Institute for Policy Reforms

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A budget full of promises

Finance Minister's budget speech was a mix of claims of economic success and promises of further growth. However, it was presented in the shadow of protests by farmers. The protests should not have been a surprise. They show the disconnect between economic policy making and realities of the productive sectors. This is stated in the report on Budget 2017-18 issued today by the Institute for Policy Reforms. Industry and agriculture need fundamental reforms to grow. The government responds with ad hoc measures.

A day earlier the Finance Ministry released the Economic Survey 2017-18, which showed several weaknesses in the economy. Considering these, government's claims of economic success sounded particularly jarring.

The Minister said that "sustained and inclusive economic growth" was anchored in successful completion of structural reforms. He did not list the specific reforms. In IPR's view, Government has not touched the structure of the economy or its political economy. By favouring indirect taxes over direct taxes, we continue with regressive taxation. Continued increase in public debt means that the whole nation pays for the profligacy of the few. The federal PSDP prefers to invest in highways over all other expenditure.

Let us first look at this year's framework in light of last year's outcomes. Fiscal deficit of 4.1% in 2017-18 would certainly be breached. An understated current account deficit does little to instill confidence in the numbers. FBR tax collection is estimated to grow by 14% and non-tax revenue by 7%. The real value of current expenditure has been kept at the level of 2016-17. However, expenditure increase on defence, subsidy, and development may force an increase in the total or a cut in PSDP. This year the cut on PSDP was 11%, which brought it down to Rs. 715 Billion from Rs. 800 Billion. Government will not achieve the estimate for provincial surplus.

Stabilization is no longer the goal. GDP growth rate is targeted to be 6% and inflation will be same as this year's 6%. However, some measures will stall growth such as withdrawal of exemptions on construction. The inevitable increase in government borrowing would affect credit available to the private sector. Government's savings and investment targets do not support growth. Public debt has reached 62.3% of GDP. GoP's promise last year to observe provisions of the fiscal responsibility law was forgotten. External debt is 23.4% of GDP.

The budget 2017-18 lists many initiatives for growth, especially for agriculture and textiles sectors, as well as for poverty reduction. Past record of such initiatives show that they have minimal effect. The report hoped the government will succeed this time.

Referring to measures to revive agriculture and industry, IPR states that even if these measures work, their contribution would be one off. The need was for long term efforts to build competitiveness and increase productivity. While reduction in input cost will help, agriculture suffers from neglect of water resources and management. The proposals for agriculture do not address the real issue of improving seeds and restricting virus. This year's PSDP provides Rs. 36 Billion for the water sector. This is 16% above last year's allocation, but still Rs. 10 Billion less than the allocation of 2014-15. Water must receive higher priority.

It is good to see a 25% increase in the development budget to Rs.1 Trillion from the original Rs. 800 billion. Two concerns remain, however. A massive growth in allocation for highways and for special schemes. The latter shows preference for ad-hoc spending. This does not connect with GoP's Vision 2025. Also, it politicizes the PSDP.

Funds for highways have grown by nearly 100% from Rs. 165 Billion to 320 Billion. About one-third of all development budget is for highways. The growth in allocation of the federal PSDP is an improvement, but at 3.3% of GDP is nowhere close to meet the large infrastructure and social deficits that constrain the economy. It was expected that with limited funds government would spend PSDP judiciously. Funds for the power sector have reduced from Rs.75 Billion in 2016-17 to Rs. 60 Billion in 2017-18. This is primarily for completion of the two LNG power projects. IPR would have preferred higher amounts for hydro projects. The PSDP does not at all address the two major constraints of transmission and distribution. CPEC projects get Rs. 180 Billion.

Take away items that logically belong to the current budget, such as settlement of IDPs and PM's youth programme, leaves a smaller effective PSDP. The number of projects have grown from last year's 813 projects. The report states that the budget offers more of the same with no strategic departure.