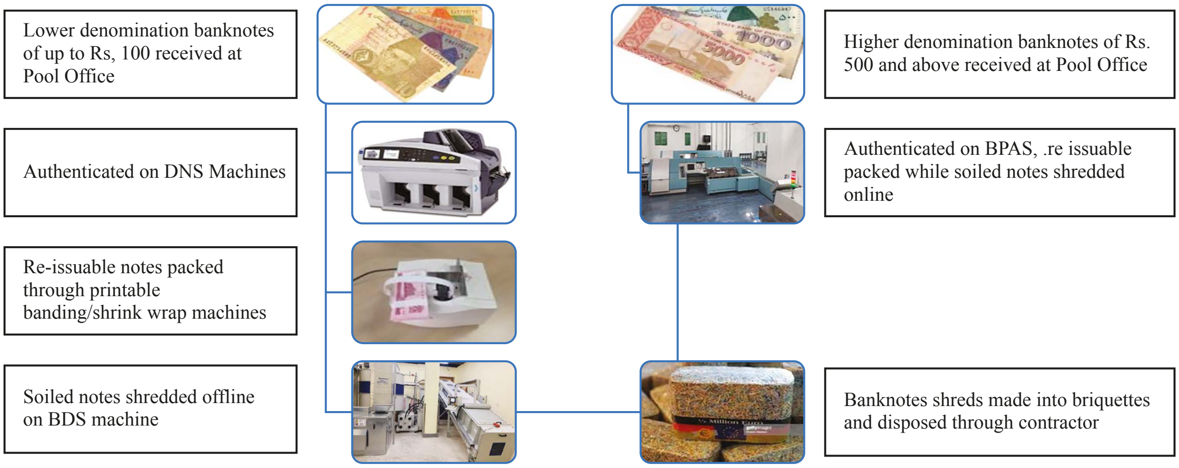
- Introduction of facility for payment of prize money and face value on NPBs through direct credit and Branchless Banking Accounts.
- Introduction of facility to claim prize money from commercial banks for facilitation of general public.

2.5.2 AML &CFT

Implementation of system-based screening of proscribed / designated persons in July 2019 to comply with AML Act 2010, ATA 1997, NACTA guidelines, UNSCRS and FATF Recommendations.

2.5.3 Currency Automation

- Award of Contract for supply of 09 Banknote Processing & Authentications Systems (BPAS) to be installed at SBP BSC Lahore, Faisalabad, Peshawar, Rawalpindi, Multan & Quetta in 2 years via phased implementation
- Successful installation of 04 Banknote Destruction Systems (BDS) at SBP BSC Lahore, Faisalabad, Peshawar & North Nazimabad
- Initiation of procurement of 03 additional BDS to be installed at SBP BSC Rawalpindi, Multan & Quetta



As per SBP's New Banknote Processing Model, the examination & destruction of banknotes shall be centralized to 7 Pool Offices, which shall be equipped with BPAS & BDS. The remaining SBP BSC offices, called linked offices shall only responsible for receipt of balances from banks and NBP chests.

Figure: 2.4 New Centralized Banknote Processing Model

2.6 Future Outlook

SBP BSC remains committed to evolve, upgrade and automate its currency and government savings functions in line with the changing business dynamics, country's economic situation and availability of technological solutions. To ensure inclusive, comprehensive and effective progress in these business areas, a detailed BPR exercise was carried out through review and analysis of end-to-end business processes. Opportunities for improvement identified in aforementioned exercise are expected to bring remarkable improvements in our processes besides accruing benefits for all our stakeholders. Some of these projects include:

- Modernization of banknote processing and elimination of manual banknote processing
- Automation/consolidation of currency accounting
- Establishment of model examination hall for consolidated banknote processing and destruction of lower denomination banknotes of entire south region (except Quetta)
- Restructuring of counter and vault operations
- Upgrading currency logistics and storage infrastructure at SBP BSC
- Implementation of banknote inventory management system, with the ability to bring all the disparate stakeholders in the cash lifecycle onto a single shared platform, and with real time track and trace capability

Additionally, SBP BSC will continue to pursue initiatives to further strengthening its AML, CFT and CPF regime in line with the applicable laws and international standards. Initiatives in this area includes;

- Real time screening of proscribed persons through state of the art sanctions screening solutions.
- Customer identification through reliable sources.
- Improved and effective documentation.
- Systematic monitoring and review of business transactions.
- Risk assessments and improving internal controls.
- Digitization drive to effectively transition from bearer instruments to registered instruments.
- Developing and introducing digital/scrip-less products with the aims to enhance of customer convenience, process improvement and international best practices while contributing to the national cause of improving AML, CFT paradigm of the country.

All such projects would not only leave a positive impact on existing structure of operations but will also enhance SBP BSC's capacity to monitor financial transactions, customer due diligence and STR reporting.