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Annual Review of the Economy 2015-16

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About the Author

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About IPR

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Executive Summary

Fiscal year 2015-16 saw the economy make fiscal consolidation gains. A number of macroeconomic indicators improved.

- Economic growth rate increased.
- Fiscal deficit, current account deficit, and inflation remained under control. These place the macro fundamentals on an improved footing.
- For the first time in recent years, FBR achieved and exceeded the revenue target for the fiscal year. FBR's revenue for fiscal 2015-16 increased by 20% over the previous year. After reducing 8.7% for GDP and CPI, the net increase is a high 11.3%. Federal taxes increased overall to realize 99% of the target. Collection of Other taxes and Non-tax revenue were a challenge. In an encouraging development, government kept current expenditure in check and increased development spending. Debt servicing stayed within budget.
- Along with stabilization, the economy has seen some growth measures. Stable markup rate has created demand for private credit, which doubled in 2015-16. Industry has seen a hint of revival.
- It is important now to address structural issues of the economy. Public policy has yet to address such matters. There are fundamental issues that prevent the economy to achieve sustained economic growth on the lines of East Asia:

In order to grow, the economy must be based on two pillars:

- ➢ improved long term fundamentals, and
- ➢ higher level of productivity.

- Whereas some fundamentals have improved, the economy suffers from vulnerabilities. Pakistan has yet to correct the distribution between direct and indirect taxes. Public debt has increased rapidly with some external financing procured at high cost.

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- Pakistan's external sector is weak. Exports have fallen, FDI so far is low despite Chinese inflows, and remittances are in modest growth with a fear of it tapering with low oil prices. All of these combined will nearly double Pakistan's annual foreign exchange needs.

- According to IMF, in the next four years, Current Account Deficit will remain between minus 1.8% and minus 2.3% of GDP, FDI will remain low, annual external financing needs will grow from USD 7.3 Billion to USD 14.4 Billion, the ratio of short-term external debt as % of GDP will nearly double from 4.2% to 8%

- Higher productivity, the second pillar, comes from better infrastructure, upgraded skills, R&D, and improvement in governance to reduce transaction cost. So far we have not seen a major policy initiative to empower economic players and improve governance.

- The productive sector of the economy has yet to regain buoyancy:
  - Industry grew at 3.21% (the National Accounts gives it a 4.6% value) yet it grew at a slower rate in second half of the 2015-16 than in the first half. GoP has pinned its hope for industrial revival on increase in credit (based on low markup), and higher flow of overseas debt and equity (mainly from China). Share of manufacturing as a percent of total private investment has declined. Power generation investment will stimulate economic growth all around. However, there is not yet any change in policy to make the total power supply chain efficient. The resultant unpaid circular debt could be a constraint on power production. Other matters need attention. Despite representations from industry, government has not yet revived a dedicated private project finance window. In the past, DFIs played this role effectively. Nor does the capital market provide easy access to project finances.
  - In agriculture, major crops fell by 6.25%. This is a matter of great concern as there are likely structural issues at play. Little has been done to address water availability and its efficient use. In fact, federal investment in water has declined in the last two years. There are also policy concerns that led to decline in agriculture credit and low fertilizer offtake.
  - CPEC will help, but its cost and transparency issues will affect effectiveness.

- There is no indication yet of a surge in savings and investment. Their ratio to GDP were well below target level. The target for fixed investment was 16.1% of GDP. It declined from 13.9% of GDP in 2014-15 to 13.6% in 2015-16. Public investment was 3.8% of GDP and private investment fell from 10.2% of GDP in 2014-15 to 9.8% in 2015-16. Investment was 13.6% of GDP compared to its target of 17.7%. Savings remained at a sluggish 14.6% of

GDP falling short of its 16.8% target. Government creates negative savings and will do so in the medium term.

- While development expenditure has increased from the previous year, questions remain about project selection, transparent procurement, and effective project management. These issues reduce the returns to the economy from PSDP spending.
- To support growth, economic policy must review the political economy. It shows most obviously in tax policy, but equally in expenditure priorities.
- Our tax structure prioritizes indirect over direct taxes. This dampens demand and places burden on the economically weak. Delay in addressing this issue leads to high government debt and does not allow sufficient public investment.

The economy needs an urgent and effective response to the constraining structural issues.

Annual Review of the Economy 2015-16

The objective of this report is to review performance of the Pakistan Economy for fiscal 2015-16. It highlights achievements against targets set by the government and assesses how it affects future economic performance. We hope this will support decision making in public and private sectors.

1. Macroeconomic Targets

For fiscal 2015-16, the government had set the following targets:

- As per GOP's Annual Plan approved by the National Economic Council, the fiscal 2015-16 target for growth of Gross Domestic Product was 5.5%. Estimated growth rate for 2014-15 is 4.04%.

- GoP targeted a fiscal deficit of 4.3% of the budget, government. The IMF Staff Report for the ninth and tenth reviews have also projected the same rate (with slight increase to 4.4% after the 11th Review).

- The fiscal deficit target was based on control of current expenditure, especially through reduction in PSEs subsidy. Other contributors were a budgeted provincial surplus of Rs. 297 Billion and increase in total government revenue. For 2015-16, the target for total revenue was Rs. 4,313 Billion, an increase of 9% over revised estimate for 2014-15. Federal tax target for fiscal 2015-16 was Rs. 3,418 Billion. Of this, FBR revenue was estimated at Rs. 3,104 Billion, an increase of 19%.

- As another fundamental of macro-economic stability, the government set a target of 6% for inflation in fiscal 2015-16. This was based on prudent fiscal and monetary policies. The budget expected moderate government borrowing and reduction in public debt from 62.9% of GDP at end June 2015 to 60% of GDP by June 2018. IMF's corresponding estimates are much higher at 64.7% and 61.2% of GDP respectively.

- The government based its planned growth revival on improved macro-economic indicators and a surge in investment. CPEC projects, public and private, and low markup rates were to boost investment. The Annual Plan targeted total investment as a ratio of GDP at 17.7%. The target for national savings was 16.8% of GDP.

- With respect to the external account, Forex Reserves were targeted at 19 Billion US Dollars. The target for the current account deficit was 1 % of GDP. The Annual Plan estimates for increase in exports and imports were 5.5% and 6% respectively over revised estimates for preceding year. It estimated FDI to grow to USD. 3.3 Billion from the revised 2014-15 estimate of USD 991 Million. The target for home remittances was USD 18.9 Billion up from USD 17.9 Billion 2014-15 revised estimate.

- Exports were estimated to grow to USD 25,547 Million and inflow of foreign direct investment was to be USD 3,344. The current account deficit was set at USD 2,891Million

2. Economic performance

GDP growth rate: The National Accounts gives a growth rate of 4.7% for the economy for fiscal 2015-16[1]. Industry contributed 1.4%, services 3.35%, and agriculture minus 0.04%. Evidently, the services sector has fueled growth with the productive sector still lacking dynamism.

Industry: Industry contributes about 19% to the GDP. Within this, LSM, construction, and power and gas supply have a combined share of 15% of GDP.

The target for large scale manufacturing was 6%. According to the Pakistan Bureau of Statistics it grew by 3.21%[2] (the National Accounts give it a 4.6% value) for fiscal 2015-16. Though this is an improvement from the previous fiscal year, 2014-15, it is hard to confirm that LSM is in revival. LSM growth of 3.21% for the year is actually below the six-month growth (July-December 2015-16) rate of 3.9%, which suggests that its growth eased in H2 compared to the first half of fiscal year. Industries with the most weight in the Index saw modest or negative growth. Textiles and food and beverages grew by less than a half percent each, while Coke and Petroleum products declined by 2.6%.

On a positive note, production in a number of industries, though with overall low weight in the Index, increased. These include automobile (on the back of higher auto financing), fertilizer, chemicals, rubber products, and pharmaceuticals.

There were significant declines in iron and steel products, wood products, engineering goods, electronics, and paper and board, see Table 1. Sugar production too fell marginally, by 0.68%[3]. Fiscal year 2014-15 had also seen a 7.75% decline over the previous year. The decline in wood products and paper and board would likely endure because of plant closures. Sluggish performance of industry finds reflection in exports.

Reflecting a lack of buoyancy in the productive sectors, exports declined by 12% during fiscal year 2015-16[4]. All major export groups registered a fall. For the period July-May 2015-16, textiles fell by 7.3%. Engineering goods fell by 16.8%, petroleum products by 75.3%, and chemicals by 18%. Food group and other manufacturing fell by 13% and 16% respectively[5].

It is possible to revive industry with favourable economic policies[6]. There are already positive forces in place that they could reinforce. These forces include low world prices for key commodities and decline in cost of consumer financing and capital[7]. Improved gas

[1] Pakistan Bureau of Statistics, National Accounts, Table 1
[2] PBS, Quantity Index of Manufacturing
[3] Pakistan Bureau of Statistics, Quantum Index of Large Scale Manufacturing
[4] Pakistan Bureau of Statistics, Monthly Summary on Foreign Trade Statistics, June 2016
[5] Ministry of Commerce, GOP, Comparative Export of Selected Commodities for 2015-16 compared with 2014-15, May 2016
[6] IPR, Strengthening Stabilization and Economic Growth, Humayun Akhtar Khan, see discussion and recommendations
[7] State Bank of Pakistan, State of the Pakistan Economy, third quarter, Chapter 2, Page 16

supply helped increase fertilizer output. Public sector CPEC projects and other projects have given boost to construction. That in turn has and will raise demand for cement, steel, glass, and other industries. A large new caustic soda plant has increased chemical production. Pakistan Steel Mill's shut down reflects in decline in the steel industry, though private production of billets, and HR sheets and strips has increased[8].

The shortfall between target and actual growth in LSM is covered by growth of 6.8% in mining, 13% in construction, and 12% energy production. The national accounts perhaps saw a sudden surge in power and gas distribution, as growth for the nine months, January-March 2015-16, was 2% and 1.6% respectively[9].

Table 1
Change in Quantum Index of Manufacturing
July-June 2015-16 over 2014-15

Manufacturing Items	**Weight**	**% Change**	**YoY Growth Impact**
		Jul-June	**Cumulative**
Textile	20.915	0.42	0.12
Food, Beverages & Tobacco	12.370	0.92	0.19
Coke & Petroleum Products	5.514	-2.59	-0.17
Pharmaceuticals	3.620	6.54	0.52
Chemicals	1.717	8.13	0.20
Non Metallic Mineral Products	5.364	10.02	1.03
Automobiles	4.613	16.11	0.93
Fertilizer	4.441	13.81	0.77
Leather Products	0.859	7.76	0.15
Rubber Products	0.262	7.16	0.03
Iron & Steel Products	5.392	-9.85	-0.38
Electronics	1.963	-1.68	-0.03
Paper & Board	2.314	-1.58	-0.06
Engineering Products	0.400	- 14.43	-0.04
Wood Products	0.588	- 65.83	- 0.08

Source: Adapted from PBS QIM for June 2016

[8] SBP, State of Pakistan Economy, first quarter 2015-16, Chapter 2, page 21, Table 2.9
[9] PES 2015-16, Tables 14.2 and 14.3, pages 170 and 171, Statistical Appendix

Agriculture: Agriculture contributes about 21% to total GDP. Crops took a hit and fell by -6.25% in fiscal year 2015-16. However, the National Accounts show an overall decline in Agriculture of just 0.19%. Growth in forestry of almost 9% and in fish and livestock production filled the gap and mitigated the effect of decline in crop production. However, some of the National Accounts numbers seem counterintuitive. Forestry production has been in secular decline along with area under forest[10]. Likewise, other sources show that fish production has declined significantly in Pakistan[11]. These factors suggest that perhaps decline in agriculture production is greater than the National Accounts show.

More importantly, there are structural and policy matters at play that have contributed to the decline. 'Water availability was particularly low during Kharif'[12]. Despite higher production of fertilizer, Urea takeoff declined by 30%. Also, tractor production fell by 34% and disbursement of agriculture credit fell by 25%[13]. Policy issues also had an effect as in 'the disconnect between local and international prices of key inputs like fertilizers', which 'left a profound impression on the rural economy'[14].

Services: Services have a 59% share in GDP. All parts of the services sector have grown. According to the National Accounts, wholesale and retail sector grew by 4.6%, transport and storage by 4%, finance by 8%, and government services (increase in pay) by 11%[15]. Within wholesale and retail, production increase by industry and growth in import volume perhaps compensated for steep fall in agriculture and exports. Growth rate of transport, storage, and communications declined from last year. Telecom and broadband have recovered because of rapid growth in mobile 3G services[16]. Profitability of the financial sector improved.

Some economists have expressed doubt about growth rates announced in the national accounts[17]. IPR largely maintains the following opinion it shared in the review of MOF's Pakistan Economic Survey[18].

"IPR recommends that GoP review the National Accounts methodology. This is especially apparent in estimates for economic growth. This year agriculture production has taken a major hit and industry (although improving) has grown at less than the target growth rate. Power shortages continue unabated despite improvements on the margin. It is counterintuitive to see increase in overall growth rate from last year.

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[10] World Bank data, In Sq. KM, area under forest was 252 thousand in 1990, 211 thousand in 2000, and 167 thousand in 2010. Economic Survey of Pakistan 2015-16 shows decline in forest production from 472,000 sqm in 2000-01 to 354,000 in 2012-13 (latest year shown), PES Statistical Appendix, page 26
[11] PES 2015-16, Table 2.1 B, page 26, Statistical Appendix
[12] State Bank of Pakistan, State of the Pakistan Economy, third quarter, Chapter 2, Page 13
[13] PES 2015-16, Table 2.1 B, page 26, Statistical Appendix
[14] State Bank of Pakistan, State of the Pakistan Economy, third quarter, Chapter 2, Page 13
[15] PBS, National Accounts, Table 6
[16] State Bank of Pakistan, State of the Pakistan Economy, third quarter, Chapter 2, Page 23
[17] Express Tribune, Govt misses most critical growth target amid suspicion, 21 May 2016 and Think tank calculates GDP growth at 3.1%, 7 June 2016
[18] Pakistan Economic Survey Review, 2 June 2016, http://ipr.org.pk/wp-content/uploads/2016/06/Pakistan-Economic-Survey-2015-16.pdf

Let us first look at industry. While LSM has grown at 4.6%, below its target rate of 6%, growth in mining and power supply exceed targets. Also, for want of a better method, GOP approximates estimates for small scale and other industry. Their growth rates have not changed for years. Rates of 8.2% and 3.6% have no support in data. This is an endemic national accounting issue.

The growth rates for mining (6.8%), power supply (12.2%), and construction (13.1%) too seem high when compared with actual activity. According to the PES, mining index is at 179.9 in 2015-16 compared to 178.1 last year. Power supply grew by 10.6% (not 12.2%), but consumption of other energy was low. Oil consumption fell by 20% in 2015-16 and coal fell by 17%. Gas consumption grew by 6%.

The 5.7% growth in services too seems high. This is the part of national accounts whose accuracy is hard to ensure. Decline in agriculture production must translate to less activity in commerce and in transport. Also, while the Economic Survey shows over 11% growth in general government services, MoF shows a YoY growth of 6% in current expenditure. IPR recommends a review of accounting methods."

In its six-month review of the economy, IPR had cautioned that GoP will not achieve its 5.5% GDP growth[19].

Key structural factors constrain sustained economic growth in Pakistan. We can address them with accurate data, information, and through well considered policy. Using unconfirmed data to show high growth rates is counterproductive. The headwind that the economy faces include continued concerns about security, which, though improving, is unlikely to change radically soon. Weak governance, erroneous policies, social tensions, regional instability, and displaced persons continue to thwart economic activity[20].

In order to grow, the economy further needs:

1. Strong macro fundamentals
2. Enhanced factor productivity requiring:
    a. Investment in education, skills, and R&D
    b. Supportive governance
    c. Improved infrastructure

Government has successfully improved some macro fundamentals through fiscal consolidation. However, IPR sees high economic vulnerability as continued borrowing has increased indebtedness. Low government revenues and inadequate national savings forces the economy to source external debt. Traditionally, external debt funded development projects while government met current expenditure from tax and non-tax revenues, and from

[19] IPR, Six Month Economic Review, Page 5, http://ipr.org.pk/wp-content/uploads/2016/03/Review-of-the-Economy-report.pdf
[20] Discussion adapted from above report

domestic borrowings. Presently, a part of the external debt also finances current expenditure. This further adds to the economy's risk.

To meet government's plan to increase investment to 20% of GDP requires GOP to borrow 4.5% to 6% of GDP annually from external sources. At current GDP value, this means an additional USD 12 Billion or more debt per year. Without extremely concessional debt, this is unsustainable and most unlikely. Gross national savings have improved marginally from 13.7% of GDP in fiscal 2013-14 to above 14% in fiscal 2015-16. IMF estimates savings to reach 15.5% of GDP by June 2020.

Government has no known plan yet for improving factor productivity. Investment in education and skills have not increased. Weak governance increases cost of doing business and causes inconvenience to the people. While public investment in infrastructure has seen some increase, better and transparent project management and selection would bring higher economic returns.

2A Investment

The level of investment in an economy determines present and future growth rates. The Annual Plan 2015-16 gives the government's macroeconomic framework. It sets a target of 17.7% of GDP for total investment with fixed investment at 16.1%. Public investment was targeted at 4.2% and private at 12.2%. The target for national savings was 16.8%[21]. With Pakistan's high capital output ratio, this level of investment cannot boost growth rates. As it turns out, the economy missed most of these targets.

Compared to the target of 16.1%, "fixed investment as a percentage of the GDP declined from 13.9 per cent in 2014- 15 to 13.6 per cent in 2015-16[22]." At 3.8% of GDP, public investment too was below its target. Private investment fell from 10.2% in 2014-15 to 9.8 per cent in 2015-16, well below its 12.2% target. National savings were a dismal '14.6 per cent of the GDP, falling short of the targeted 16.8 per cent, but increased from the revised estimate of 14.5 per cent in 2014-15.'[23]

The object of investment matters its much as its amount. A good predictor of future growth is not total investment, but the portion that goes to projects that yield a high rate of return. Elsewhere, this report raises the issues of project selection and weak procurement and management practices that reduces the impact of public sector projects.

With respect to private investment, its distribution among sectors is a concern. Investment in manufacturing as a share of total private investment has declined. The sector had a share of 22.7% in total private investment in 2006-07. This fell to 14.7% in 2015-16. Investment in manufacturing must revive to sustain economic growth and to create jobs[24].

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[21] GoP, Planning Commission, Annual Plan 2015-16, Chapter 1, Page 10, Annexure II
[22] Planning Commission, Annual Plan 2016-17, Chapter 1, Page 5
[23] Ibid
[24] Planning Commission, Annual Plan 2016-17, Chapter 1, Page 5, Table A, Distribution of Private Investment

Government recognizes this challenge. The above Annual Plan 2016-17 states that "The success of developing countries in achieving their target of growth is reliant on the level of investment in the economy. In this regard, the low rate of savings is an obstacle in achieving high level of growth and development, that is, target of 5.5 per cent GDP growth."[25]. We have yet to hear how GoP plans to address this challenge.

2B Import of Machinery

The trend of machinery imports indicates the industries and areas receiving capital investment. Total machinery imported amounted to USD 8.6 Billion, a growth of 16% from last year. Table 2 below gives the share of each sector and their growth from the previous year. Three areas saw major growth in import. These include electrical machinery, power generation equipment, and construction and mining machinery. With respect to share in total imports, the three major areas were power generation, electrical machinery, and telecom equipment. Import of power generation machinery of about USD 1,800 Million suggests a healthy increase of 1,800 MW in generation capacity. Textile machinery import saw a modest increase of 2.6%.

Table 2
Machinery Imports
July-June 2015-16
USD Million

	2014-15	**2015-16**	**Share in Total Import**	**Growth %**
Power Generation Machinery	1,375.3	1838.3	21.4	33.7
Office Machinery	398.1	328.3	3.8	-17.5
Textile Machinery	449.5	461.5	5.4	2.63
Construction & Mining	269.8	342.9	3.9	27.1
Electrical Machinery	1,205.5	1,806.7	21.0	49.9
Telecom	1,377.1	1,365.3	15.9	-0.68
Agriculture Machinery	104.4	85.1	0.9	-18.4
Other Machinery	2,237.2	2,371.5	27.6	6.0
Total	**7416.9**	**8,599.6**	**100**	**15.9**
Source: Trade Statistics, Ministry of Commerce based on PBS data[26]				

[25] Ibid Page 6
[26]

2C PSDP Releases

Unlike past years, when release of funds for projects were well below budget, GoP released most of the budgeted amount for fiscal 2015-16. In Rupees, government released 97%, almost the full amount allocated for projects. Foreign aid disbursed was 61% of the total[27]. Sectoral releases are in Table 3:

Table 3
PSDP Releases 2015-16
Rs. Billion

	Budget 2015-16	Revised Budget 2015-16	Releases 2015-16	% Released
HEC	19.9	20.7	20.4	98.5
Health	20.7	25.6	25.1	98.2
PAEC	30.4	41.9	38.1	90.9
Railways	41.0	26.3	25.8	98.2
Water Sector	30.1	32.4	30.2	92.2
NHA	159.6	159.6	111.9	70.1
Power	113.9	122.8	114.1	95.8
Others	284.4	270.7	263.2	97.2
Total	**700.0**	**700.0**	**628.8**	**89.8**

Source: Planning Commission, Status of PSDP Releases
Notes: Releases in PKR 97%, Disbursement of foreign credit 61%

It is unusual to see low release for roads and highways, which is a stated priority for the government. Roads also are a major part of CPEC's public investment and with top-level supervision, it is disingenuous to see the slow progress in this sector. Here too, the Rupee amount has been disbursed in full, though foreign assistance was a mere 25% of budget. This reflects either flawed budgeting or process issues with loan disbursing organizations.

Normally, releases do not necessarily mean that money has been spent. This year, however, almost the full amount has been spent. Actual booked federal expenditure is Rs. 594 Billion, which is 95% of the released of Rs. 628 Billion.[28] Economic growth and progress of project depend on actual expenditure. This is a major improvement from past years.

Public investment is important to increase economic productivity and to crowd in private investment. While it was encouraging to see a 29% increase in total federal PSDP budget (from Rs. 542 Billion in 2014-15 to Rs. 700 Billion in 2015-16), IPR has concerns with some of government's priorities.

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[27] Planning Commission, GoP, PSDP 2015-16, Status of Releases as on 30.6.2016. All data about releases in this section have been taken from this statement. Data about booked expenditure are from MOF's fiscal operations.
[28] MOF, Summary of Consolidated Federal and Provincial Budgetary Operations, 2015-16 (July December 2015), Table 4

Compared to last year, budget for higher education and national health services have reduced by 22% and 34% respectively. The water sector sees a 35% decline (30% revised estimates). These three sectors are important determinants of future growth. More importantly, they could defuse the time bomb posed by the youth bulge. Water scarcity could pose, in the coming years, a greater challenge to the country than power does at present. It has begun to affect seriously our agriculture. It would possibly increase friction among provinces.

Highways received a disproportionate increase of 46%. The economic return on grand highways projects is yet to be proven in Pakistan. Similarly, while IPR welcomes the 131% increase in allocation for the power sector, it is concerned that the exclusive focus of the increase is on two LNG power projects. The medium term economic viability of LNG power is still unproven. Many questions remain unanswered about its use for power.

For it to be an engine of growth, public investment needs well considered project selection as well as quality governance. They increase output and jobs, and help efficiency all around. However, overpriced public projects, with further cost and time overruns, and a high share of prestige projects reduce the impact of public investment. Regardless, increase in spending will reflect in short-term economic growth.

2D Bank Credit

Net assets of the banking system shows the credit growth in the economy. In FY 2016, net domestic banking assets increased by 12.89% to reach Rs. 1,349 Billion. While government preempted most of the credit, an encouraging sign was increase in private credit. The growth rate of private credit was 105% from Rs. 224 Billion in 2014-15 to Rs. 461 Billion in 2015-16. Private credit is used for both fixed assets and working capital needs. About half the credit went to fixed investment in a broad range of sectors[29].

Growth in government borrowing declined in 2015-16 although from a high base. In fiscal 2014-15, net government borrowing increased greatly by 185% to Rs. 933 Billion from the previous year. Compared to this, government borrowed an additional Rs. 847 Billion in fiscal 2015-16[30]. Gross government borrowing from scheduled banks was much higher at Rs. 1,335 Billion. This is 2.8% of GDP in additional borrowing. Stock of net government borrowing (domestic) on 30 June 2016 was Rs. 7.8 Trillion or 26% of GDP[31].

OMO injections by the State Bank of Pakistan continued to be high, as banks have borrowed far more than growth in their deposits (perhaps as an arbitrage to further lend to government at a spread). SBP has thus maintained overnight repo rate close to the policy rate. In fact, growth in deposits declined because of low markup on deposits[32].

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[29] State Bank of Pakistan, State of the Economy Q3, Chap1, Pg.4
SBP Open Market Operations, Reverse Repo (Injection), http://sbp.org.pk/ecodata/OMO-Inject-Hist.pdf
[30] State Bank of Pakistan, Provisional Data on Monetary Aggregates as on 26 August 2016
http://sbp.org.pk/ecodata/BroadMoney_M2.pdf
[31] State Bank of Pakistan, Provisional Data on Monetary Aggregates as on 26 August 2016
http://sbp.org.pk/ecodata/BroadMoney_M2.pdf
[32] State Bank of Pakistan, State of the Economy Q3, Chap1, Pg.4

2E Inflation

GOP's Annual Plan for 2015-16 targets a 6% inflation rate[33]. Based on fiscal consolidation measures, fall in international commodity prices, and a strong Rupee, inflation has been under control. Most inflation measures show a decline. Year on year CPI rose from 3.16 to 3.19 for fiscal 2015-16. For the same period, Sensitive Price Index fell from 1.12 to 0.74, and WPI rose from minus 1.97 to 0.24. In June 2016, core inflation that includes items other than food and energy was 4.6%. Despite stable prices, core inflation (non-food, non-energy) is higher than CPI, SPI, and WPI[34]. This suggests that overall demand in the economy has revived.

Within CPI, food inflation also declined. In June 2016, year on year food inflation was 1.2%. This was 2.4% in June 2015. Prices of different commodities showed a mixed trend, however. Prices of many vegetables declined as they did for wheat, cooking oil, and rice. Prices of pulses, tea, tomatoes, eggs, and potatoes, increased[35].

Inflation picked up from its low point of September 2015. This was because of a number of reasons. Government imposed regulatory duties on a wide range of items, increased tariff on gas, and relied heavily on indirect taxes to raise revenue. For now, the economy seems to have absorbed the price increase from taxes. Aggregate demand increased during 2015-16 as evident from the rise in core inflation. This is so perhaps because SBP kept policy rates low. Growth in construction and higher overall investments would likely keep demand high.

In its report for July-December 2014, IPR discussed the dampening effect on inflation caused by procedural and methodological reasons. They bear repeating. The methodological issues pertain to jerks in housing rent assessment that dampens the effect on monthly and quarterly CPI calculation. Inflation is underestimated also as PBS does not include fuel charge adjustments and the many surcharges in power tariff. This understates electricity tariff [36].

Table 4
July 2015-June 2016 Inflation and YoY Changes

Percentage

	Averages Changes %			YoY Changes %		
	2015-16	2014-15	2013-14	2015-16	2014-15	2013-14
CPI	2.86	4.53	8.62	3.19	3.16	8.22
SPI	1.31	1.74	9.30	0.74	1.12	6.24
WPI	-1.05	-0.30	8.15	0.24	-1.97	7.73

Source: Reproduced Table from PBS Monthly Review of Price Indices June 2016

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[33] Planning Commission, Annual Plan 2015-16, Page 9 (Annexure II)
[34] Pakistan Bureau of Statistics, Monthly Review of Price Indices, June 2016, Table 1 and Table 1.1
[35] Pakistan Bureau of Statistics, Monthly Review of Price Indices
[36] IPR, Six Month Economic Review 2014-15, Dr. Hafiz Pasha, Page 14, http://ipr.org.pk/wp-content/uploads/2015/03/IPR-six-Month-report-Final.pdf

Table 5 Inflation in Major Food Items, Commodities, and Services, June 2016 YoY		
	Weight in CPI	**Inflation %**
General CPI	**100.00**	**3.19**
Food Group	**34.83**	**1.24**
Wheat flour	4.16	**-0.17**
Rice	1.58	**-10.8**
Meat	2.43	**5.78**
Chicken	1.36	**-19.58**
Milk (fresh)	6.68	**3.5**
Cooking oil	1.75	**-7.05**
Vegetable ghee	2.07	**-2.19**
Fresh fruits	1.86	**8.57**
Pulses	***0.95**	**25.91**
Vegetables	****1.68**	**2.44**
Sugar	1.04	**4.12**
Tea	0.84	**10.3**
Cigarettes	1.39	**18.43**
Clothing and Footwear	**7.57**	**4.93**
Cotton cloth	1.73	**5.35**
Readymade garments	0.97	**6.47**
Tailoring	0.88	**7.68**
Housing, Electricity, Gas	**29.41**	**5.29**
House rent	21.81	**5.73**
Electricity	4.36	**2.84**
Gas	1.57	**9.9**
Health	**2.19**	**5.11**
Drugs and Medicines	1.27	**3.44**
Doctors' fee	0.59	**7.25**
Transport	**7.20**	**5.18**
Motor Fuel	3.02	**-12.26**
Transport Services	2.70	**-2.13**
Communication	**3.22**	**0.4**
Recreation & Culture	**2.02**	**1.4**
Education	**3.94**	**7.38**
Restaurants and Hotels	**1.23**	**5.69**
Misc. Goods and Services	**2.75**	**4.5**
Source: PBS, Monthly Review of Prices, Annexure A, June 2016		

3. Public Finance

Details of fiscal operations released by Finance Ministry show some positive signs:

- Budget deficit for fiscal 2015-16 is 4.6% of GDP marginally above the target of 4.3%[37]. FBR revenue increased during the last quarter and totaled Rs. 3.12 trillion (Rs. 8 Billion above its target of 3,104)[38].

- For the first time in recent history, FBR has not only achieved, but exceeded the revenue target set in the budget. This seemed likely throughout the year as FBR's year on year performance was significantly better than that in previous years. Tax collection for July-December 2015 was 19.8% over the same period last year and 18.5% for July-March 2015-16 over the comparable period. Increase for the fiscal year is over 20%.

- Budget estimate of Rs, 3,418 Billion for federal taxes for fiscal 2015-16 was 21.5% over last fiscal's actual collection of Rs. 2,812 Billion. Federal taxes collected for the year was Rs. 3,377 Billion, 99% of the budget. Total tax and non-tax revenue for the year was Rs. 4,080 Billion, 95% of the budget of Rs. 4,312 Billion.

- Budget estimate 2015-16 of Rs. 315 Billion for federal Other Taxes was 40% above last year's actual. Actual collection of Rs. 265 Billion is 84% of budget, though 18.5% above last year's collection[39].

- Federal non-tax revenues remained a concern during the year as also indicated in IPR's past reports. 2015-16 collections are 18% below the previous year. Non-tax revenue collected in 2015-16 totaled Rs. 703 Billion, about 82% of budget. Collection in all non-tax heads have declined[40]. Dividend and profits from oil companies have fallen with low oil prices. Also, profits from the State Bank of Pakistan have fallen. Collection was Rs. 192 Billion below the target of Rs. 895 Billion[41]. While government has mostly achieved targets for FBR and other taxes, this is a major shortfall with effect on overall budgetary balance.

- With respect to expenditures, total current and development expenditure remained within budget. Total expenditure budget for 2015-16 was Rs. 3,921 Billion against a budget of Rs. 4,451 Billion. Of this, current expenditure was Rs. 3,178 Billion and development (including others and net lending) Rs. 742 Billion (PSDP expenditure was Rs. 594 Billion against a budget of Rs. 700 Billion). Development expenditure picked up in the last quarter of fiscal year as implementation of CPEC road projects gather steam. As of 30

[37] Ministry of Finance, Pakistan: Summary of Consolidated Federal and Provincial Budgetary Operations, 2015-16
[38] Ibid
[39] Ministry of Finance, Federal Government Fiscal Operations, 2015-16, Table 4
[40] ibid
[41] Based on MOF information in Budget in Brief 2015-16 and Fiscal Operations 2015-16

June 2016, GoP released 97% of the Pakistan Rupee budgeted amount for fiscal 2015-16. Foreign aid disbursement fell short of budget.

- Current expenditure grew a marginal 6% during fiscal 2015-16 over the previous year. On the other hand, development spending grew by 19% percent during the year. This is a positive trend.

- Consolidated deficit for fiscal 2015-16 is Rs. 1,349 Billion (4.6% of GDP). Apart from shortfall in non-tax revenue, the annual estimate of 4.3% was contingent on provincial surplus of Rs. 297 Billion[42]. In effect, the provincial surplus was Rs. 141.6 Billion[43]. In 2014-15, provinces generated a surplus of Rs. 87 Billion. The combination of non-tax revenue shortfall and lower than estimated provincial surplus have forced the fiscal deficit to be slightly above target.

- Interest payment (debt servicing) remained within budget. Total servicing of domestic and foreign debt was Rs. 1,263 Billion against a budget of Rs. 1,279 Billion. An amount of Rs. 1,304 Billion was spent in this head during 2014-15.

- Subsidy for the power sector appears to be within budget because of low oil prices and surcharges imposed last year. However, there is almost Rs. 650 to 700 Billion in accumulated circular debt payments. These have to be liquidated at some point and will affect fiscal deficit. Subsidy for other PSEs did not decrease as government has yet to restructure and privatize them.

- Of the Rs. 1,349 Billion deficit financing, Rs. 370 Billion was from external sources and Rs. 979 Billion from domestic. Of this, Rs. 192 Billion comes from non-banking sources and Rs. 787 Billion from banks i.e. 80% of the total domestic financing of the deficit.

Tax policy is an issue not only as a public finance matter, but one that is also fundamental to the economy’s sustained growth. Indirect taxes are 62% of total FBR revenue and 64% of total federal tax revenue. Indirect taxes comprise 68% of the consolidated federal and provincial tax revenue. Such a high burden of indirect tax on the economy (12% of GDP) needs correction. Indirect taxes dampen demand and create anti-export bias.

There are concerns also about the direct tax. In an environment of wide scale tax avoidance and evasion, government’s reliance on Withholding Tax understandably has increased. In fiscal 2015-16, withholding tax contributed over 67% to direct taxes and 26% to total taxes[44]. This tax has been the most reliable source for government in its bid to raise direct taxes. Despite its advantages, withholding tax poses questions. It often acts as an indirect tax. It carries compliance cost for all businesses, though minimal for the government.

[42] MOF, Budget in Brief 2015-16 Table 6
[43] MoF, Pakistan: Provincial Government Fiscal Operations, 2015-16, Table 5
[44] SBP State of Pakistan Economy, Q3, Page 48

The issue of tax policy has been discussed extensively in the policy space in Pakistan, including in a number of IPR reports on economic policy. Pakistan's economic fundamentals cannot improve without addressing the political economy of tax policy. If not done, our economy will continue to rely on external savings. The economy will not have enough resources to invest in productivity enhancing services.

Consequently, government debt has increased and currently domestic and external debt finance current expenditure. On 30 June 2016, the federal government debt stood at Rs. 19,041 Billion[45] or 64% of GDP[46]. While, the level is not a grave cause for worry, it is important to note two developments. First, that government debt has grown rapidly in the last decade. Total public debt[47] was Rs. 6,126 Billion in FY 2008 or 49% of GDP. It was Rs. 14,318 Billion in FY 2013[48] or 59%[49]. In Rupee terms, it has more than tripled in eight years. Second, external debt as a percentage of total debt has declined in recent years from about half to one-third at present. External debt from multilateral and Paris Club sources is usually concessional (though they come with exchange risk exposure). However, in the last three years, Pakistan has incurred high cost debt from the capital market (details in succeeding paras).

During fiscal 2015-16, central government debt increased by Rs. 2,073 Billion. Of this amount, external debt increased by Rs. 643 Billion or 31%. By June 2016, total debt of the federal government stood at Rs. 19,041 Billion[50]. Table 6 below is a snapshot of government debt.

As stated in the foregoing para, external loans finance both current and development expenditure. This is not sustainable. In its 2015-16 Q3 State of the Pakistan Economy, SBP says, "During Jul-Mar FY16, net external borrowing financed a total of 22.1 percent of the budget deficit, compared to 13.1 percent in the corresponding period of last year"[51]. SBP further says that this was largely derived from issuance of Eurobonds in the international market. Pakistan's external debt, including IMF and forex liabilities reached USD 61.3 Billion by June 2016. Including PSE guaranteed debt, the total liabilities amounted to USD 62.6 Billion. Debt repayment is a worry for Pakistan. While MoF's Pakistan Economic Survey expresses satisfaction at sustainability indicators, concerns remain. Recent debt revaluation has decreased debt stock by USD 2.3 Billion (since then this benefit reversed by a billion to prove the fallacy of such an approach). Despite this, external debt as a ratio of foreign exchange earnings increased to 1.6 in 2015 from 1.2 in 2013[52].

Cost of credit obtained in recent years is high. Two Eurobonds of USD 1 Billion each floated in 2013-14 carry fixed interest rates of 7.25 and 8.25. Their maturity is due in 2019 and 2024

[45] SBP, Central Government Debt, July 2016, http://www.sbp.org.pk/ecodata/cengovdebt.pdf
[46] GDP of Rs. 29,598 Billion according to MOF, fiscal operations 2015-16.
[47] MOF defines public debt as "the portion of debt which has a direct charge on government revenues as well as the debt obtained from IMF is defined as public debt." Pakistan Economic Survey 2015-16, Chapter 9, Page 147.
[48] MOF, Pakistan Economic Survey, 2015-16, Chapter 9, Page 148, Box 1, MOF's public debt figure is usually marginally higher than SBP's figure for Central Government debt.
[49] MOF, PES, Table 1.5 Statistical Appendix
[50] SBP, Central Government Debt, July 2016, http://www.sbp.org.pk/ecodata/cengovdebt.pdf
[51] SBP, State of the Pakistan Economy Q3, Chapter 4, footnote on Page 47
[52] MoF, PES, 2014-15

respectively. Sukuk Bond of USD 1 Billion floated in 2014-15 is at 6.75% fixed. Similarly, USD 500 million debt incurred in September 2015 is at 8.25%[53].

In recent years, ratio of project aid has declined as a percent of total disbursements. This ratio shows the extent to which external aid is invested to generate future economic returns. In fiscal 2000-01, project aid was 47% of total. In 2009-10, it was 41%. In 2013-14, ratio of project aid fell to 29.5%.

All this suggests that if the economy proceeds on planned lines, Pakistan's need for foreign cash flows will increase rapidly. Quoting IMF, SBP says that "Pakistan's annual gross external financing needs (current account deficit, plus amortization on medium- and long-term debt, plus short-term debt at end of previous period) will rise to US$ 10.7 billion in FY17 and further to US$ 13.0 billion by FY20"[54]. IMF's Eleventh Review Staff Report estimates forex need of USD 14.4 Billion in 2019-20 and 15.4 Billion in 2018-19[55].

Table 6
Federal Government Debt

Billion Rs

	June 2015	**June 2016**	**July-June 2015-16**
Total Domestic Debt	**12,193**	**13,623**	**1,430**
Long-term	**7,583**	**8,622**	**1,039**
Market Loans	2.8	2.8	0
Federal Government Bonds	4,483	5,287	804
PIBs	(4,155)	(4,921)	(766)
Prize Bonds	523	646	123
Unfunded Debt	2,570	2,681	111
NSS	(2,417)	(2,526)	(109)
Foreign Currency Loans	5	5	0
Short Term	**4,609**	**5,002**	**393**
Market Treasury Bills	2.169	2,771	622
External Debt	**4,775**	**5,418**	**643**
Long term	4,672	5,241	(569)
Short Term	103	177	(74)
Total Federal Government Debt	**16,968**	**19,041**	**2.073**

Source: SBP: Central Government Debt[56]

3A Projections agreed with IMF for 2015-16 and the medium term:

Pakistan's extended funding facility with IMF ended recently. There is a macro-economic framework to move forward. If achieved, the agreed upon economic indicators will improve Pakistan's macro fundamentals.

[53] MOF, PES 2015-16, Table 9.5, Statistical Appendix
[54] SBP, State of the Pakistan Economy Q3, Chapter 5, footnote on Page 62
[55] IMF, Eleventh Article IV Review, Page 27, Table 5
[56] SBP, Central Government Debt, July 2016, http://www.sbp.org.pk/ecodata/cengovdebt.pdf

Table 7 compares budget estimates, IMF projections, and fiscal operations for 2015-16. The last column gives selected agreed indicators for fiscal 2020.

- IMF's Eleventh Review projection for federal tax revenue of Rs. 3,377 Billion is Rs. 41 Billion below government budget.
- For the medium term, fiscal 2019-2020, IMF projects increase in consolidated (federal and provincials) tax revenue from 12.4% of GDP to 14.4%.
- IMF also estimated a shortfall of Rs. 50 Billion in federal non-tax revenue for 2015-16. Actual shortfall in non-tax collection against budget is Rs. 176 Billion.
- There is no change in target of Rs. 3,104 Billion for FBR revenue, direct and indirect taxes combined. Actual FBR revenue was Rs. 3,112 Billion.
- Federal government's budgeted current expenditure was Rs. 3,166 Billion. IMF projected this at Rs. 3,402 Billion with higher estimates for subsidies and grants. Actual is Rs. 3,178 Billion, though with considerable circular debt in escrow.
- For the medium term, IMF projects total expenditure as percent of GDP to increase modestly from 19.6% of GDP in 2015-16 to 19.9% of GDP. It expects current expenditure to decline to 14.9% of GDP in 2019-2020 from 15.9% in 2015-16 and development spending to grow by one percentage point from 4% of GDP to 5% of GDP. A PSDP of 5% of GDP is inadequate for the development needs of the country. This is, however, a realistic projection given the present levels of savings and government revenue.
- The budgeted federal PSDP was Rs. 700 Billion. Provincial budgeted amount was Rs. 814 Billion to total Rs. 1,514 Billion. IMF's corresponding projections were Rs. 510 Billion, Rs. 530 Billion, and Rs. 1,040 Billion. Actual federal spending was Rs. 594 Billion, Rs. 592 Billion for provincial governments with a total of Rs. 1,186 Billion. For 2019-20, IMF projects total PSDP at Rs. 2,194 Billion.
- Government estimate for 2015-16 fiscal deficit was Rs. 1,328 Billion. IMF projected a lower number of Rs. 1,223 Billion. Actual deficit was Rs. 1,349 Billion. For 2019-2020, IMF projects a low fiscal deficit of 2.5% of GDP with a primary balance surplus.

Table 7
Summary of Public Finance
Budget 2015-16, IMF Projections, Fiscal Operations

Rs. Billion

	Budget 2015-16	IMF Projections 2015-16	Actual Fiscal Operations 2015-16	2019-2020
A. Revenue and Grants	**4,688**	**4,625**	**4,447 15.0%**	**7,636 17.4%**
Revenue	4,648	4,556	4,447	7,636
A.1 Tax Revenue	**3,729**	**3,643**	**3,660 12.4%**	**6,319 14.4%**
Federal	3,418	3,377	3,377	
FBR Direct Indirect Other taxes	3,104 (1,348) (1,756) 315	3,104 (1,284) (1,820) 273	3,112 (1,191) (1,920) 265	
Provincial	311	265	283	
A.2 Non-Tax Revenue	**963**	**913**	**787 2.7%**	**1,317 3.0%**
Federal	895	873	693	
Provincial	68	76	93	
B. Expenditure	**6,017**	**5,848**	**5,796 19.6%**	**8,734 19.9%**
B.1 Current Expenditure	**4,786**	**4,882**	**4,694 15.9%**	**6,539 14.9%**
Federal	**3,166**	**3,402**	**3,144**	
Interest Payments	1,280	1,289	1,263	
Defence	781	781	758	
Subsidies	138	165	NA	
Grants	410	616	362	
Others	557	551	761	
Provincial	1,620	1,480	1,550	
B.2 Development Exp & Net Lending				
PSDP	**1,514**	**1,040**	**1,186 4%**	**2,194 5%**
Federal	700	510	594	
Provincial	814	530	592	
Other Development	164		116	
Net Lending	58		13	
E. Fiscal Deficit % GDP	**4.3**	**4.3**	**4.6**	**2.5**
F. Financing Net	**1,328**	**1,223**	**1,349**	
External	346	493	370	
Domestic	982	730	979	
Bank Non-Bank	283 699	511 219	787 191	
Memorandum Item				
Nominal GDP		**29,598**	**29,598**	**43,888**

Source:
1. Pakistan revenue and expenditure from SBP State of Pakistan Economy, **2.** Federal revenue and expenditure from MoF, Budget in Brief, **3.** IMF Projects from Eleventh Review, Staff Report, Page 27 and 28, **4.** Actuals from MoF Fiscal Operations 2015-16, various tables

4. Balance of Payment

Declining exports, moderate growth in remittances, very low FDI, and increase in import of capital equipment and LNG, means that Pakistan's BoP is financed by external debt.

Exports declined by 12.4% for fiscal 2015-16 compared to last year. The decline was across the board in a wide range of products. Impact on the current account deficit from the drop in USD 3.1 Billion in exports was mitigated by a fall of USD 1 Billion in total imports, see Table 8. Exports fell by 12.1% and imports by 2.3%.

Exports are a big concern where both values and quantity declined. Key export items lost in export volume. This includes items in which Pakistan has been competitive such as cotton yarn, tents and canvas, art silk. Leather garments, gloves, and footwear also declined. Quantity of a number of food items reduced. They include sugar, Basmati rice, fish, fruits and vegetables. Exports of a number of products, which until recently appeared to have the potential for export diversification, declined. They include naphtha, molasses, plastic goods, and the emerging area of engineering goods.

This seems a structural issue at two levels. First, domestic issues are important. It would help to revisit international competitiveness of our export products. Equally, it is critical to study how to enhance factor productivity (an area that is hard for public policy to impact quickly). Pakistan may review too the current value of the Rupee against US Dollar. Exporters have lost out from Rupee value: from the appreciation of US Dollars against most other currencies, and because of adverse REER (many other developing economies have sharply reduced the value of their currencies). Second, for some years, world trade has fallen. It is important for policy makers to take note. Moderate GDP growth rates in China may not revive soon. These will affect medium term demand. So far, lower oil prices have not affected home remittances, yet that may happen. This needs attention.

Increased import of LNG and coal for power plants may burden future trade deficit of the country, even with low energy prices. Import of machinery will also likely to increase. However, trade deficit has somewhat improved. There is slight variation in data obtained from SBP and Ministry of Commerce. The former shows a decline of 5% in trade deficit while the latter shows 7%, (SBP takes actual cash flows). These minor changes may not take our eyes off the structural economic issues.

The Annual Plan sets a target of 1% of GDP for the Current Account deficit[57]. SBP data shows that with a current account deficit of 0.9% for the year the economy achieved this target[58]. Home remittance is an important external financing source for Pakistan. Home remittance received in 2015-16 was USD 19,919 Million. Last year's actual was USD 18,721 Million[59]. The country saw an increase in remittance of 6%. A significant part of remittances

[57] PC Annual Plan 2015-16, Page 95
[58] SBP Summary Balance of Payments as per BPM6 – July 2016, Page 2
[59] SBP Summary Balance of Payments as per BPM6 - July 2016.

to Pakistan is from oil dependent economies. Footnote 36 gives IMF's estimate of risk to home remittances from decline in oil prices. So far, the country seems to continue to attract remittances.

Table 8 Trend in Trade June July 2015-16 compared with 2014-15					
Commodity	**July-June 2014-15**	**Share in total export %**	**July-June 2015-16**	**Share in total export %**	**Change %**
Exports (**Million USD, %**)					
Food Group	4,563.4	18.4	3,990.5	18.3	-12.6
Textiles	13,453.9	54.1	12,455.8	57.1	-7.4
Petroleum & Coal	585.6	2.4	160.7	0.7	-72.6
Other Manufactures	3,850.9	15.5	3,230.0	14.8	-16.1
Chemicals and Pharmaceuticals	980.9	3.9	803.5	3.7	-18.1
Engineering Goods	224.2	0.9	189.8	0.9	-16.1
Others	8.1	--	---	--	--
Total	23,667	100	20,802	100	-12.1
Imports (**Million USD, %**)					
Food	5,027.8	10.9	5,389.0	11.9	7.2
Machinery	7,417.0	16.1	8,599.6	19.1	15.9
Transport	2,699.6	5.9	2,973.6	6.6	10.2
Petroleum	11,793.8	25.7	7,606.0	16.9	-35.5
Textile	2,561.7	5.6	3,146.7	6.9	22.8
Chemicals	7,494.9	16.4	7,226.8	16.0	-3.6
Metal	3,705.8	8.1	4,120.8	9.1	11.2
Miscellaneous	1,060.0	2.3	1,109.7	2.5	4.7
Others	4,065.4	8.9	4,592.8	10.9	12.9
Total	45,826.0	100	44,765.0	100	-2.3
Trade Deficit	**22,159**		**23,963.0**		
Source: Ministry of Commerce Statistics and PBS data					

In addition to decline in exports, the second weakness in the Balance of Payment comes from low FDIs. The Annual Plan targets USD 3,344 Million as FDI for 2015-16 more than three rimes the revised 2014-15 estimate of USD 991 Million[60]. Actual FDI received in 2014-15 was USD 1,580 Million[61]. FDI during 2015-16 fell a further 28% to USD 1,138, about one

[60] Ibid
[61] Ibid

third of original estimate[62]. The Annual Plan targets negative flows for portfolio investment of USD 800 Million. The negative flows were USD 329 Million.

Largely, external debt has sustained the BOP. For the year, 2015-16, public external debt increased by USD 6,683 Million. Of this, government debt grew by USD 4.8 Billion, $ 4.2 Billion long-term and $ 676 Million short-term. Government borrowing centres on increase from multilateral and bilateral sources (usually concessional), as well as from commercial lenders. During the year, IMF credit increased by USD 1.9 Billion and PSEs debt by USD 268 Million. Table 10 gives increase in external debt and liabilities for fiscal 2015-16. The country's total liabilities increased by USD 7,837 Million. Total stock of the country's forex liabilities stood at USD 72,978 Million.

Table 9
Government External Borrowing 2015-16

Million USD

Head	**End of year external debt stock**		**Increase in external debt 2015-16**
	June 2015	**June 2016**	
A. Public External Debt	**54,674**	**61,357**	**6,683**
1. Government	46,861	51,714	4,853
Long term	45,849	50,027	4,178
Short term	1,012	1,688	676
2. From IMF	4,103	6,043	1,940
3. Forex Liabilities	3,709	3,600	-109
B. Public Sector Enterprises	**2,482**	**2,750**	**268**
C. Banks	**2,286**	**2,725**	**439**
Borrowing	1,334	1,668	304
Deposits	952	1.088	136
D. Private Sector	**2,996**	**3,293**	**297**
E. Debt liabilities to investors	**2,702**	**2,853**	**151**
Total External Debt & Liabilities	**65,141**	**72,978**	**7,837**

Source: SBP[63]

On 30 June 2016, official net reserves stood at USD 18.1 Billion (against the USD 19 Billion target)[64]. Net foreign currency reserves were USD 13.5 Billion. This year's level is a substantial increase from the last year, though almost wholly sourced from credit. With declining exports and moderate increase in remittances, growth in FE has come from borrowings. At about seven month's imports, current official reserves are at an acceptable level. However, high borrowings have increased debt servicing needs. IMF estimated gross

[62] Op.Cit. 38
[63] SBP Pakistan's External Debt and Liabilities-Outstanding http://www.sbp.org.pk/ecodata/pakdebt.pdf
[64] SBP, LIQUID FOREIGN EXCHANGE RESERVES, September 2016

external financing needs to double from of USD 7.3 Billion in fiscal 2015-16 to 14.4 Billion in 2019-20[65] (SBP quotes IMF's 2019-20 estimate at USD 13.0). This is a major challenge for the sustainability of our external account that economic planners must address.

After remaining firm for two years, Rupee value declined during the fiscal year. It fell by over two percentage points in August 2015 and again one percentage point in October 2015. The Rupee began the fiscal year at 101.85 to USD 1[66]. It was Rs. 104.81 on 2 September 2016[67]. Clearly, the change in value has not done enough to boost exports though we must consider all competitiveness factors. While the Pak Rupee has lost value during the fiscal year, it has gained value since December 2103. It fluctuated between Rs. 105 and Rs. 108 against the USD in December 2013[68]. Consequently, its real effective exchange rate did not help our exporters.

Table 10
Summarized Balance of Payments Projections
USD Million

	Annual Plan 2015-16	2014-15	2015-16	Change
1. Current Account	-2,891	-2,627	-2,885	-258
Exports	25,547	24,083	21,961	-2,122
Imports	43,282	41,401	39,583	-1,818
Balance on Goods	-17,735	-17,318	-17,622	-304
Remittances	18,989	18,720	19,186	466
2. Capital Account	295	378	426	48
3. Financial Account	-7,246	5,004	5,687	683
FDI	3,344	852	1,385	533
FPI	-800	1,903	46	-1,857
Net Foreign Assistance	-922	893	4,237	3,344
Others		283	-196	-479
4. O&E		-119	-315	-196
5. BoP deficit/surplus	-4,497	-4,230	-4,830	-600
6. Use of IMF Credit		1,594	1,918	324
7. Change in FE Reserves		-2,636	-2,912	-276
Source: IMF[69]				

[65] IMF, Eleventh Article IV Review, Page 27, Table 5
[66] XE Currency Charts, http://www.xe.com/currencycharts/?from=USD&to=PKR&view=1Y
[67] SBP Weighted Average Customer Exchange Rates as on 2-Sep-16
[68] XE Currency Charts: http://www.xe.com/currencycharts/?from=USD&to=PKR&view=5Y
[69] IMF Eleventh Review Staff Report http://www.imf.org/external/pubs/ft/scr/2016/cr1601.pdf