INSTITUTE FOR POLICY REFORMS

IPR REPORT

April 2018

Review of the Economy July-December 2017-18

About IPR

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Executive Summary

Pakistan's real economy is performing well with favourable signs for GDP growth rate, inflation, consumption, and private sector economic activities. Weak economic fundamentals, however, detract from this positive picture. Budget deficit will exceed target by a large margin, the current account deficit for the year will end at an unprecedented high. Pakistan is effectively in a debt trap where new borrowing is servicing past debt. Growth in imports and debt servicing means that Pakistan's foreign exchange needs are much above what is available. Both domestic and external debt are at an all-time high. Continued weak fundamentals will damage the real sector and reduce growth rate. It will soon impact welfare of the people. The longer we postpone addressing the real causes of the economy, the worse would be its effect.

While tabling this fiscal year's budget, GoP announced a combination of macro stabilizing and growth measures, to achieve its target GDP growth rate of 6% in FY 18. These measures included higher revenues and lower current expenditure, as well as increase in investment, especially through FDI from China and a large PSDP. As the fiscal year progressed government offered fiscal incentives to boost exports and increase production of agriculture and industry.

Actuals for the half year show growth rates approaching target. LSM has grown by 5.55%, just 0.8% off target. With a favourable monetary policy, demand has fueled production of consumer durables. Estimates for growth of major crops are favourable and half-year power supply grew by 11.8% over last year.

Yet, there are signs that this positive picture may not continue for long. Growth inducing machinery import declined by 3%, import of power generation machinery fell by 26% and construction machinery by 24%. So far, GoP had attributed the economy's runaway current account deficit to such imports.

Stock of private sector bank credit grew by 7% over June 2017 but declined in terms of flow for July-December 2017-18, compared to

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the same period last year. Just 10% of bank credit went to fixed investment. Government has also reduced PSDP envelope as well as the pace of release of funds. And each year, the economy misses its target for saving and investment impeding growth.

Already weak, economic fundamentals have worsened. This is especially because of the economy's inability to deal with the structural twin deficits. Fiscal deficit for half year was 2.2% of GDP against an annual target of 4.1%. It is expected to go up to 5.5% by year end. Fiscal operations show a primary budget deficit, meaning that government is borrowing even to pay markup.

Current account deficit is a particular concern. The deficit for July-February 2017-18 was USD 10.8 billion, 4.8% of GDP. It already exceeds the annual target USD 8.9 Billion or 2.6% of GDP. Trade gap was USD 19.7 Billion. Annualizing this eight-month data, suggests a current account deficit of USD 16.2 Billion for 2017-18, 82% more than the Annual Plan's estimate. PBS data shows imports for the half year grew by 20.4% and trade deficit by 24.3 %.

External debt has financed the current account. Total external debt and liabilities increased by USD 5,799 Million during the half-year 2017-18. Their stock stood at USD 83,092 Million in June 2017. They grew to USD 88,891 Million by December 2017. Government external debt, not including PSEs, increased by USD 4,408 Million during the first half of fiscal year. During first half 2017-18, the economy serviced USD 3.6 Billion in mark-up and principal. Of this, USD 2.8 Billion was for central government debt, 72% of budget. Ballooning foreign exchange obligations is a major risk for the economy.

Foreign exchange reserves came under severe pressure and fell by a large margin. In one year, between February 2017 and February 2018, net SBP foreign reserves fell by over USD 4.8 Billion down to USD 12.2 Billion or less than three months' import.

Larger issues lie behind Pakistan's perennially poor macro indicators. Its weak fundamentals are symptoms of a deeper malaise. An elitist economy has caused chronic social and infrastructure deficit, the true determinants of growth. This makes Pakistan permanently dependent on external savings to meet its foreign exchange needs. The economy is exposed to continuous loan rollover and re-pricing risks. In effect, the economy is in a debt trap, but successive governments have developed no exit plan. We face today the outcome of deeply flawed policies of decades. Decision makers are focused on macro numbers without concern for what drives those indicators. Governance has continued to worsen with government at all levels doing little to reduce the cost of doing business. These are the building blocks of a competitive economy. So far, there is not even a discussion on these matters.

To enhance the economy's repayment capacity, there must be sustained growth of GDP and of exports. That in turn needs higher savings and investment (including public investment). Inevitably, this will need higher imports, and more external capital. Breaking out of this circular logic that constrains the economy is government's challenge. The economy needs a combination of stabilization and growth policies with perhaps rescheduling of loans, where possible, and targeted sourcing of FDIs.

Government policy has been adrift and two months before the elections the economy is sliding deeper into a morass of its own making. The immediate cause of this lies in decisions taken five years ago. For years, this Institute cautioned about the impending finale, as an obviously overvalued Rupee encouraged imports and dampened exports distorting the economy. This was the time when GOP celebrated its performance based on cursory and casual reports by foreign media. It also received extensive exemptions by an ever-accommodating IMF. Regrettably, hubris, hyperbole and patting the self on the back are no substitutes for strategy.

Review of the Economy: July-December 2017-18

1. Targets:

GoP set the following macro performance targets for fiscal 2017-18, as announced in the Annual Plan 2017-18 and the annual national budget:

- GDP growth: The Annual Plan sets a target of 6% for GDP growth for fiscal 2017-18. The target for growth of industry is 7.3%, for agriculture 3.5%, and services 6%. Largescale manufacturing is targeted to grow by 6.3%[1]. Last fiscal, GDP grew by a rate of 5.28%[2].

- Fiscal deficit: The fiscal deficit target for the year is 4.1% of GDP. Despite a growth rate higher than last year, GoP targeted to keep the deficit within moderate limits, in line with its stated goal of fiscal consolidation[3]. In FY 17, fiscal deficit was 5.8% of GDP.

- Inflation: The Annual Plan sets a target of 6% for increase in CPI. This is against actual CPI growth of 4.1% for fiscal 2016-17[4].

- Savings and investment: Government's Annual Plan sets a target respectively of 14.6% and 17.2% of GDP for savings and investments. This is against actuals of 13.1% and 15.8% respectively for FY 17[5].

- Forex Reserves: The Finance Minister's budget speech targets foreign exchange at four months of imports, i.e. USD 16.3 Billion based on import estimated in Annual Plan FY 18[6]. Reserves on 31 May 2017 were USD 16.4 Billion[7].

- Public Debt: GoP planned to keep net public debt to GDP below 60%. In March 2017, it was 59.3%[8].

- Balance of Payments[9]

    - Current Account Balance: GoP's estimated a deficit of USD 8.9 Billion or 2.6% of GDP for FY 18. In FY 17, Current account deficit was USD 12.4 Billion or 4.1% of GDP.

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[1] GoP Planning Commission, Annual Plan pages 7 and 8
[2] PBS, National Accounts, Macroeconomic Indicators
[3] MoF Budget speech to National Assembly by the Finance Minister, Page 13
[4] GoP Planning Commission, Macroeconomic Framework, Page 8
[5] Ibid
[6] MoF Budget speech to National Assembly by the Finance Minister, Page 13.
[7] SBP, LIQUID FOREIGN EXCHANGE RESERVES
[8] MoF Budget speech to National Assembly by the Finance Minister, Page 13. Actuals from pages 76-77 of Annual Plan and 148-149 of Pakistan Economic Survey 2016-17
[9] Planning Commission, Annual Plan 2017-18, Pages 88, and 90 to 92

- Exports (fob): Target for growth in exports is 5.5% growth reaching USD 23.1 Billion against actual of USD 21.9 Billion in FY 17 (SBP Summary Balance of Payments).
- Imports (fob): Estimated import amount for FY 18 was USD 48.8 Billion or about the same as FY 17 fob import of USD 48.5 Billion (SBP figure).
- Remittances: The Annual Plan estimates growth of 3.5% to reach USD 20.7 Billion
- Debt Servicing: Budgeted amount for servicing and repayment of domestic and external public debt is Rs. 1,650 Billion (USD 15.7 Billion)[10]. Of this amount, budgeted foreign loan repayment was Rs. 286 Billion or are USD 2.7 Billion[11]

- Government based its planned economic performance on a combination of macro stability and growth measures. Announcing current fiscal's budget, GoP declared intention was to increase revenues, rationalize current expenditure, increase investment, especially through FDI from China, better access to finance, and fiscal incentives and stimuli for growth of exports, agriculture and industry production.

2. Economic Performance

The key determinants of GDP growth are industry, especially increase in LSM, agriculture, and services. We use import and credit data, investments/bank credit data, energy and power supply, construction, and mining activities to estimate of GDP growth is on track to achieve its target:

Industry

LSM grew rapidly by 5.55% in July-December 2017-18 compared to Jul-Dec 2016-17. Highest growth came from automobiles, iron and steel products, non-metallic mineral products, and automobiles, among others. Production of food, beverages and tobacco, fertilizer, and leather products fell. According to PBS, "industrial growth in the last two months (November and December 2017) decreased due to delay of cane crushing". Sugar production fell by 37.3% as compared to the same period last year. Food, beverages, and tobacco recovered rapidly in January. Overall, LSM growth during July-December 2017-18 has been healthy, though it is so far below the target of 6.3%[12]. Also, LSM growth has fluctuated. FY 18 Q1, YoY LSM growth was almost 10% (see Table 1).

According to SBP in Q1, "Significant contribution came from construction and consumer durables industries. A number of developments explain this performance, for example, better energy supplies (as reflected in increased availability of LNG and electricity), strong domestic demand, rising purchasing power and improved security situation.[13]" A liberal monetary policy also has increased domestic demand. This may change soon if prices of energy and other

[10] Converted at Rs. 105=USD 1, exchange rate at time of budget
[11] MoF Budget in Brief, Table 15
[12] Pakistan Bureau of Statistics, Quantum Index Numbers of Large Scale Manufacturing Industries (QIM) for December 2017 and January 2018
[13] State Bank of Pakistan, State of the Economy, First Quarterly Report for FY18, Pages 15 and 16

commodities (steel and copper) rise or as the economy shows the effect of correction in Rupee value. Higher prices coupled with rise in mark-up will dampen demand, especially as cost of consumer financing for autos and other durables increase. Proliferation of ride hailing services also have fueled auto sales. These are especially dependent on financing.

Lately, public and private CPEC spending has stimulated construction activities and consequently demand. Government has reduced PSDP spending by a minimum of Rs. 100 billion, though estimates of cuts vary[14].

What this points to is an endemic problem of competitiveness of industry that this Institute has brought to attention repeatedly. At present, GDP growth is determined by removal of negatives (such as improved power supply) or from cyclical changes (such as low prices). They do not result from the true drivers of growth in manufacturing that increase competitiveness, and raise productivity[15]. There is no progress yet on most of the indicators (listed in footnote 15) that are the true determinants of sustained growth. Without a comprehensive sustained growth strategy, there can be no long-term growth. Fiscal incentives to boost tired 'infant' industry is no policy.

Chinese public and private investment will stimulate manufacturing. Their positive effect on the economy will increase if government couples this investment with structural reforms and improved governance. The economy also awaits how GoP's SEZs and industrial parks' plans, under CPEC, unfold. A lot would depend on their location[16], support services, logistics, their overall management, and success in targeting "backward" industries of China and other economies that are a step or two above the technology level in Pakistan. Thus far, there is little on ground work to indicate its likely success. World experience shows that success of SEZs is not a given. Significant complementing effort is needed. China's vast experience with SEZs would be guide. We must draw lessons also from our own EPZA experience and why it failed.

[14] National Assembly Secretariat "Questions for Oral Answers and Their Replies", 16 March 2018, pages 10 and 11, reply by Planning Minister. Also, many news reports.

[15] There are many ways to list these. The list to follow is from World Economics' Forum in collaboration with Deloitte Touche Tohmatsu Limited "Manufacturing for Growth Strategies for Driving Growth and Employment", Page 9: Talent-driven innovation, Economic trade, financial and tax system, Cost of labour and materials, Supplier network, Legal and regulatory system, Physical infrastructure, Energy cost and policies, Local market attractiveness, Government investments in manufacturing and innovation. Another good source is World Bank's Growth Report, lead writer Michael Spence. Please also see IPR's Re-engineering Economic Structure, March 2017.

[16] The two governments have agreed on nine locations, of which China has prioritized three: Rashekai, Faisalabad, and Dhabeji. Source: Planning Commission CPEC Secretariat.

Table 1
Change in Quantum Index of Manufacturing
July-December 2017-18/2016-17

Manufactured Items	Weight	% Change	YoY Impact
		July-December 2016-17	Cumulative
Textile	20.915	0.55	0.16
Food, Beverages, & Tobacco	12.370	-0.27	-0.05
Coke & Petroleum Products	5.514	8.14	0.53
Pharmaceuticals	3.620	3.63	0.32
Chemicals	1.717	-0.40	-0.01
Non-Metallic Mineral Products	5.364	10.23	1.18
Automobiles	4.613	21.86	1.53
Fertilizer	4.441	-9.84	-0.65
Leather Products	0.859	-5.93	-0.09
Rubber Products	0.262	5.92	0.03
Iron & Steel Products	5.392	37.13	1.40
Electronics	1.963	50.46	0.87
Paper & Board	2.314	8.84	0.32
Engineering Products	0.400	4.20	0.01
Wood Products	0.588	-19.22	0.00
			5.55

Source: Based on PBS QIM for December 2017

Agriculture

Production of major crops recovered during the period, with increase in production of all major crops compared to last year. Except cotton, production of all major crops will exceed GoP's target for FY 18, with sugarcane reaching unprecedented production level. While cotton production estimates show an increase of about 15% at 12.6 Million bales, it is still below the level of almost 14 Million bales achieved in 2014-15.

The aggregate of cotton, rice, and sugarcane has a share of 56% in total major crop production. Wheat also

Table 2
Major Crops Production, Yield, Area
FY 18

Crop	Share in major crops %	Area Hectares Million	Yield	Production Million Metric Tons Cotton, Million Bales			
				FY 17	Target FY 18	Estimated FY 18 SBP	Estimated FY 18 USDA
Cotton	21.7	2.5 to 3.0	778 KG/H	10.7	14.0	12.6	12.3
Rice	12.4	2.7	4.0*T/H	6.8	6.8	7.4	7.2
Sugarcane	14.3	1.3	60.5 T/H	73.6	68.5	79.3	--
Maize	11.2	1.3	4.6 T/H	6.1	5.6	6.1	6.0
Wheat	--	9.05	2.93 T/H	25.6	--	--	26.5

Source: USDA World Crop Production data and SBP, State of Pakistan's Economy, Q1 FY, Page 14, Table 2.1, *substantial difference in yield between SBP and USDA data. For rice, SBP estimates a yield of 2.5 T/H

contributes about 2% of the country's GDP. Growth in agriculture production will help the economy move towards achieving the target GDP growth rate.

Government's 6% target for GDP growth rate is in part based on growth of 3.5% in agriculture, which is expected to achieve the 3.5% target. In addition to crops, PBS counts livestock, forestry, and fishing in agriculture estimates. Data on these is less than robust and given to estimates, which puts to question the accuracy of PBS' overall economic data.

Production estimate data is substantiated by figures for fertilizer off take, release of water, and disbursements of agriculture credit. It is encouraging to see production growth, in part, result from increase in yield per hectare.

Yet, the improvement is marginal and Pakistan's crop productivity is well below those in China and East Asia. For some crops, yield is lower than those achieved in India and Sri Lanka. In addition to low productivity, volatility too is endemic. Production remains contingent on international prices, weather conditions, and virus. Without investment in water infrastructure, improvement in water use and service delivery, and appropriate research, extension services, and policy interventions, growth of farm produce remains uncertain. Adequate research does not exist. There isn't enough analysis on why production levels vary year to year.

Power supply

Despite improvement, power supply was again a constraint on economic activity. For the period July-December 2017, total power supply was 61,849.7 GWh[17]. This was a healthy 11.8% higher than the power supply of 55,324 GWh for the same period in 2016. Government's plans for increase in generation capacity have begun to show in more production. Continued, though declining, import of generation equipment suggests that capacity will continue to be added. Whether addition to generation capacity is enough to ensure reliable power supply in the country is open to question.

Numbers for FY 16 of billing and recoveries by DISCOs show no improvement in reduction of line losses and aggregate technical and commercial losses[18]. This reflects on the quality of DISCO level governance, which despite low oil prices, is the key reason for circular debt. With more than a quarter of sales that remain unrecovered, leads to accumulation of circular debt, which in turn hobbles generation as it creates financial disruption for producers (see Table 3). It also prevents private sector participation in generation.

Table 3
Line losses and less than billed amount received by DISCOs FY 16

	Units Purchased GWh	Units Sold GWh	Line Losses GWh/%	Amount Billed Rs. Million	Amount Received Rs. Million	Amount unrecovered Rs. Million %
PEPCO	93,815.8	76,430.8	17,385.0 18.53%	955,291.6	902,556.7	52,735 5.5%
K Electric	17,304	12,864	4,440 25.7%	209,687.0	183,767.0	25,920 12.4%
Total	111,119.8	89,294.8	21,825 19.6%	1,164,978.6	1,086,323.7	78,655 6.8%

[17] NTDC data
[18] NEPRA

Resultantly, government is forced to give extremely liberal incentives to IPPs. This means Pakistan has an endemic problem of short supply of power despite unreasonable prices. In addition to circular the system is also constrained by underinvestment in transmission and distribution. Though government has invested in transmission lines, it is not clear if this is enough to create a reliable T&D system.

2B. Investment

The Annual Plan sets a target of 17.2% of GDP and 14.6% for total investment and national savings in fiscal year 2017-18. Each year the economy misses the savings and investment targets. So, the Annual Plan FY 18 has rightly reduced its estimates for the year. It is still above last year's actuals of 15.8 and 13.1% of GDP for investment and savings respectively[19].

2C. Import of Machinery

Machinery grew by double digits in the last two fiscal years. However, it declined by 3.3% during July-December 2017 over the same period previous year. Import of power generation machinery fell by over 26% during the period. Import of office and construction and mining machinery also fell (Table 4). According to SBP, flow of credit to private sector for energy sector declined by 45% in October-December 2017-18[20].

Table 4
Machinery Imports
July-December 2017-18

USD Million

	2016-17	2017-18	Growth %
Power Generation	1683.5	1243.7	-26.13
Office Machinery	258.1	236.6	-8.33
Textile Machinery	258.8	287.6	11.14
Construction & Mining	250.6	190.3	-24.09
Electrical Machinery	962.6	1069.8	11.15
Telecom	660.0	739.6	12.06
Agriculture Machinery	52.1	50.0	-3.90
Others	1545.3	1677.0	8.52
Total	5,671.0	5,494.6	-3.11

Source: Trade Statistics of Ministry of Commerce

[19] GoP, Planning Commission, Annual Plan 2017-18 data
[20] SBP, Quarterly Performance Review of the Banking Sector, Q4 CY17, Table 2: Sector-wise Advances Flows, Page 6

Since 2014-15, Pakistan has imported power generation machinery of about USD 7 Billion. According to CPPA/NEPRA, in December 2017, total dependable capacity stands at 29,444 MW. Dependable capacity is about 90% of installed capacity, which suggests present installed capacity of about 32,000 MW. NEPRA's State of the Industry Report 2016 gives total installed capacity of 25,374 MW as of December 2016 and 23,702 MW in 2014 (before CPEC began)[21]. It appears that Pakistan is on track to increase power generation by 13,000 MW by 2020 (10,700 MW under CPEC and 2,400 MW LNG), if the decline in power equipment does not become a trend[22].

2D. PSDP Releases

The pace of PSDP spending has declined. PSDP releases up to 9 March 2018, over eight months into the fiscal year, are 55.7% of budget. These include all releases, including foreign assistance[23]. Releases up to 9 March 2018 should have been close to 70%. With weakening macroeconomic indicators, government has reduced pace of releases. It has also revised PSDP envelope to Rs. 900 Billion from Rs. 1,000 Billion for 2017-18. Table 5 also gives selected sectoral releases. Release of funds for roads and motorways is highest. This is a stated priority of the government. Roads also are a major part of CPEC's public sector programme. On the other hand, releases for health is low at 17%.

Releases do not necessarily mean that money has been spent. There is time lag between release and booked expenditure and therefore variance with information compiled by Finance Ministry. Against total release of Rs. 557 Billion, booked amount is Rs. 248 Billion[24].

Public investment in infrastructure has grown, though we would like it to be based on judicious selection of projects with high economic returns. Public investment is important to increase economic productivity and to crowd in private investment. While it is encouraging to see a 25% increase in total federal PSDP budget this fiscal (from Rs. 800 Billion in 2016-17 to Rs. 1,001 Billion in 2017-18, since reduced to Rs. 900 Billion), IPR notes flawed government priorities.

Water sector is a special concern. The sector needs essential and urgent policy and investment intervention by government. Against this year's budget for water sector of Rs. 36.5 Billion, the sector had Rs. 43.5 Billion in 2014-15. From being water stressed, Pakistan is emerging as a water scarce country. This could pose a greater challenge to the country than power did until now. It has begun to affect seriously our agriculture. It could likely lead to friction among provinces as well as with neighbouring countries. A critical sector is denied due allocation. Together with health and education, the three sectors are important determinants of growth and productivity. More importantly, they could defuse the time bomb posed by the youth bulge.

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[21] NEPRA State of Industry Report 2016, Table 4, Page 107
[22] Initial plan under CPEC was to add 10,700 MW capacity. Since then, government claims 17,000 MW under CPEC, see Business Recorder 4 April 2018, CPEC to add 17,000 mw to national grid
[23] Planning Commission, Status of PSDP Releases, 9 March 2018
[24] MoF, Fiscal Operations July-December 2017, Table 4

This contrasts with disproportionate increase in allocation for highways. The economic return on grand highways projects is yet to be proven in Pakistan. For it to be an engine of growth, public investment needs well considered project selection as well as quality governance. Public investment increases output and jobs as well as helps efficiency all around. However, public projects at inflated costs, with further cost and time overruns, and the presence of prestige projects in the portfolio, reduce economic impact.

Table 5
PSDP releases 2017-18

Rs. Billion

	Full Year Budget 2017-18	Releases 2017-18 As on 9 March 18	% Released
HEC	35,662.8	18,945.9	53.1
Health	48,701.5	8,373.2	17.2
PAEC	15,085.0	10,763.9	71.4
Railways	42,900.0	18,270.9	42.6
Water Sector	36,750.0	22,059.4	60.0
NHA	324,720.3	207,663.1	63.9
Power	60,909.4	30,759.8	50.5
Others	436,721.0	241,147.9	55.2
Total	1,001,000.0	557,984.1	55.7

Source: Planning Commission, Status of PSDP releases as on 9 March 2018

2E. Bank Credit

Another indicator of economic activity and growth is the pace of bank credit to private sector. A look at net assets of the banking system shows increase in borrowing by government. During fiscal 2017-18 (July to 16 March 2017-18), net government borrowing for budgetary support was Rs. 554 Billion, an increase of 6.6% over the stock on 30 June 2017. Loans to private sector increased by Rs. 369.8 Billion up to 16 March 2018, an increase of 7% over the stock ending June 2017[25].

Commercial banks' domestic advances to the private sector grew by 3% for July-December 2017-18 over the corresponding period previous year. Of total advances to private sector, a mere 10.7% was for fixed investment. Working capital was 72.6% and consumer finance 8.8%. Growth rate of advances for energy projects, sugar mills, financial sector, and chemicals and pharmaceuticals fell. Loans to agriculture/agribusiness, textiles and apparels increased. SBP data shows decline in bank credit for fixed investment and trade finance to private sector[26].

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[25] SBP, Provisional Data on Monetary Aggregates 16 March 2018
[26] SBP Quarterly Performance Review of the Banking Sector Q4CY17, Tables 2 and 3

As stated before, government's macro-economic framework sets a target of 17.2% as the investment to GDP ratio. The target for total fixed investment is 16.1%. Of this, public investment is 4.5% (federal and provincial) and private is 11.2%. Last year, private investment was 9.9% of GDP. Stagnant machinery imports suggest stable to declining overall investments including private investment (Table 4 above). FDI has increased. It grew by 15.7% during July-February 2017-18 over the same period in 2016-17[27]. (Most FDI growth is debt based with equity increasing by 5% only)[28]. The pace of private bank credit should fuel growth.

Other areas affecting growth

Significant headwinds still stall growth. These have encumbered Pakistan's economy for some years. Despite strong resolve shown by the state, security in Pakistan remains a challenge. It would likely be so for the near future. Social tensions, regional instability, and displaced persons (though reduced in number) continue to thwart economic activity.

For the medium-term, it is important to remember that sustained growth needs strong macro fundamentals, enhancement in productivity through investment in human resource, and improved infrastructure. These factors crowd in private investment. Most social indicators show Pakistan well behind other emerging economies. More significantly, there is not enough thought given to job growth for the two million young Pakistanis entering the job market each year. Given the major social deficit that do not equip human resources for the market, Pakistan must start urgently a programme of workers' skills training. Resource constraints demand also that public investment in infrastructure, especially, must be based on judicious selection of projects with high economic returns. This is, at best, work in progress.

Despite government's commendable work on fiscal consolidation, macro fundamentals are still vulnerable as continued borrowing (especially external) have greatly increased public debt (details in subsequent sections). Borrowing is not for investment alone. Contrary to government claims, these also meet current expenditure.

Improvement in domestic savings is necessary to increase investment to contain indebtedness. It is desirable that debt should fund projects while government meet current expenditure from tax and non-tax revenues. Presently, there is not just budget, but also a primary deficit of about 1.5%. This means that government is borrowing also to pay interest on past loans. For years, multilateral external funding has not been for projects alone. They have been disbursed as budgetary support. This has added to the economy's vulnerability. This will likely continue in the future.

IMF estimates savings will reach 15.1% by 2019-2025. To meet government's plan for increase in investment to 20% of GDP, the economy must rely on external savings by almost 5% of

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[27] Board of Investment Pakistan, Foreign Investment inflows in Pakistan ($Millions)
[28] SBP, Summary Balance of Payments as per BPM6 - February 2018

GDP. At current GDP value, this means additional about USD 16 Billion per year. Pakistan must very significantly increase FDI as incurring further debt is unrealistic and unsustainable.

The economy's mixed profile continued in the quarter. On the positive side, growth kept its momentum, as seen in LSM and crops data. IMF forecasts the economy to grow by 5.6%, "supported by improved power supply, investment related to the China-Pakistan Economic Corridor (CPEC), strong consumption growth, and ongoing recovery in agriculture"[29].

But, with it, serious vulnerabilities continued, especially because of the economy's inability to deal with the structural twin deficits. These could affect growth rate and damage the positive profile of the real sector. Fiscal deficit for half year was 2.2% of GDP against an annual target of 4.1%[30]. Current account deficit of 4.8% (for July-February 2017-18) already exceeded the annual target of 2.6% of GDP[31]. In absolute value, as of February 2018, current account deficit was USD 10.8 Billion, and the trade gap was USD 19.7 Billion[32]. Annualizing this eight-month data, suggests a current account deficit of USD 16.2 Billion for 2017-18, 82% more than the Annual Plan's estimate of USD 8.9 Billion. PBS data shows imports for the half year grew by 20.4% and trade deficit by 24.3 %[33].

So far, GoP had attributed the runaway current account deficit to growth boosting machinery imports. However, during half year FY 18, when YoY current account deficit worsened, import of machinery fell by over 3%. Import of power generation fell by over 26%, construction machinery by over 24%, and office machinery by 8.3% (see Table 4). Major growth in imports were from LNG and petroleum crude, iron and steel scrap, and automobile, including CKD cars, buses, trucks, and motorcycles[34].

The economy has financed the current account from increased external indebtedness. Total external debt and liabilities increased by USD 5,799 Million during the half-year 2017-18. Public external debt, not including PSEs, increased by USD 4,408 Million during the first half of fiscal year. Total external debt and liabilities were USD 83,092 Million in June 2017. They grew to USD 88,891 Million by December 2017 (see Table 11). During first half 2017-18, the economy serviced USD 3.6 Billion in mark-up and principal externally. Of this, USD 2.8 Billion was for central government debt, 72% of budget[35].

Foreign exchange reserves came under severe pressure and fell by a large margin. External borrowing raised it somewhat in December but fell again in subsequent months. Net SBP foreign reserves were as follows[36]:

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[29] Express Tribune, March 7 2018, Risks to Pakistan's economic outlook have increased: IMF, Shahbaz Rana
[30] MoF, Pakistan's Fiscal Operations, July-December 2017
[31] SBP, Summary Balance of Payments as per BPM6 - February 2018
[32] Ibid
[33] PBS, Monthly Summary on Foreign Trade Statistics, December 2017
[34] Ministry of Commerce, Monthly Statements Showing Exports/Imports, Comparative Imports of Selected Commodities, July-December 2017-18
[35] SBP, Pakistan's External Debt and Liabilities and Debt servicing data
[36] SBP Liquid Foreign Exchange Reserves

- February 2017: USD 17,081.0 Million
- June 2017: USD 16,144.8 Million
- December 2017: USD 14,106.9 Million
- February 2018: USD 12,227.3 Million

Ballooning foreign repayment obligations is a major risk for the economy. IMF fears a current account deficit of 4.8% of GDP or USD 16.6 Billion. It "noted with concern the weakening of the macroeconomic situation, including a widening of external and fiscal imbalances, a decline in foreign exchange reserves, and increased risks to Pakistan's economic and financial outlook and its medium-term debt sustainability" [37]. It is understood that multilateral financial institutions rely also on IMF signaling to continue funding. Reports suggest a hiatus in multilateral concessional disbursements to Pakistan.

GoP has not shared its plans about meeting the forex gap. Restoring relations with IMF may need US government support, which is not automatically assured. The larger issue is that Pakistan is permanently dependent on external savings to meet its foreign exchange needs. The economy is exposed to continuous loan rollover and re-pricing risks. In effect, the economy is in a debt trap, but successive governments have no exit plan for it. Its more recent, though delayed, response is change in the Rupee exchange rate. Going back to IMF will mean continued exchange rate adjustments by large margins. Though needed, that is insufficient policy. The economy can turn around if all leaders show firm intent to take challenging decisions.

To enhance its repayment capacity, there must be sustained growth of GDP and of exports. That in turn needs higher savings, investment (including public investment). Inevitably, this will need higher imports, and more external capital. Breaking out of this circular logic that constrains the economy is government's challenge. The economy needs a combination of stabilization and growth policies with perhaps rescheduling of loans and targeted sourcing of FDIs. (Government may face constraints in rescheduling of commercial financing, a source of financing on which GOP has relied on considerably in recent years).

Two months before elections, government policy is adrift with the economy sliding deeper into a morass of its own making. The genesis of this lies in decisions taken four years ago. For four years, this Institute cautioned about the impending conundrum, especially because an apparently overvalued Rupee distorted the economy. Rupee value encouraged import and dampened exports. This was the time when GOP celebrated its performance based on (what was even then apparent as) cursory and casual reports by foreign media. It also received extensive exemptions by the IMF. Regrettably, hyperbole and patting the self on the back are no substitutes for strategy.

[37] IMF, Press Release, First Program Monitoring Discussions, 6 March 2018

3. Public Finance

Details of fiscal operations released by Finance Ministry show mixed signs[38]:

- Budget deficit for the first quarter was 2.2% of GDP[39]. Actual deficit will almost certainly exceed target deficit of 4.1% for the fiscal year. IMF estimates the deficit to go up to 5.5% of GDP or an unprecedented Rs.2 Trillion, or 39% of the budget size[40].

- Revenue: First half FY 18 federal tax revenue increased to Rs. 1,850.5 Billion,16% above revenue for the same period FY 17, which was 1,595.5 Billion[41]. Budget estimate of Rs, 4,330 Billion for federal taxes for FY 18 is 18.7% above last fiscal's actual collection of Rs. 3,647.5 Billion[42].

- FBR tax collection has done better and is in line with growth target. Year on year increase for first half FY18 is 17.9% above last year's revenue for the same period. The budget estimate of Rs. 4,013 Billion is 19% above last fiscal's actuals. It is important to view increase in FBR revenue in perspective. In 2015-16, FBR taxes registered an unprecedented increase of more than 20% over the previous fiscal. In FY 17, FBR revenue increased a further 17.6%.

Table 6
FBR Tax Collection

Billion Rs.

	Budget 17-18	July-Dec 16-17	July-Dec 17-18	% Growth 16-17	% Growth 17-18
Direct Tax	1,594.9	586.4	673.8	8.4	14.9
Indirect Tax	2,418.1	880.9	1,056.3	4.4	19.9
Total	4013.0	1,467.3	1730.1	5.9	17.9
	October-December 16-17		**October-December 17-18**		
Direct Tax		354.9		386.9	9.0
Indirect Tax		487.5		578.4	18.6
Total		842.4		965.3	14.6

Source: MoF Fiscal Operations July-December 2017-18 and July-June 2016-17

- Other Taxes declined: Budget estimate 2017-18 for Other Taxes (GIDC, Airport tax, Petroleum Levy) is 11% above last year's actual. However, actual collection for H1 FY 18

[38] MoF, Fiscal Operations July-December 2017
[39] Ibid Table 1
[40] The Express Tribune, Risks to Pakistan's economic outlook have increased: IMF, 7 March 2018, Shahbaz Rana
[41] MOF Fiscal Operations July-December 2017 and fiscal 2016-17
[42] MoF Budget in Brief 2017-18

was 6.1% below the corresponding period last year (each component of Other taxes fell, except Petroleum Levy)[43].

- Federal government's non-tax revenues grew by 36% after consistent drop for previous two years. Its component of SBP Profits rose by 42.5% and reflects government's borrowing preference.

Expenditure

- With respect to expenditure, total H1 current and development expenditure of the federal government is 14.5% above the amount spent last year, though it is within proportional budget. Last year, expenditure in H2 was over 60% of total, with 35% in the last quarter.

- In H1 FY 18, consolidated federal and provincial expenditure, which is the basis for the fiscal deficit, was 14% above last year's spending. Second half consolidated spending in 2016-17 was also about 60%, with 36% in the last quarter alone.

- To limit the deficit, GoP must keep an eye on trend of current expenditure. Federal budget 17-18 estimates decline in current expenditure over Revised 2016-17 by 3.7%, whereas H1 increase is 12.3% above last year. July-December debt servicing (mark-up payment) is especially higher than estimate. It has grown by 17% above last year, 55% of the budgeted amount. Given the inevitability of debt servicing expenditure because of increased indebtedness, it seems unlikely that the government has control on expenditure. Mark-up is 45% of current account budget.

Deficit

- The year's fiscal deficit target is 4.1%. The deficit for July-December is Rs. 796.3 Billion, 2.2% of GDP, which proportionately exceeds GoP's target of 4.1% of GDP for the year. Deficit for the same period last year was 2.4% of GDP, when the year's deficit was 5.8% of GDP.

- Of especial concern is that fiscal operations is running a primary deficit. This was Rs. 515.6 Billion in 2016-17 or 1.6 % of GDP. For July-December 2017-18, primary deficit was about Rs. 45 Billion. This suggests that there is no debt retirement as even mark-up is being paid from borrowings[44].

- Target deficit is contingent on provincial surplus of Rs. 347 Billion[45]. Last year, provinces generated a deficit of Rs. 163 Billion against a target of Rs. 339 Billion[46]. It appears that the combination of revenue shortfall and lower than estimated provincial surplus will lead to a fiscal deficit that is higher than the target.

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[43] MoF, Fiscal Operations July-December FY 18 compared to July-Dec FY 17, Table 4
[44] MoF Fiscal Operations for 2016-17 and July-December 2017-18
[45] MoF Budget in Brief 2017-18, Page 8, Table 6.
[46] MoF Fiscal Operations 2016-17, Table 5

- Debt servicing spending is considerably more than proportionate budget. First half's markup payment is 55% of annual budget. This trend would likely continue as GoP has incurred higher debt, including external debt. During July-January 2017-18, government borrowed an additional Rs. 1.9 Trillion. Domestic debt grew by Rs. 947 Billion (all short-term) and external debt was higher by Rs. 975 Billion. In November 2017, GoP again floated a sukuk bond for USD 1 Billion and USD 1.5 Billion Eurobond at 5.625% and 6.875% markup respectively. Since then, it has raised foreign debt at regular intervals. In January 2018, the government is said to have borrowed USD 704 Million, and in February 2018, it borrowed USD 500 Million from China's ICBC[47].

- Other heads: Power circular debt has climbed again. Total liabilities stand at Rs. 922 Billion. Of this, government's direct payable is Rs. 472 Billion and the rest Rs. 450 Billion are bonds of the Power Holding Private Ltd[48]. The issue of circular debt will remain until government does not reduce line losses and bills and recovers amount due from consumers. Otherwise, increase in generation capacity will increase circular debt. Without governance improvement, the power sector's sustainability is questionable. That this has happened during a period of low energy prices and three surcharges to help meet the deficit, is surprising. Government has the tariff rationalization surcharge, debt servicing surcharge, and Neelum Jhelum surcharge. Subsidy for other PSEs also will remain as they have neither been reformed nor privatized.

- Several other expenditures are likely to weigh on the budget. These include continued expenditure on the pressing need for border and internal security and on settlement of IDPs.

- Of the Rs. 796 Billion deficit financing for July-December 2017-18, government sourced about evenly between domestic and external borrowing. External financing was Rs. 384 Billion, while domestic financing was Rs. 412 Billion. Of the balance Rs. 412 Billion from internal sources, GoP has financed Rs. 80 Billion from non-banking sources and Rs. 332 Billion from bank[49].

While the economy is showing signs of recovery, it is critical that GoP pays immediate attention to the twin fiscal and current deficits.

[47] Express Tribune, Pakistan borrows another $500m from Chinese bank, Shahbaz Rana, 17 February 2018
[48] Express Tribune, Never-ending cycle of debt, Editorial 3 March 2018 also Dawn, Energy sector circular debt touches record Rs922bn, 2 March 2018
[49] MoF Fiscal Operations Table 10

Table 7
Summary of Fiscal Operations, July-December 2017-18
Budget 2017-18, IMF Projections, Fiscal Operations

Rs. Billion

	Budget 2017-18	**IMF Projections**	**Actual Fiscals Six Months**	**% of Budget**
A. Revenue			1,025	
A.1Tax Revenue			911	
Federal	4,330	4,330	1,850	43
FBR • Direct • Indirect Other taxes	4,013 1,595 2,418 317	4,013 1,595 2,418 317	1,730 674 1,056 120	43 42 44 38
Provincial		627	176	
A.2 Non-Tax Revenue		1,210	364	
Federal	980	966	300	31
Provincial		244	64	
B. Expenditure		7647		
B.1 Current Expenditure		5546		
Federal	3,477	3603	1,667	48
Interest Payments	1,363	1363	751	55
Defence	920	920	393	43
Subsidies	139	144		
Grants	430	551	130	30
Others	625		91	15
Provincial		1943	896	
B.2 Development Exp & Net Lending	2,265	2101	616	27
Federal	1,001	1001	248	25
Provincial	1,112	1112	317	29
Other Development	152		55	36
Lending and grants	123		2	2
E. Fiscal Deficit	4.1%	-3.0%	2.2%	54
F. Financing Net (after provincial surplus of Rs. Billion)	1,480	1413	796	54
External	512	626	384	75
Domestic	968	787	412	43
Bank Non-Bank Grant	390 578	551 236	332 80	85 14
Primary Surplus/Deficit	+85	-515	-45	--
Memorandum Item				
Nominal GDP			35,919	

Central Government and Public Debt

Federal government debt increased by Rs. 1,922 Billion for the period July-January 2017-18. Of this amount, Rs. 975 Billion is from external sources (Table 8). Within domestic debt, short term debt grew by Rs. 1,393 Billion for the period (MTBs), while long term debt decreased by Rs. 445.7 Billion[50].

Stock of Pakistan's total debt and liabilities on 31 December 2017 was Rs. 26,814.7 Billion, an increase of Rs. 1,741 Bill during the six months July-December 2017-18[51]. In addition to government debt, this gross figure includes PSEs debt, support from IMF, non-government, and debt liabilities. Some of the increase is also because of Rupee exchange rate effect on external debt.

Table 8
Federal Government Debt

Billion Rs.

	January 2017	**June 2017**	**January 2018**	**Increase July-January 2017-18**
Total Domestic Debt	14,515.5	14,849.2	15,796.6	947.4
Long-term	8,022.5	8,298.4	7,852.7	-445.7
Market Loans	2.8	2.8	2.8	0
Federal Government Bonds	4,549.8	4,778.4	4,237.5	-540.9
PIBs	4,184.6	4,391.8	3,850.8	541
Prize Bonds	713.0	747.1	798.6	51.5
Unfunded Debt	2,752.2	2,765.3	2,808.8	43.5
NSS	2,597.6	2,630.6	2,674.0	43.4
Foreign Currency Loans	4.7	4.7	4.7	0
Short term	6,492.9	6,550.9	7,944.0	1,393.1
Market Treasury Bills	3,563.9	4,082.0	4,315.4	233.4
External Debt	5,367.0	5,918.7	6,894.1	975.4
Long term	5,221.5	5,826.2	6,783.1	956.9
Short term	145.5	92.5	111.0	18.5
Total Federal Government Debt	19,882.5	20,767.9	22,690.7	1,922.8
Source: SBP Central Government Debt				

[50] SBP, Central Government Debt Provisional, February 2018
[51] SBP, Pakistan Debt and Liabilities Profile

Balance of Payment

Continuing their trend from the early months of 2017, exports grew 11% in July-December 17-18. Before 2017, exports had been free fall for three years. In 2014-15, exports declined 8% from the previous year. In 2015-16, they fell by a further 12.4% and then took another hit of 1.6% in 2016-17[52]. Imports grew by 19% during the half year (Table 9). The trade deficit for the period increased to almost USD 18 Billion, 24.3% above the same period last year[53].

Table 9
Trend in Trade
YoY July-January 2017-18

Exports

Million USD

Commodity	July-December 2016-17	Share in total %	July-December 2017-18	Share in total %	Change in value %
Food Group	1,654.2	16.7	1,932.3	17.6	16.8
Textiles	6,146.6	62.1	6,642.9	60.4	8.1
Petroleum & Coal	89.3	0.9	163.6	1.5	83.2
Other Manufactures	1,528.9	13.9	1,694.2	15.4	10.8
Chemicals and Pharmaceuticals	396.1	3.6	538.9	4.9	36.0
Engineering Goods	83.9	0.8	98.8	0.9	17.7
Cement	145.6		118.6		-3.0
Others	475.8	4.8	569.0	5.2	19.6
Total	9,894.9		11,001.9		11.2

Imports

Million USD

Commodity	July December 2016-17	Share in total %	July-December 2017-18	Share in total %	Change in value %
Food	2,864.5	11.8	3,239.7	11.2	13.1
Machinery	5,671.0	23.3	5,484.6	19.0	-3.11
Transport	1,404.1	5.8	2,012.8	7.0	43.4
Petroleum	5,003.1	20.6	6,675.2	27.4	33.4
Textile	1,364.2	5.6	1,378.9	4.8	1.1
Chemicals	3,594.1	14.8	4,284.3	14.8	19.2
Metal	1,960.1	8.1	2,568.8	8.9	31.1
Miscellaneous	574.3	2.4	651.7	2.3	13.5
Others	1,887.8	7.8	2,634.9	9.1	39.6
Total	24,323.2		28,940.9		18.9
Trade Deficit	14,428.3		17,939.0		24.3

[52] All figures based on PBS and MoC data.
[53] PBS Monthly Summary of Foreign Trade

SBP data shows growth in July-December FY18 trade deficit to be 26.7% higher than the same period last year. FY 17's trade deficit of USD 26.6 Billion was 8.7% of GDP, the highest ever. SBP has voiced concern stating that "it must be acknowledged that while imports are essential … there is a need for equivalent increase in foreign exchange earnings to finance these imports and thereby maintain the external sector's stability". Since then, the deficit has grown further. Deficit for July-January 2017-18 has gone up to over USD 17 Billion, 23.6% above the same period last year[54].

Table 10
Change in exports YoY
July-December 2017-18

% Change

	Value	Quantity	Unit Value
Textile products			
Cotton yarn	10.8	0.62	-9.2
Cotton cloth	-0.01	-6.88	7.4
Knitwear	13.4	8.4	4.6
Bedwear	6.2	2.4	3.7
Towels	0.3	1.2	-0.8
Readymade garments	13.5	10.9	2.3
Rice	18.3	9.2	8.3
Leather products			
Garments	-2.0	-9.7	8.5
Gloves	9.7	18.2	-7.2
Sports goods			
Footballs	7.2	20.0	-10.9
Gloves	-9.1	-20.9	14.9
Source: Ministry of Commerce, Monthly Trade Statistics, December 2017			

Though exports have grown by 11.2% for the half year, a faster increase in imports of 18.9% means a widening trade gap. Exports of all products, except Engineering Goods, increased. There are mixed signs of competitiveness of textiles as there are just a limited number of goods whose quantity as well as unit value grew (Table 10). These include traditional export anchors such as rice, knitted apparels, bed linens, and garments.

Two observations are important. Pakistan's exports continue to be locked in primary or low value-added standard textile goods with no product differentiation. Second, that Pakistan

[54] SBP, Summary Balance of Payments, January 2018

mostly competes on price. This strategy means that there will always be new low-cost entrants to compete on price and that our exporters must reduce prices further. This is true especially during periods of slow growth in trade. This strategy results in frequent demands for fiscal incentives to exporters. After over half a century, textiles exports still need fiscal incentives. Their limited ability to upgrade products entails an expense on tax payers. It is important to build export by diversifying into new products and by pursuing a product differentiation strategy within textiles.

However, what is surprising is a lack of thoughtful analysis about what ails our manufacturing, especially textile industry, despite natural competitive advantage and why is it that Pakistan has not, in any meaningful way, moved beyond textiles to new industries. A proactive and concerted effort to increase competitiveness is needed to move to new products that are value added and processed.

Among imported goods, the increase was across the board. Petroleum products and auto imports grew rapidly. Petroleum imports increased by USD 1,672 Million in six months, 33.4%. LNG grew by 71% in value. Import of crude, refined, and LPG also grew. Import of autos increased by over USD 600 Million, or 43.4%, both CBU and CKD. Import of fertilizer, plastics, and iron and steel also grew. Import of iron scrap grew by 76% (Table 9)[55].
Contrary to GoP's explanation for rising current account deficit, import of machinery has declined by over 3%. Import of power generation machinery fell by 26% and construction machinery by 24%.

Increasing trade deficit has meant a higher current account deficit, financed by external debt. FY 17's current account deficit was USD 12.4 Billion, or 4.1% of GDP. Annualized July-January current account deficit of USD 9.2 Billion is 4.7% of GDP, an increase of 48% over the same period last year. The ever-widening gap means is alarming. Its rate of growth has slowed somewhat with correction in the Rupee value. Yet, the increase in current account deficit, estimated to go up to USD 16.6 Billion by IMF seems unsustainable[56]. The Annual Plan sets a current account deficit target of 2.6% of GDP (USD 8,991 Million)[57]. By January 2018, this target had been surpassed already.

Regarding FY 17, SBP states that "to finance the current account gap, the country had to scale up external borrowings (Figure 6.4). Most of these borrowings comprised commercial loans, including short-term ones, which exposed the economy to both rollover and re-pricing risks." SBP counsels limiting import and stimulating exports. Debt sustainability will be a concern in coming years.

Home remittance is an important external financing source for Pakistan, which mitigates the large trade deficit. After a 3% decline in FY 17, workers' remittances increased by 3.5% during July-January 2017-18 over last year. FDI inflows increased during July-January 2017-18, by

[55] Based on MoC Trade Statistics, December 2017
[56] Express Tribune, Pakistan's economic outlook at risk: IMF, 8 March 2018
[57] PC, Annual Plan 2017-18 Page 90

USD 1,941 Million or 15.7%[58] and somewhat eased the Balance of Payment. The Annual Plan targets net FDI of USD 4,183 Million for 2017-18[59]. This is almost twice more than last fiscal's actual of USD 2,411 Million. As expected, FDI has increased from China. Although private flows are hard to predict, especially with CPEC investment due, FDIs in 2017-18 will perform better than last year, though may fall short of target substantially. In limited amounts, FDI from UK, Germany, and Switzerland also grew.

Increase in external debt has financed the increase in current account deficit. External debt and liabilities increased by USD 5.8 Billion in six months between July and December of the fiscal year. Of this, government debt grew by an alarming USD 4.17 Billion. During this period, borrowings by banks grew by USD 184 Million, and private sector borrowing increased by USD 731 Million[60]. Compared to December 2016, total external debt and liabilities grew by USD 13,133 Million by December 2017. Government external debt grew by USD 8.5 Billion. In December 2017, total external debt and liabilities was 27.3% of GDP.

Table 11 gives increase in external debt and liabilities. The last two columns give debt accumulation for the year from December 2016 to December 2017 and for the half year July-December 17-18.
On 31 December 2017, foreign currency reserves stood at USD 14,106 Million, $ 2,038 Million lower than June 2017 reserves of USD 16,144 Million. Reserves fell further to USD 12,227 Million in February 2018. Continued correction in Rupee and imposition of regulatory duties (a practice with which this Institute does not agree) have dampened imports.

There are several structural and competitiveness factors that stop Pakistan from becoming a major export economy. If exports do not increase, Pakistan must continue to borrow to finance imports. This is a especial concern as energy prices, though still low, have risen by an average of 18% in one year (February 17 to February 18). However, most forecasts expect a correction to norm and some decline in price[61].

We hope that recent machinery and fuel imports would soon stimulate the economy and increase exports. Though the economy is in modest recovery, exports are still in recovery. Pakistan's debt sustainability, therefore, is a major concern. Pakistan may also review if its tariff structure supports exports. We may reorient our approach to tariff policy from one where import tariff is viewed as a source of public finance to one that supports exports. Such a review would reduce average tariff rates and do away with protection that carry high economic cost.

[58] Board of Investment, Pakistan, Foreign Investment inflows in Pakistan($ Millions), July-February 2017-18
[59] PC Annual Plan 2017-18, Page 90
[60] SBP Pakistan's External Debt and Liabilities - Outstanding
[61] Source: Knoema

Table 11 Increase in External Debt and Liabilities July-December 2017-18 Million USD				
	Amount			
	June 17	**December 17**	**Increase/Decrease December 2016 to December 2017**	**Increase/Decrease June-Dec 17-18**
A. Public External Debt	66,103	70,511	9,025	4,408
1. Government	56,430	60,603	8,504	4,173
Long term	56,287	59,445	8,519	3,158
Short term	882	1,158	-14	276
2. From IMF	6,109	6,256	350	147
3. Forex Liabilities	3,564	3,652	170	88
B.Public Sector Enterprises	2,706	2,943	162	237
C.Banks	4,519	4,703	1,488	184
Borrowing	3,303	3,462	1,317	159
Deposits	1,203	1,242	172	39
D. Private Sector	6,505	7,236	2,047	731
E. Debt liabilities to investors	3,258	3,498	412	240
Total External Debt & Liabilities % GDP	83,092	88,891	13,133	5,799
Official Reserves	16,243	14,329		-2,038
GDP	303,779 27.3	325,257 27.3%		
Source: SBP Pakistan External Debt and Liabilities				

Most BoP indicators have worsened, especially the trade deficit. The fragile current account is accompanied by a financial account that is equally unbalanced and a BoP in deficit Table 12.

Table 12 Summarized Balance of Payment Million USD				
	Annual Plan 2017-18	**Actuals July-Jan 2016-17**	**Actuals July-Jan 2017-18**	**% Change**
1.Current Account Balance	-8991	-6182	-9156	48.1
Exports	23731	12440	13909	11.8
Imports	48829	26299	31042	18.0
Balance on Goods	-25731	-13859	-17133	23.6
Remittances	20673	10993	11385	3.6
2.Capital Account	371	135	187	38.5
3.Financial Account	10003	-5332	-5947	11.5
FDI	4183	1532	1489	-2.9
FPI	1080	670	2419	261.0
Net Foreign Assistance	3684	1063	1888	77.6
Others	2275	1708	285	-83.3
4.Errors & Omissions	0	16	-220	
5.BoP deficit/surplus	1384	-699	-3242	363.8
Current Account Balance % of GDP	-2.6	-3.5	-4.7	
Source: SBP Balance of Payments				

Inflation

GOP's Annual Plan for 2017-18 targets a 6% inflation rate[62]. Based on government's fiscal consolidation measures, a stable Rupee, and fall in international commodity prices, inflation has been well under control for the last three years. However, inflation may increase with recent adjustment in Rupee value. For the period July- December 2017-18, average year on year CPI was 3.75% compared to 3.88% for the corresponding period previous year. For the same period, rate of growth in Sensitive Price down slightly to 1.33% from 1.35%, last fiscal. WPI growth rate dropped to 1.96% from 3.06% in the previous year[63]. In December 2017, core inflation that includes items other than food and energy was 5.5% compared to 5.2% in

[62] Planning Commission, Annual Plan 2017-18, Page 10 (Annexure II)
[63] Pakitan Bureau of Statistics, Monthly Review of Price Indices Table 1.1

December 2016. Core inflation (non-food non-energy) is higher than CPI, SPI, and WPI[64]. This suggests revival in overall demand in the economy. Food inflation has stayed below CPI. In December 2017, year on year food inflation was 3.8%, which is a sudden jump from 2.4% in November 2017.

Table 13
July-December 2017-18 and YoY Changes

%						
	Average Changes %			**YoY Changes for December**		
	2017-18	2016-17	2015-16	2017	2016	2015
CPI	3.75	3.88	2.08	4.57	3.70	3.19
SPI	1.33	1.35	0.26	2.24	0.53	2.91
WPI	1.96	3.06	-2.35	3.39	3.08	-0.42

Source: Reproduced Table from PBS Monthly Review of Price Indices December 2017

Increase-decrease in price of individual items

Table 14 gives change in prices of individual items

Food items that increased YoY were Onion (130.36%), Tomatoes (49.35%), Potatoes (21.52%), Chicken (21.21%), Betel Leaves & Nuts (16.18%), Rice (15.12%), Fresh Vegetables (12.04%), Meat (7.69%), Tea (7.59%), Honey (6.90%), Fresh Fruits (6.58%) and Readymade Food (6.38%).

Food items whose price decreased were: Pulse Gram (28.85%), Pulse Mash (27.41%), Pulse Moong (21.19%), Pulse Masoor, (20.68%), Besan (20.25%), Cigarettes (18.47%) Sugar (13.45%) and Gram Whole (7.64%).

Non-food Items with increase in price were Drugs & Medicines (14.82%), Kerosene Oil (13.51%), Education, (12.40%), Motor Fuel (11.07%), Personal Equipments (8.30%), Doctor MBBS Fee (7.60%), Construction wage Rates (7.31%), Medical Tests (6.78%), Tailoring (6.77%), House Rent (6.49%), and Personal Care (6.08%).

[64] Pakitan Bureau of Statistics, Monthly Review of Price Indices Table 1

Table 14 Inflation in Major Food Items, Commodities, and Services, December 2017 YoY		
	Weight in CPI	**Inflation %**
General CPI	**100.00**	**4.57**
Food Group	**34.83**	**5.16**
Wheat flour	4.16	0.38
Rice	1.58	15.12
Meat	2.43	7.69
Chicken	1.35	21.21
Milk (fresh)	6.68	3.86
Cooking oil	1.75	2.73
Vegetable ghee	2.07	2.65
Fresh fruits	1.86	6.58
Pulses	0.95	13.47
Vegetables	1.71	12.04
Sugar	1.04	13.45
Tea	0.83	7.59
Cigarettes	1.39	18.47
Clothing and Footwear	**7.57**	**3.64**
Cotton cloth	1.72	4.04
Readymade garments	0.97	4.53
Tailoring	0.88	6.77
Housing, Electricity, Gas	**29.41**	**4.86**
House rent	21.81	6.49
Electricity	4.39	0.00
Gas	1.57	0.00
Health	**2.18**	**10.92**
Drugs and Medicines	1.26	14.82
Doctors' fee	0.59	7.60
Transport	**7.20**	**4.45**
Motor Fuel	3.02	11.07
Transport Services	2.70	0.22
Communication	**3.21**	**1.23**
Recreation & Culture	**2.02**	**0.59**
Education	**3.94**	**12.40**
Restaurants and Hotels	**1.22**	**6.38**
Misc. Goods and Services	**2.75**	**6.50**
Source: PBS, Monthly Review of Prices, Annexure A, December 2016[38]		