INSTITUTE FOR POLICY REFORMS

IPR FACT SHEET

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Pakistan Economic Survey 2016-17

About IPR

Institute for Policy Reforms is an independent and non-partisan think tank established under Section 42 of the Companies Ordinance. IPR places premium on practical solutions. Its mission is to work for stability and prosperity of Pakistan and for global peace and security. IPR operations are supported by guarantees from the corporate sector.

State of the Economy

After three years of consolidation, the economy has missed most of its targets this year. It is easy to see why:

- This was the first year that the economy functioned without IMF's watchful eyes. (The EFF ended in September 2016).
- After limited recent success, GoP set vastly ambitious targets that cannot be met within the present policy framework. For example, after 20% increase in FBR revenue last year, the budget set a target of another 16% growth this year. GoP also reduced corporate tax rates.
- Most important, its balance of payments look especially weak.

It is no surprise that the economy missed most targets. What is surprising is that this happens each year and no one draws a lesson. The Pakistan Economic Survey 2016-17 gives us an overview of how the economy has done this fiscal. Below is performance of the headline indicators against targets approved by the NEC in Annual Plan 2016-17:

- GDP grew at 5.28% against a target of 5.7%. Industry, especially LSM rates were well below target.
- Fiscal deficit has already breached the target of 3.8%. It will reach about 4.5% end of year
- Government's total revenue will fall short by Rs. 500 to 600 Billion. FBR taxes will be about Rs. 120 Billion short. Target for total federal tax revenue was Rs. 4,916 Billion with Rs. 3,621 Billion for FBR taxes
- Current account deficit is USD 7.25 B by April 2017. It is expected to be USD 8.5 Billion by year end.

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- Exports were estimated to be USD 21.5 Billion, against a target of USD 24.75 Billion
- Workers' remittance will be USD 19.5 Billion versus the target of USD 20.2 Billion
- FDI will be USD 1.9 to 2.0 Billion against the target of USD 4.55 Billion

- Low savings and Investment affect growth:
  - Investment was 15.8% of GDP. Its target was 17.7 % of GDP
  - National savings was 13.1% of GDP against a target of 16.2%. Domestic savings was 7.5% of GDP. Both fell from last year.

- Inflation (CPI) was 4.09% YoY up to April 2017 against a target of 6%. WPI increased to 4% from -1.3% last year.

This Institute has time and again proposed a way forward with deep structural reforms, which could help them achieve those targets and more. The government has not made policy changes to improve long term growth prospects.

Economy's Performance:

GDP Growth Rate: The target growth rate of 5.7% was anchored on agriculture growth of 3.5%, industry 7.7%, and services 5.7%. Within industry, large scale manufacturing was targeted to grow by 5.9%. Actual corresponding numbers are: GDP 5.28%, agriculture 3.46%, industry 5.02%, and services 3.54%. LSM grew at 4.93%. The economy missed all growth targets. It almost achieved the target for growth in agriculture, but from a very low base in 2015-16 when production of major crops fell radically. The contribution to the GDP growth rate from the commodity producing sectors is 1.74%, of which 1.05% is from industry and 0.69% from agriculture. The rest 3.54% is from services. Growth needs a stable macro-economic framework. As we will see below, government has not even begun to think about it.

Without major reforms, the economy will continue to grow at moderate rates. There is no talk yet in policy circles on structural reforms. GoP must put in place structures to reduce cost of doing business. Economic policies reflect political choice. There is, so far, no effort to improve governance and discuss our grievous political economy.

Accuracy of GDP growth rates and other indicators:

For several years, IPR has questioned the method of estimating growth rates in the national accounts. PBS's assumptions increase GDP growth estimates.

Industry includes LSM, small scale manufacturing, others, mining, energy and power, and construction. LSM grew at 4.9%, below its target rate of 5.9%. Mining grew at 1.34% and energy and power supply at 3.4% against targets of 7.4% and 12.5%. Each year, GOP approximates estimates for small scale and other industries. Their growth rates have not changed for years. Rates of 8.2% and 3.6% have no support in data.

The 5.98% growth in services too seems high. This is the part of national accounts whose accuracy is hard to ensure. Services are produced mainly to help the economy's productive sector. The productive sector missed all targets, yet services bettered its targets. Industry and agriculture grew at 5% and 3.46% yet wholesale and retail trade has grown at 6.8% and finance and insurance at 10.77%. According to SBP, commercial bank profitability fell in first half 2016-17. Along with moderate increase in domestic production, export fell in value and were stable in volume. Though imports increased in volume, it is unlikely that this compensated for low domestic production and exports. Housing has grown by exactly 3.99% each year for several years and other private services at above 6%.

IPR recommends a review of accounting methods. It appears that the much-celebrated reorganization of government statistics organization has not achieved any result.

Fiscal Operations

Federal Government Revenue

Against a target increase of 20%, total federal revenue grew by 4.6% during July-March 2016-17 over the same period last year. Within this, tax revenue grew by 7.4%. FBR tax

Government Revenue
Comparison of Target with Actuals

Billion Rs.
%

	Actual 2015-16 Billion Rs.	Budget 2015-16 Billion Rs.	Growth C/B %	Actual July-March 2016-17 Bill. Rs.	Growth July-March 2016-17 %
A	B	C	D	E	F
Total Revenue	4,080	4,916	20	2,866	4.6
Tax Revenue	3,377	3,956	17	2,464	7.4
FBR Tax	3,112	3,621	16	2,260	7.5
Direct Tax	1,192	1,558	31	892	12.4
Indirect Tax	1,920	2,063	7	1,368	4.5
Other Tax	265	335	26	203	6.3
Non-Tax	703	959	36	402	-9.7

collection has grown by 7.5%, while direct tax collection grew by 12.4%. Their targets were 16.3% and 31% respectively. FBR revenue will be short by about Rs. 120 billion for the year. This is less than the concessions of about Rs. 150 Billion granted by GoP, including reduction in corporate tax rates. Effectively, FBR would have achieved its overall target after a 20% increase last year. Other taxes have grown by 6.3% during the nine months, against a target of 26%. Non-tax revenue fell by 9.7% compared to the last period. The target for its increase was 36%. Clearly, revenue estimates were overstated in the budget.

Forecast and shortfall for 2016-17

	Target	Projected	Shortfall
Total Revenue	4,916	4,350	556
FBR Tax	3,621	3,500	121
Total Shortfall			677

Fiscal Deficit

Target fiscal deficit was 3.8% of GDP for 2016-17. This target was breached by March 2017 when the deficit was 3.9%. It is almost certain that end of year deficit will be more than the target. IPR estimates it to be about 4.5%. The higher than estimated fiscal deficit is because of ambitious revenue and provincial surplus targets. Federal revenue is expected to be shy of the budget by about 12 to 13% and FBR by 4%. The budget estimated provincial surplus of Rs. 339 Billion for 2016-17. Surplus up to March 2017 was Rs. 137.5 Billion. It would have to increase by Rs. 200 Billion to reach the target.

Expenditure might help. It is expected to be Rs. 100 B or so below the estimate of Rs. 4,895 Billion for the year. It depends mostly on a. if debt servicing is due in the last quarter, b. if security needs increase, and c. if PSDP payments suddenly hike. Whatever the deficit, it is understated as there is a large unpaid liability of about Rs. 700 Billion of circular debt. Of this amount, about Rs. 400 Billion is current and the rest kept in Resource Corporation.

Inflation

Prices have picked up from last year, though will stay within the target rate of 6% inflation. CPI is 4.09% this year, up to April 2017, compared to 2.79% for the same period last year. WPI grew at 4% compared to -1.30% last year. Core inflation non-food non-energy has grown at 5.5%. For the next year, it is necessary to keep an eye on inflation. Currency in circulation grew times in first half 2016-17. Both government and private borrowings grew.

Government borrowing grew by 40%. Private borrowing grew by over 60%. Of this 57% of the loans were for working capital. Credit for manufacturing grew after a steep fall last year. Surprisingly, credit to power sector did not grow.

Balance of Payments

Current Account Deficit for July-April 2015-16 has worsened compared to last year. For July-April 2015-16, CAD was USD 7,247 Million. The balance was USD 2,378 for the same period earlier year. This is a decline of over 200%.

Exports of goods and services have declined for July-April 2016-17. Month on month exports have picked up since March 2017. It is to be seen if this trend builds up. Comparison with March 2016 is easy as exports bottomed out then. Pakistan has not adapted to the changes in world economy. Low growth in major economies called for measures to address competitiveness issues. In absence of such measures, exports have been adrift. This is a major concern with which GoP has not yet come to terms. In 2016-17, exports were 6% of GDP. Historically this ratio has been over 10%. It was 13.5% in 2002-03 and 10.3% in 2012-13. These are indicators of a serious secular decline. We have yet to see a policy response.

FDI is the other concern. It grew by 8% for July-April 2016-17 over the same period last year. Total FDI of USD 1,645 Million is still very low. GoP's FDI target for the year was USD 4,455 Million. FDI will be between USD 1.9 to 2.0 Billion. Pakistan must do something special to attract investment.

External Debt for July- March 2017-2017 has grown by over USD 2.7 Billion from July 2016. Total external debt reached an unprecedented 72.237 Billion. This does not include foreign exchange liabilities. Increase in commercial foreign debt has grown by USD 1,317 Million since July 2016. In addition, Eurobonds and Sukuk have grown by USD 1.0 Billion. These are high cost debt.

Gross foreign exchange stood at USD 17,453 Billion on 30 April 2017. This is about USD 2 Billion below the level of 19,446 Million on 30 June 2016. However, foreign reserves have significant debt component and have increased the economy's risk profile. Some of it is commercial borrowing at high cost. Since 2014-15, GoP has made substantial borrowing from commercial sources at a cost. Most of this debt is to pay back earlier loans.

Under-performance of energy sector

Energy shortage, especially uncertain power supply, has hampered industry and commerce. We would have expected government to take benefit from low energy prices and place the power sector on a sustained path. Overall, consumption of energy may have declined as seen by oil and coal use. According to the Pakistan Economic Survey power consumption fell by 2% during July March 2016-17 compared to the same period last year. Total consumption was 68,415 GWh in July-March 2016-17 compared to 69,545 GWh last year.

Social sector indicators

It was thought that social sector indicators would improve with greater autonomy and fiscal resources with the provinces. There is no or, at best, marginal improvements in social sector indicators. Human development is not just a moral issue. It stimulates growth. There can be no sustainable economic growth without it. The sector suffers from low public sector allocation. Low top level priority also suggests low monitoring. So, what finds the sector gets is often poorly spent.