Institute for Policy Reforms
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A hurriedly prepared budget

"This is a budget with some realistic, some fanciful numbers, and more than a dash of electioneering." This was stated in the review of the budget 2018-19 by the Institute for Policy Reforms. Despite claims that the budget is a strategic breakthrough in economic policy, measures in the budget are tepid lacking a coherent strategy. The government takes credit for revival of GDP growth rates. However, several developments, such as recovery of world economies from the 2008 financial crisis, low energy prices, growth in world trade, improved security in Pakistan, and large-scale investment in infrastructure from China helped Pakistan's economic growth. Yet, despite these favourable developments, government has not placed the economy on a sustained growth path.

The economy's fundamentals are weak, especially its external sector with a runaway current account deficit. Government so far has no response on how it will manage the external account. Its estimate that imports will grow by just 4.8% is unrealistic.

For FY 19, government forecasts a growth rate of 6.2%. Fiscal deficit is targeted at 4.9% of GDP. GoP has clearly made a policy transition from stability to growth. This would change if the vulnerable external sector makes Pakistan knock on the doors of the IMF again.

With unprecedented growth in revenue in the last three years, FBR's performance has helped limit budget deficit. Revenue is targeted to grow by a further 12.7% in FY 19, despite widescale tax relief. The budget estimates 114% increase in non-tax revenues. We have to see if this is because of higher energy prices or GOP plans to increase the rate of petroleum levy.

Other aspects would negatively affect the deficit. The budget estimates a provincial surplus of Rs, 285 Billion in FY 19. This is very unlikely to happen. Actuals for several expenditure heads will exceed budgeted estimates. These include the minor increase in current expenditure, especially with increase in pay and pension, and need for PSEs subsidy. In fact, virtual closure of Pakistan Steel Mills and continued losses in PIA were avoidable. Power sector subsidy is still high. Line losses and less recovery of bills haven't improved in five years. Each new unit of power generated needs subsidy. The budget for markup payment seems below need, as central government debt has increased rapidly, and the share of high cost commercial debt has increased in borrowing.

All these will stress the fiscal framework and make it difficult to stay within the deficit target. In any case, the deficit does not include over Rs. 900 Billion in circular debt, which is a liability that must be paid.

To limit fiscal deficit, government has drastically reduced PSDP. Development expenditure has been reduced to Rs. 800 Billion, whereas defence has grown to Rs. 1,100 Billion. Also, there are signs that private investment is stable or declining. Machinery imports have declined and just 10% of bank credit for businesses go to fixed investment. Yet government expects growth rate to increase to 6.2%.

The macro framework also plans to reduce Net Public Debt from the present 70% of GDP to 63.2% of GDP. The budget does not say how this will happen, especially as budget deficit this year would likely be 5.5% and 5% or more next year.

Two recent developments hold promise, though their success is by no means guaranteed. National water policy could conceivably help with much needed policy and infrastructure interventions. The tax amnesty could begin a process of documentation of the economy. Overall to build economic dynamism, policy makers need to do a lot more to build competitiveness and productivity.

There are several concerns with effective use of PSDP, which is now a paltry 2.4% of GDP. Almost 25% of PSDP is for highways whose economic benefit is unproven. There is also a large component of discretionary special schemes totaling Rs. 232.5 Billion or a quarter of the development budget. This is nothing but politicization of development funds. In essence, the federal PSDP is Rs. 568 billion rather than Rs. 800 Billion.

The Pakistan economy has been in low to moderate growth for several years. The people of Pakistan expect jobs and economic activity to grow. Serious infrastructure gaps and social deficit constrain business development and depress living standards. They are important for providing stimulus to the economy as well as to enhance business competitiveness.