Institute for Policy Reforms

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Will economic revival last? Pakistan Economic Survey FY 21

Exceeding expectation, the 4% GDP growth in FY 21 is cause for relief and satisfaction. Celebration may be premature. It is more important to analyze what caused the unexpected growth and how can it be increased and sustained over a long period. Also, we must see the source of growth and whether it benefits the poor. Merely focusing on one indicator minimizes the complexity of the processes that create growth.

Going beyond growth, not all signs are sanguine. The economy must address some fundamental issues, without which this revival will be short lived. They include unsustainable debt levels with debt servicing needs that strain both the fiscal and the current accounts.

A special concern is low savings and investment levels, that declined further in FY 21. Without enough investment exports suffer and growth becomes transitory, fueled by one time spending. In the public sector, this shows in serious infrastructure shortage and human capital deficit. In the privates sector, it shows in low real growth in production and investment, low productivity and weak job growth.

On the fiscal side, revenue numbers are a special concern. During July-March, year on year FBR revenue grew by 11.5 %, just a little over the CPI increase. GoP's target growth rate for FY 21 is 24% to Rs. 4,963 Billion. To achieve that, FBR revenue must now grow by 64% in the last quarter, and it must collect Rs. 1,568 Billion. FBR collection may fall short by about Rs. 350- 400 Billion. Another concern is decline in direct taxes to 36% of total from 38% last year and 40% in FY 2010.

With respect to expenditures, both the federal and provincial governments have contained spending up to March 2021. Perhaps reflecting government priority, PSDP spending is down by 15% over last year.

At Rs. 2,104 Billion by March 2021, debt servicing is 82% of net federal receipts and 45% of its total expenditure, leaving little space for other essential services. This may grow as GoP plans to borrow more in FY 21. Policy makers must balance between the vital need for relief to citizens and debt sustainability.

Overall fiscal deficit up to March 2021 is 3.6% of GDP, contained by provincial surplus. To stay within the target of 7% of GDP, revenue must grow radically, provincial surplus must continue, and GoP should limit spending. As revenue has crossed Rs. 4 Trillion by May, government could stay close to its target. Last fiscal too, nine month deficit was 3.8% which jumped to 8.1% by year end.

FY 21 GDP growth rate of 3.94% is based on increase in LSM by 9.3% and important crops, especially wheat by 2.8%.

Yet growth was caused by fiscal incentives and concessional credit for investment and social protection payments. It did not come from investment. GoP's declared goal of reaching 5% GDP growth in fiscal will happen only if IMF allows such largesse to continue.

But such feel good growth does more harm than good. Borrowings have to be paid back with interest. GoP must invest the borrowing into infrastructure that boosts exports.

Total investment and gross capital formation for FY 21 (15.2 and 13.6% of GDP) are slightly down from FY 20's 15.3% and 13.7% of GDP. Private sector capital formation declined in FY 21 from the previous fiscal. This is especially notable in manufacturing and construction. Construction was offered huge incentives and amnesty, yet investment fell by 28.7%. Government's express goal of sustained growth will come about only if high profits get reinvested. Net FDI fell by 32 %.

Production in some areas have taken a hit. Power generation and distribution fell by 23%. Yet consumers and taxpayers must still pay for capacity guarantees.

Government must focus on growth in energy production. Crude and gas production is up 5 and 7% this year. This is not enough to reduce the burden of high energy import bills. Pakistan must improve policy to exploit the known reserves of conventional and shale oil and gas as well as lignite.

Regarding the balance of payments, eleven months imports grew by 22.5%, as trade deficit worsened by 30.5%. Similarly, external debt servicing is estimated to touch $ 14 Billion for FY 21. Remittances grew by 29% mitigating their impact.

Inflation is up again. CPI grew by almost 11% over May 2020. The sensitive price index was up by 19.7% and wholesale prices by 19.4%. Food inflation too was in double digits. For the period July-May FY 21, CPI grew by 8.8%, sensitive price index by 13. 5%.