The Institute for Policy Reforms

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Economy caught in a slow-growth trap

Institute for Policy Reforms held an event in Islamabad to review the country's economic performance for the first quarter (July-September) fiscal 2014-15as wellas government's economic performance scorecard vis a vis objectives set in the 2013 elections manifesto. Dr. Hafiz Pasha former Finance Minister andDeputy Chairman Planning Commission gave a stimulating presentation. The event was well attended. IPR also released two reports,titled The Review for First Quarter 2014-15 and Economic Scorecard of the PML N Government in 2013-14 authored by DR. Hafiz Pasha.

Introducing the discussion, Chairman IPR, Mr. Humayun Akhtar Khan stated that the country's economic growth rate is a source of concern. For a number of years, economic growth has not touched 4%. In the first quarter too, there seems to be no improvement. It was expected that,upon assuming responsibilities, the Governmentwould address short-term measures to put the economy on firm footing and then launch a comprehensive plan for sustained economic growth. In the event, the government did neither. IPR analysis shows that while government has kept the fiscal deficit within target, growth has suffered. Manufacturing has been sluggish, exports have declined, and public and private investment was weak. It is curious that exports declined in a year when Pakistan became a beneficiary of European Union's GSPPlus scheme. The reasons are not hard to see. The Rupee appreciated significantly in the first half of 2014 and industry continued to suffer from power shortage. Last year, people were led to believe that electric power supply would normalize after Government settled the circular debt. In fact, load shedding has continued while tariffs have increased.

Mr. Humayun Akhtar Khan said that critical to growth and stabilityis increase in the tax to GDP ratio. Successive governments have been unable to do so. The present government has relied on domestic and external borrowingsoften at high cost. This also limits government's ability to take a long-term view for sustained growth.

Dr. Pasha presented an economic scorecard measuring government's performance for fiscal 2013-14 against key targets set in PML N's 2013 elections manifesto. The methodology took the manifesto's 2018 targets and computed benchmarks to be achieved in the first fiscal year. Of the 14 targets in the manifesto for which data is available, nine relate to the macro economy, two to efficiency improvements, and three to the social sector. At best, Government's performance was mixedagainst targets that it set for itself. Of the 14 targets, government achieved just one, that of reduction of budget deficit, a key IMF condition. Four indicators showed some improvement, but were well below target and another four did not change at all. These include growth rate of large-scale manufacturing, level of T&D losses in power sector, education spending as a percentage of GDP and the level of non-pension social protection spending as a percentage of the GDP.Five key areas show actual decline. GDP growth, rate of investment, and three unsurprisingly related to the electric power sector.

Reviewing economic performance, Dr. Pasha recognized significant stabilization of the economy in 2013-14 and infirst quarter. Balance of payments position had improvedhelped by a Fund programme. This government could not sustain the upward trend in foreign exchange reserves in the first quarter.

For fiscal 2014-15, Government set an ambitious growth rate of over 5% and foreign exchange reserves equal to three months import. However,"the outcome in the first quarter of 2014-15 has been somewhat disappointing," Dr. Pasha said. Agriculture production has been affected by the floods. All other sectors show sluggish progress. Large-scale manufacturing and electricity supply have seen slow growth (under three percent) while exports declined by over 5% in the first quarter. Investment too has been tardy. Private credit grew by just 5 billion rupees in the first quarter as opposed to 32 billion in the same period last year. PSDP releases were a particular concern with just seven percent of the budget spent in three months. It is not clear how government planned to deal with the uncertainties from both political developments and the "hiatus in the IMF programme." He hoped that the Fund's Executive Board would release the next tranche. International commodity prices have declined in recent months, but these were yet to transmit to domestic prices.

Tax collection remains a concern. First quarter receipts alone showed a shortfall of Rs.49 billion.Outlook on growth was uncertain. The economy was unlikely to achieve the targeted growth rate of 5%. He forecast a growth rate of 3.5 to 4% for the fiscal year. Public finances targets too were uncertain. Fiscal deficit target will worsen if tax collection continued to slip and the energy circular debt was settled. IPR forecasted a fiscal deficit of 5.5% to 6% of GDP higher than the target of 4.9%. BoP improvements were contingent on IMF's decision on the next tranche. If thatwas postponed again, the rupee value would decline despite increase in home remittances. Investment would also fall short of target at an estimated 14% to 14.5% of GDP.