5 External Sector

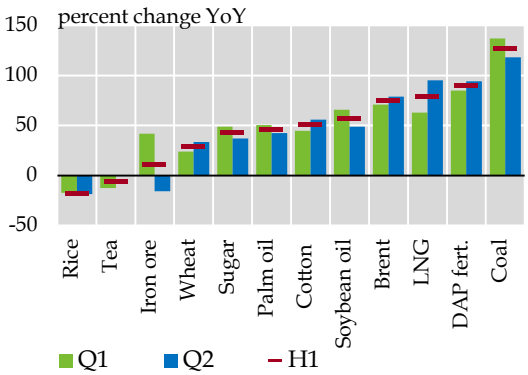
The continued surge in global commodity prices in response to supply-side bottlenecks and buoyant global demand had largely negative consequences for Pakistan's external account during H1-FY22. This surge in prices was the dominant factor behind the sharp increase in import payments during the period. While textile exports benefited from the higher global cotton prices and contributed to the rise in overall export receipts to record half-yearly levels, the sharper uptick in import payments widened the trade deficit. Buoyant workers' remittances provided some respite, but could not offset the higher trade deficit. Resultantly, the current account deficit rose and contributed to a 10.7 percent depreciation in the PKR. However, the SBP's FX reserves increased slightly over the six-month period to US$ 17.7 billion by end-December 2021, amidst higher financial flows from multilateral, bilateral and commercial sources.

5.1 External Sector Developments

The external account remained under pressure during the H1-FY22. This was mainly due to consistently rising global commodity prices (**Figure 5.1**), ongoing Covid-19 vaccine procurement, the continued need to import wheat and sugar to plug domestic supply gaps, together with some demand-side pressures associated with the sustained domestic recovery from Covid. While export receipts and workers' remittances both rose substantially to record half-yearly levels, they could not offset the surge in import payments. As a result, the current account deficit (CAD) widened to US$ 9.0 billion during H1-FY22, against a surplus of US$ 1.2 billion last year (**Table 5.1**). This FX payments gap was generally reflected in the interbank market, where the PKR depreciated 10.7 percent against the US Dollar during H1-FY22. However, the SBP's foreign exchange buffers remained largely intact during the period on the back of higher external financing.

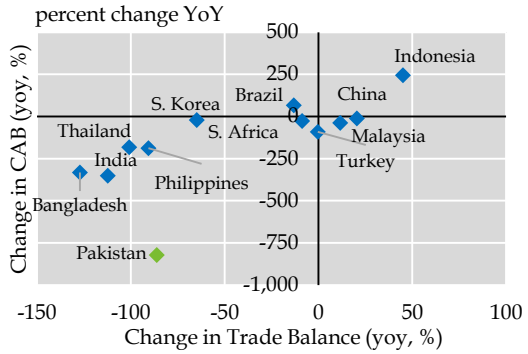
In addition to Pakistan, multiple other net oil importing emerging markets (EMs) also witnessed a deterioration in their current account balances, mainly due to a higher trade deficit (**Figure 5.2**). In Pakistan's case, higher international commodity prices had a more pronounced impact on the trade account as compared to some other EMs,

Growth in Major Global Commodity Prices during Jul-Dec FY22 **Figure 5.1**



Source: World Bank Commodity Prices

Change in EM Trade & Current Account Balances in Jul-Dec FY22* **Figure 5.2**



*goods trade balance

Source: Haver Analytics and State Bank of Pakistan

given the country's narrow export base and the fact that the post-Covid

Pakistan's Balance of Payments **Table 5.1**

million US Dollars

	Q1-FY21	Q1-FY22	Q2-FY21	Q2-FY22	H1-FY21	H1-FY22
Current account balance	**865**	**-3,526**	**382**	**-5,497**	**1,247**	**-9,023**
Merchandize trade balance	**-5,283**	**-10,194**	**-6,103**	**-10,993**	**-11,386**	**-21,187**
Exports	5,354	7,201	6,461	8,034	11,815	15,235
Imports	10,637	17,395	12,564	19,027	23,201	36,422
o/w Energy imports	2,076	3,974	2,206	4,598	4,283	8,571
Non-energy imports	8,561	13,421	10,358	14,429	18,918	27,851
Services balance	**-533**	**-877**	**-411**	**-946**	**-944**	**-1,823**
Primary income balance	**-1,489**	**-1,006**	**-1,184**	**-1,475**	**-2,673**	**-2,481**
o/w interest payments	646	469	644	930	1,290	1,399
Secondary income balance	**8,170**	**8,551**	**8,080**	**7,917**	**16,250**	**16,468**
o/w Workers' remittances	7,143	8,199	7,060	7,609	14,203	15,808
Financial account balance^	**854**	**-5,730**	**-1,163**	**-4,322**	**-309**	**-10,052**
Direct investment inflow	458	480	422	578	880	1,058
Portfolio investment inflow	-145	879	-290	-1,285	-435	-406
o/w Eurobonds/Sukuk	-	1,000	-	-1,000	-	-
Build-up in FX assets abroad	1,106	410	467	5	1,573	415
FX loans & liabilities (net)	20	4,774	1,480	5,090	1,500	9,864
o/w General government	1,422	1,637	1,620	4,231	3,042	5,868
SBP	-1,000	2	69	1	-931	3
Banks	-642	137	21	434	-621	571
SDR allocation	-	2,773	-	-	-	2,773
SBP's liquid reserves (end-period)*	**12,154**	**19,254**	**13,415**	**17,686**	**13,415**	**17,686**
SBP's forw. liabilities (end-period) *	-5,774	-4,870	-4,610	-4,382	-4,610	-4,382
PKR app(+)/dep(-) in percent*	**1.4**	**-7.7**	**3.7**	**-3.3**	**5.1**	**-10.7**

*Change in reserves, forward liabilities and PKR ex. rate during the period (Jul-Sep for Q1, Oct-Dec for Q2, H1- for H1). ^Negative sign with financial account balance means net FX inflow into Pakistan and vice versa. Positive sign with change in financial acct. balance means higher net FX inflow into Pakistan on YoY basis and vice versa.
Source: State Bank of Pakistan

policy-induced economic rebound had already pushed up the import demand for a wide range of products (**Box 5.1**). On the other hand, the deterioration in the current account deficit was relatively lower, given Pakistan's buoyant and resilient remittances. The growing trade imbalance had necessitated a policy reorientation from September 2021 onwards. The SBP's Monetary Policy Committee raised the policy rate by a cumulative 275 basis points during September-December 2021, and the SBP also undertook multiple administrative and regulatory measures to manage domestic demand.[1]

The rise in global cotton prices supported Pakistan's textile exports during H1-FY22, with textiles contributing over two-thirds to the overall export growth during the period. Apart from the favorable pricing environment abroad, Pakistani exporters continued to capture market share from competitors in the major destinations (**Section 5.5**). The SBP's concessionary financing schemes for working capital and fixed investment provided much-needed

[1] These measures included changes in prudential regulations to tighten auto and consumer financing, imposition of cash margin requirement on an additional 114 items, and an increase in the cash reserve requirement for banks by one percent.

support to eligible firms to cope with the rising input costs (**Chapter 3**). Meanwhile, workers' remittances continued on their upward trajectory amidst the continuation of incentives for remittance processors to attract inflows via formal channels, and favorable wage and employment dynamics in the advanced economies.

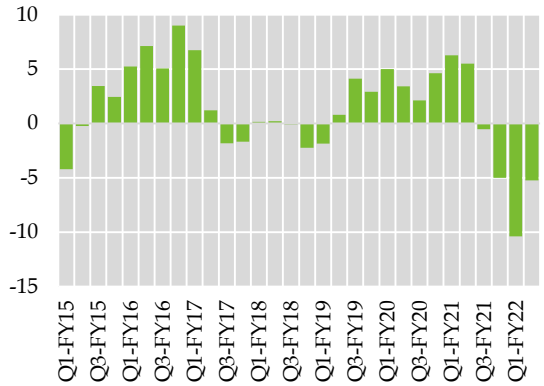
Box 5.1: Factors Driving Import Growth in Pakistan & their Impact on Interbank FX Availability

The recent growth in import payments is primarily responsible for the worsening in Pakistan's current account balance during H1-FY22. This box analyzes the major drivers of this import growth, and finds that global and domestic factors have both contributed to the increase. Specifically, there are three points worth noting.

(i) Terms of trade shock amidst the surge in global commodity prices: Pakistan is experiencing its worst terms of trade shock in over 7 years during FY22, owing to the sharp and broad-based rise in global commodity prices (**Figure 5.1.1a**). On the other hand, as per available data for import volumes of major products, import demand also played some, albeit relatively small role in pushing up imports of both energy and non-energy commodities during the H1-FY22 period (**Figure 5.1.1b**).[2] Energy prices had been rising consistently from the start of 2021, amidst rising demand as the global economic recovery picked up pace, and relatively tighter supplies as OPEC+ adhered to tepid planned supply increases, and the inability of US shale producers to achieve pre-Covid production levels due to financing and labor constraints. Reflecting these demand- and supply-side factors, average Arab Light crude prices were 69.2 percent YoY higher in H1-FY22. Similar supply constraints and strong world demand contributed to a surge in global LNG prices as well.

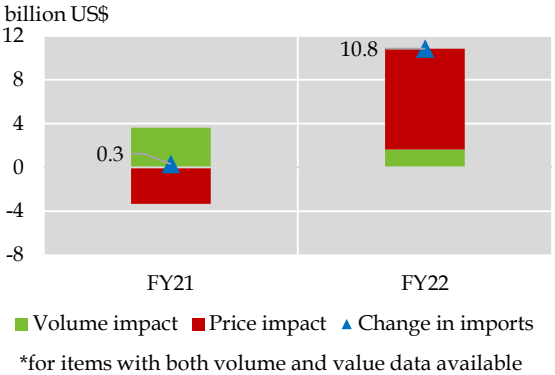
In Pakistan's case, the higher energy prices played a major role in pushing up energy imports during the review period (**Figure 5.1.2**). The impact of higher prices was starkly evident in case of crude oil, where, despite a 0.7 percent YoY drop in import volumes, import values grew 82.2 percent during H1-FY22. In case of POL products also, while demand for fuels for transportation (petrol and HSD) and power

Pakistan's Terms of Trade **Figure 5.1.1a**



Source: Pakistan Bureau of Statistics

Contribution of Volume & Price Effects to Change in Imports in Jul-Dec* **Figure 5.1.1b**



*for items with both volume and value data available

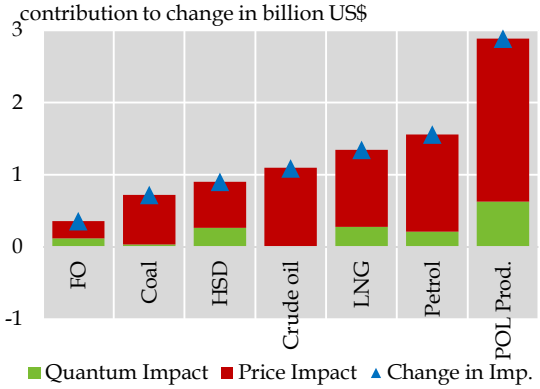
[2] In **Figure 5.1.1b**, the breakdown of volume and price impact is shown for only those items for which both import volume and value data is available. These items had a 59.3 percent share in overall imports during H1-FY22.

generation and industrial usage (LNG, coal and FO) was also higher, the rising prices of these commodities had a dominant impact in pushing up their import values.

For non-energy commodities also – especially food items, such as palm and soybean oil, pulses, tea and spices – the same dynamic was at play: primarily higher prices contributed to the uptick in import values of these commodities during the period, despite a drop in their import volumes.

(ii) Investment activity also pushed up import demand to some extent: The analysis of HS-8 level data for non-energy products indicates that industrial raw materials & intermediates, and capital goods were major contributors to the higher imports during H1-FY22 (**Table 5.1.1**). Demand for imported cotton was significantly elevated despite a pick-up in domestic production, reflecting strong demand for Pakistan's textile products in the major global markets (**Section 5.5**). Among other raw materials, the import demand for industrial and agricultural inputs and intermediates, such as fertilizer and plastic, also stayed elevated.

Breakdown of Energy Import Growth in Jul-Dec FY22 **Figure 5.1.2**



Source: Pakistan Bureau of Statistics

Analysis of Imports by Economic Category (HS-8 level)* **Table 5.1.1**

Category	Import Values (million US$)**		
	H1-FY21	H1-FY22	Change
Raw Material & Intermediates	7,844.4	11,364.9	3,520.6
Vaccines and pharma	130.1	2,704.6	2,574.6
Capital goods	4,701.1	6,641.1	1,940.0
Consumer goods	2,304.0	3,418.8	1,114.8
Food items	4,002.7	4,934.2	931.5
Non-Energy	**18,982.2**	**29,063.7**	**10,081.5**
Energy (oil, gas and coal)	**5,423.7**	**11,631.9**	**6,208.2**
Total	**24,405.9**	**40,695.6**	**16,289.6**

*As per categorization of imports jointly prepared by Ministry of Commerce & SBP
**Average M2M exchange rate for six-month period used to arrive at cumulative imports during the period.
Source: Pakistan Bureau of Statistics

At the same time, input demand of the domestic steel industry was also elevated, as firms geared up to meet the demand from the construction industry in the wake of policy focus on encouraging housing finance, including for affordable housing units. Output of the domestic steel industry – as captured in the LSM – grew by a sizable 18.4 percent on provisional basis during H1-FY22, against a drop of 12.1 percent in the same period last year. On the import side, based on HS-8 level data, the steel industry's demand for some scrap items, old ships for shipbreaking, and cold rolled coils were elevated.

The import demand for capital goods was also high. The textile industry's import of capital machinery remained strong, stimulated in part by the industry's access to concessionary financing under the SBP's Temporary Economic Refinance Facility (TERF) and the Long-Term Financing Facility (LTFF). Apart from textile machinery, imports of CKD mobile phones, power generation machinery and solar panels increased substantially during the period. The higher CKD cell phone imports mainly reflects the coming

online of several local manufacturing firms, with positive implications for domestic industrial activity, employment and skills transfer.

Imports of consumer goods were dominated by automobile-related imports, especially CKD car kits. The tax and duty relaxations under the FY22 budget to encourage automobile sales, coupled with product launches by new car entrants under the Automobile Policy 2016-2020 – aimed at product diversification and increasing competition – contributed to a sizable increase in imports of CKD kits, as well as auto parts, rubber tyres, and other related items. The higher imports also reflected in the uptick in domestic auto manufacturing, with the sector's production growing by a provisional 69.4 percent YoY in H1-FY22, against 3.4 percent growth recorded last year.

Lastly, imports of pharmaceutical products, including Covid-19 vaccines, rose quite substantially as compared to last year; in fact, they were the second-largest contributor to the rise in overall imports, after energy imports. However, as discussed below, the country also had access to external financing for these vaccine imports.

(iii) The full extent of higher imports is not falling on the interbank market: It is important to note that the payment pressures for some major imports are not entirely falling on the interbank FX market. In case of energy imports, the country arranged significantly higher external financing for oil and LNG imports from the Islamic Development Bank's (IDB) International Islamic Trade Finance Corporation (IFTC) and from commercial banks, according to the Economic Affairs Division (EAD).[3] So, while the purchase of these energy items is recorded in the imports data and contributed to the worsening in the current account balance, the external financing for some of these purchases was recorded in the financial account. As a result, the full extent of the higher energy imports did not fall on the interbank FX market.

The impact of Covid-19 vaccine imports is also not falling on the interbank market. These imports are being largely financed via external financing from multilateral agencies. The government informed the IMF during the 6th EFF review that US$ 2 billion from the additional SDR allocation of US$ 2.8 billion would be used to procure vaccines.[4] In addition, according to data from the EAD, the ADB has also disbursed almost US$ 0.5 billion to Pakistan during H1-FY22 to procure Covid-19 vaccines. Furthermore, the FX payments for vaccine imports by the government from its own sources are also not being made from the interbank market. As a result, even though these vaccine purchases are being reported in the import data and resulting in a higher current account deficit, their financing burden is not falling on the interbank FX market.[5]

In such a scenario where the FX earnings from exports and remittances could not fill the payments gap, the available external financing proved quite valuable in stabilizing the reserves position. Major financial flows from the additional SDR allocation and bilateral deposits from Saudi Arabia were supplemented by the continued financing from multilateral agencies and commercial lenders.

[3] Pakistan received US$ 800.7 million in short-term financing from the IDB/IFTC during H1-FY22 for energy imports, against US$ 245.7 million last year. Similarly, another US$ 487.3 million in energy import financing was arranged from a foreign commercial bank in H1-FY22, against US$ 220 million last year.
[4] Source: IMF Country Report 22/27, February 2022.
[5] However, FX payments for vaccine imports by the private sector would fall on the interbank market.

5.2 Current Account

The current account amounted to a deficit of US$ 9.0 billion during H1-FY22, against a surplus of US$ 1.2 billion in the same period last year. The main contributor to the CAD deterioration was the 86 percent increase in the merchandize trade deficit due to the sizable uptick in import payments. While export receipts also surged, mainly on the back of an uptick in textile exports, they could not completely offset the rise in import payments. The services deficit also grew over last year's levels, mainly in response to higher freight import payments and the resumption of international air travel. Workers' remittances also registered a sizable increase, with higher inflows recorded from most major corridors. The primary income deficit remained close to last year's levels, as a slight increase in interest payments on external debt was offset by a reduction in the profit and dividend repatriation by foreign firms operating in the country during the review period.

Workers' remittances

Remittances to multiple major recipient economies have generally decelerated so far in FY22, as indicated in **Figure 5.3**.[6] For some countries, it appears that the surge in remittances last year might have been driven by one-off factors, and inflows appear to have normalized this year.

Growth in Remittances to Major Recipients in Jul-Dec **Figure 5.3**

percent change YoY

*2021 growth for Jul-Sep (latest available data)
Source: Haver Analytics and State Bank of Pakistan

In Pakistan's case, inflows grew 11.4 percent YoY to US$ 15.8 billion. The advanced economies were among the major contributors to this increase, followed by the six Gulf Cooperation Council (GCC) countries (**Table 5.2**).

Remittances to Pakistan from the advanced economies, especially the US and the UK, continued their rising trend throughout the first two quarters of FY22 on YoY basis. While the fiscal stimulus in the advanced economies has generally tapered off, the economic recovery has picked up momentum, allowing for better employment and wage prospects for emigrants working and settled in these economies.[7] This, in turn, enhanced the ability of these emigrants to remit higher amounts to their relatives and friends back in Pakistan.

[6] The outsized growth in Nigeria can be partly attributed to the introduction of an incentive scheme in March 2021. Similar to the scheme introduced in Pakistan and Bangladesh in earlier stages of the Covid-19 pandemic, the scheme incentivized migrants to remit funds via formal channels. The growth in inflows to Mexico is largely explained by its large diaspora in the US, which benefited from the sizable fiscal support in the US and remitted higher funds back home.

[7] For instance, in the US, the unemployment rate fell from 5.9 percent to 3.9 percent during H1- 2021, whereas average hourly earnings of all employees grew by 4.8 percent YoY during the period. Source: US Bureau of Labor Statistics

Remittance Inflows to Pakistan from Major Corridors **Table 5.2**

million US Dollars

	Q1-FY21	Q1-FY22	Q2-FY21	Q2-FY22	H1-FY21	H1-FY22
US	632.7	762.5	548.6	731.2	1,181.3	1,493.7
UK	985.5	1137.3	890.8	1009.6	1,876.3	2,146.9
Germany	94.5	132.7	102.2	127.5	195.2	260.2
France	90.6	131.1	107.9	126.5	197.4	257.6
Italy	138.6	230.4	150.2	216.8	286.2	447.3
Australia	141.3	189.7	148.1	200.6	289.6	390.3
Canada	117.3	170.4	128.3	169.0	245.6	339.4
GCC	4,285.8	4,610.7	4,240.2	4,238.3	8,526.0	8,849.0
Saudi Arabia	*2,080.4*	*2,095.4*	*1,873.9*	*1,938.7*	*3,954.3*	*4,034.0*
UAE	*1,421.0*	*1,601.1*	*1,532.7*	*1,407.3*	*2,953.6*	*3,008.4*
Other GCC	*784.5*	*914.3*	*833.6*	*892.3*	*1,618.1*	*1,806.6*
Other countries	659.9	833.6	721.7	789.2	1,381.6	1,622.8
Total remittances	**7,146.2**	**8,198.6**	**7,038.0**	**7,608.6**	**14,184.2**	**15,807.2**

Source: State Bank of Pakistan

At the same time, some differences in remittance trends to Pakistan can be seen within Q1-FY22 and Q2-FY22. Specifically, remittances from the GCC countries slightly declined on YoY basis in Q2, with an 8.2 percent drop in inflows noted from the UAE (**Table 5.2**). The resumption in international air travel may have re-directed some inflows back to informal channels, partly in response to exchange rate margins charged by formal sector entities. Survey-based data collected by the World Bank shows a slight uptick in exchange rate margins charged by money transfer operators (MTOs) and exchange companies in the two major Middle East corridors (**Figure 5.4**). Furthermore, it is also likely that rising inflation in these host countries is straining the amounts remitted by emigrants, especially low-skilled ones.[8]

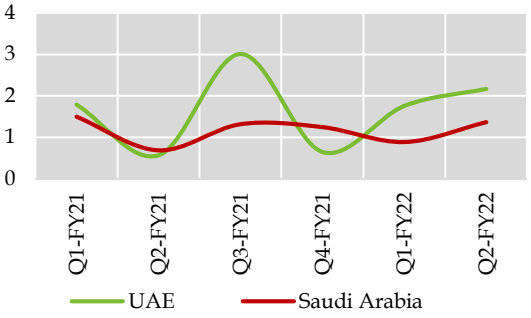
However, the government and the SBP have taken additional measures to sustain the inflow of remittances via formal channels. These include the launch of the Sohni Dharti Remittance Program (SDRP) in November 2021, and the continuation of fiscal incentives announced soon after the start of the pandemic.[9] Under the SDRP, remittances sent by emigrants via MTOs, banks and exchange companies are tracked via a mobile application, and the senders are immediately given reward points as per a pre-defined amount-based criteria. These reward points can be used to pay for a wide range of public services, including PIA air tickets, duties for bringing cell phones from abroad, and fees for the renewal of CNIC, NICOP and passport, among others. Along with these supportive measures, the number of Pakistanis going to the Middle East has also risen in Q2-FY22, which might have

[8] CPI inflation in the UAE reached 2.3 percent YoY in Q2-FY22, up from 0.6 percent in Q1. CPI inflation rose to 1.1 percent in Saudi Arabia in Q2, from 0.4 percent in Q1. Source: Haver Analytics

[9] A tiered incentive system was introduced in April 2020, which tied the reimbursement of marketing charges for banks, MTOs and exchange companies with the YoY growth in remittances processed by these entities. These incentives were renewed for FY22 via EPD Circular Letter No. 8 of 2021 in July 2021.

Exchange Rate Margin for Remitting to Pakistan from Major GCC Corridors* **Figure 5.4**

percent



*percent of transaction amount of US$ 200

Source: World Bank Remittance Prices

positive implications for the trajectory of remittance inflows from the region.[10]

Services Account

The services account deficit almost doubled from last year to US$ 1.8 billion during H1-FY22. Similar to the merchandize trade account, the rise in services imports was much sharper than the growth in services exports, which widened the payments gap.

Disaggregated data indicates that the doubling of net freight imports was the primary contributor to the higher overall services deficit (**Table 5.3**). Freight imports are linked with the magnitude of goods imports, and the sharp rise in goods import payments during the period also resulted in the sizable uptick in freight payments.[11] Apart from freight, the resumption in international air travel from Pakistan also contributed negatively to the services balance, as more Pakistani residents visited abroad on foreign airlines, especially for leisurely travel. Similarly, with the resumption of international flights, more Pakistani students could go abroad for studies, which in turn resulted in an increase in FX outflows for the payment of tuition fees and accommodation and living expenses.

Breakdown of Services Balance during H1-* **Table 5.3**

million US Dollars

	FY21	FY22	Change**
Transport	-955.0	-2,174.0	-1,219.0
Air passengers	*46.4*	*-137.8*	*-184.2*
Freight	*-911.9*	*-1,957.6*	*-1,045.7*
Travel	*-166.9*	*-312.0*	*-145.1*
Education exp.	*-60.5*	*-117.8*	*-57.2*
ICT Services	681.2	971.9	290.7
Exports	*959.1*	*1,301.9*	*342.8*
Imports	*277.9*	*330.0*	*52.1*
Financial Services	-41.0	-45.1	-4.0
Other Services	-462.4	-264.4	198.0
Services Balance (net)	**-944.1**	**-1,823.5**	**-879.4**

*Negative balance means deficit and a positive sign means surplus.
**Positive sign shows YoY improvement in services account & vice versa

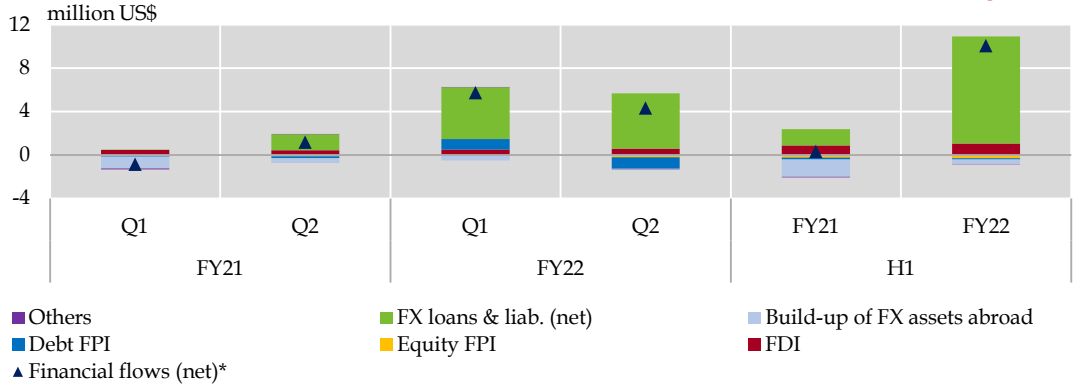
Source: State Bank of Pakistan

Nonetheless, on an encouraging note, the country's exports of information and

[10] The number of Pakistanis who went to the GCC countries for work rose to 156,307 in H1-FY22, from 44,034 in the same period last year. Moreover, monthly data shows that the number of workers who went to the GCC had risen to 63,253 in December 2021, which was the highest level since February 2020, before the outbreak of Covid-19. Source: Bureau of Emigration and Overseas Employment

[11] For BoP data, the SBP calculates freight payments by applying a uniform freight factor to the goods import payments made by banks. The factor is periodically derived from a survey of representative sample of importers. From July 2015 to June 2018, the freight factor was 3.5; it was reduced to 2.7 during July 2018 to June 2021, and then increased to 3.17 from July 2021 onwards. The higher the value of goods imports, the higher will be the freight import payments. Effective from Q1-FY22, the SBP began conducting this survey on a regular, quarterly basis.

Breakdown of Financial Flows Received by Pakistan **Figure 5.5**



*Financial account balance sign reversed from BPM6 convention. Positive value indicates net FX inflow & vice versa.
Source: State Bank of Pakistan

communications technology (ICT) continued their rising momentum, with net exports growing by 42.7 percent and reaching US$ 971.9 million during H1-FY22. Within ICT, exports of services related to call centers, software development and consultancy, and hardware development, all recorded notable increases. The continued rise in ICT exports indicate efforts by Pakistani tech firms, entrepreneurs and freelancers to capture the growth in global demand for digital solutions in the wake of the Covid-19 pandemic. Both the government and the SBP are actively supporting the ICT services industry, including via ease in FX regulations regarding capital mobility for IT firms, payments to major global vendors and suppliers, and issuing convertible debt instruments to attract foreign venture capital investors.

5.3 Financial Account

The net financial flows into Pakistan amounted to US$ 10.1 billion during H1-FY22, against an inflow of US$ 309 million in the same period last year (**Figure 5.5**).[12] The major inflows included US$ 3.0 billion in deposits from Saudi Arabia, and a US$ 2.8 billion in additional SDR allocation from the IMF. The country also retained access to financing from multilateral and commercial sources, and also to the international capital markets. Pakistan had raised US$ 1 billion from the tap issuance of a Eurobond in Q1 and repaid a maturing Sukuk of equal amount in Q2-FY22. Inflows into Naya Pakistan Certificates (NPCs) via the Roshan Digital Accounts (RDAs) also proved to be an important source of external financing for the government, with gross inflows of US$ 1.1 billion during H1-FY22. Moreover, net FDI increased by 20.2 percent YoY, indicating foreign investors' long-term interest in some sectors of the economy.

[12] After accounting for repayments of previous IMF loans (below the line repayments), the net financial flows dropped to US$ 9.5 billion in H1-FY22, against a net outflow of US$ 248 million last year.

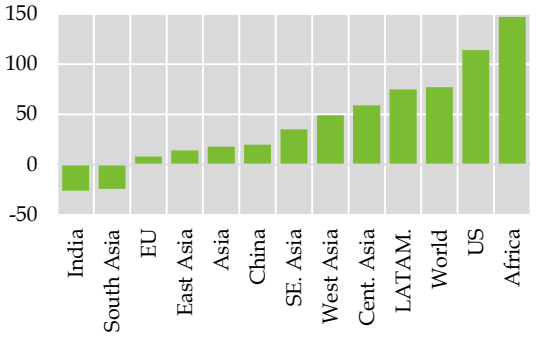
Foreign direct investment

Global FDI inflows rebounded strongly in 2021 and surpassed pre-Covid levels, with around 75 percent of the increase recorded in advanced economies. The sizable fiscal and monetary stimulus in these economies – including lower borrowing costs, along with attractive investment opportunities in infrastructure and digital services – resulted in a sizable uptick in FDI flows to these economies (**Figure 5.6**). On the other hand, FDI to EMs grew at a lower rate than to advanced economies, and there was also a wide dispersion within EMs. The sectoral analysis shows that FDI into IT services firms rose significantly, as investors tried to capture the growth in demand for digital services after the start of the pandemic.

To some extent, these global trends also reflected in FDI inflows to Pakistan during H1-FY22, which rose 20 percent to US$ 1.1 billion. FDI into the IT and telecom sectors accounted for most of this YoY increase (**Table 5.4**). Pakistan's ICT exports are rising, and start-ups in the sector are also attracting foreign investment. Most of the FDI into the sector came from the US, Netherlands and Singapore. The US invested in tech-oriented companies, including those providing cloud services; the Netherlands invested considerably in one of the leading mobile network service providers in the country; and Singapore directed funding into a tech-enabled logistics platform. Meanwhile, the telecom sector saw higher FDI inflows, largely due to the awarding of a 4G spectrum license to one of the largest telecom companies in the country. Furthermore, the financial services industry also recorded higher FDI inflows, with investments flowing into a few well-established conventional banks in technological and digital innovations as well as into microfinance institutions.

Growth in FDI to Major Global Economies in 2021 **Figure 5.6**

percent change YoY



Source: UNCTAD Investment Trends Monitor (Jan 2022)

The higher inflows into IT and telecom sectors helped offset a drop in FDI into the power sector, mainly due to a slowdown of investment from China. Most of the power

Sector-wise Net FDI inflow in H1 **Table 5.4**

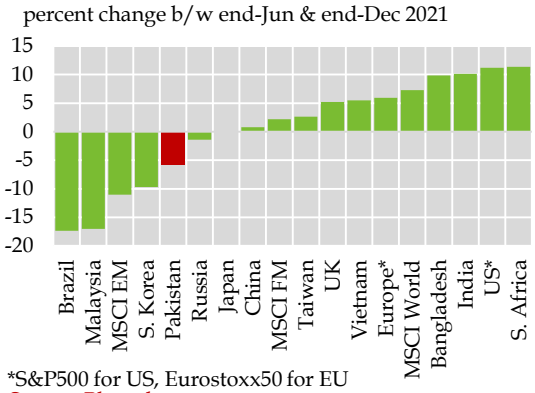
million US Dollars

	FY21	FY22	Change
Food*	5.7	2.1	-3.6
Chemicals	9.2	8.8	-0.4
Trade	42.9	35.5	-7.4
Oil & gas**	98.6	130.1	31.5
Electronics	-6.2	-18.2	-12.0
Electrical machinery	60.2	31.5	-28.7
Transport	-30.7	9.1	39.8
Power	497.1	363.7	-133.4
Coal	291.0	240.9	-50.1
Hydel	112.8	42.0	-70.8
ICT	-41.5	146.5	188.0
Telecom	-67.6	56.9	124.5
IT	26.1	89.7	63.6
Financial firms	127.4	205.7	78.3
Others	116.9	141.8	24.9
Total	**879.7**	**1,056.6**	**176.9**

*includes food packaging **exploration & refining

Source: State Bank of Pakistan

Equity Market Performance of Major Economies during Jul-Dec FY22 **Figure 5.7**



*S&P500 for US, Eurostoxx50 for EU
Source: Bloomberg

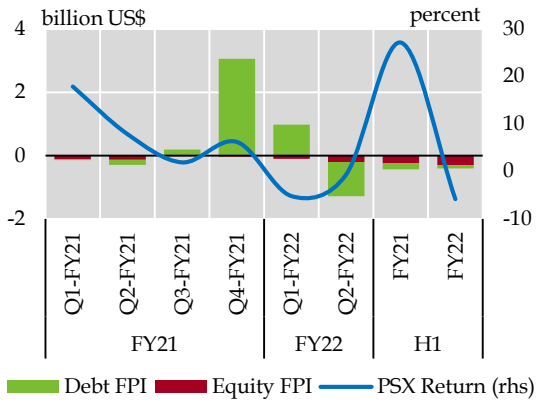
projects under CPEC are near completion or have already become operational, leading to a slowdown in FDI from the country into the power sector. Furthermore, there have been recent moves globally to phase out coal usage in power generation over environmental concerns.[13] Thus, investment from China in coal ventures abroad (including in Pakistan) is diminishing.

Foreign portfolio investment

Similar to global FDI flows to EMs, the trend in FPI flows to EMs has also reflected some divergence recently, with some economies receiving more inflows than others. However, one thing that appears to be consistent across most EMs is that their debt securities have attracted higher FPI than their equity securities during the course of 2021.[14] This can be explained by two main factors. First, EM central banks had begun to increase interest rates ahead of their advanced economy (AE) counterparts, thereby resulting in their debt securities offering investors higher yields. And second, equity markets across many advanced economies, especially the US, performed better than most EMs (**Figure 5.7**). As a result, for investors looking to increase their stakes in equities, AEs offered relatively better returns than many EMs. And within EMs also, countries whose stock markets performed better, offered more attractive investment opportunities to foreign investors than those whose equity markets relatively underperformed, such as Pakistan's.

These global trends were somewhat also evident in Pakistan's case. Net FPI into Pakistan recorded an outflow of US$ 406 million in H1-FY22, similar to the trend last year (**Figure 5.8**). With regards to debt securities, the country had raised US$ 1 billion from the tap issuance of a Eurobond in Q1-FY22, and repaid a maturing US$ 1 billion Sukuk in Q2-FY22.

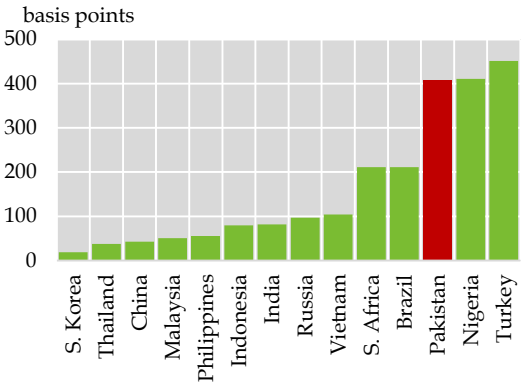
FPI into Pakistan and PSX Returns **Figure 5.8**



Sources: Haver Analytics & Bloomberg

[13] The Glasgow Climate Pact, United Nations Framework Convention on Climate Change, December 13, 2021.
[14] Source: IMF World Economic Outlook (January 2022).

Average CDS Rates for Major EMs during Jul-Dec FY22 **Figure 5.9**



Source: Bloomberg

Meanwhile, almost three-fourth of the overall net FPI outflow was recorded from equity securities. The underperformance of the domestic equity market, along with uncertainty regarding the resumption of the IMF program and rising external sector pressures, deterred foreign investment into Pakistani equities. Moreover, even though the risk premium attached to Pakistan – as captured by the credit default swap rates – declined slightly during H1-FY22, it was still elevated as compared to major EMs (**Figure 5.9**). Also, the MSCI downgrading of Pakistan from an emerging economy to a frontier market economy played a role in the equity outflows. Additionally, there was an ongoing underperformance of the domestic equity market. Data from the National Clearing Company of Pakistan Ltd. (NCCPL) indicates that foreign investors sold their equity holdings across multiple major sectors, including cement sector (US$ 275 million), followed closely by the fertilizer industry (US$ 273 million) and the food and personal care products segments (US$ 271 million).

Gross Loan Disbursements in H1 **Table 5.5**

million US Dollars

	FY21	FY22
Commercial loans	2,054	2,031.8
ADB	1,117.7	1,060.0
Eurobonds	-	1,000.0
World Bank*	738.7	932.2
IDB**	249.8	805.0
AIIB	250.0	36.6
Bilateral deposits	1,000	3,000
Others	277.4	408.3
Official External Loans	**5,687.6**	**9,273.9**

*IDA+IBRD **including short-term

Source: Economic Affairs Division

Net incurrence of liabilities

The net inflow of FX loans and liabilities in Pakistan rose to US$ 9.9 billion in H1-FY22, against an inflow of US$ 1.5 billion in the same period last year. Deposits from Saudi Arabia worth US$ 3 billion for BoP and budgetary support dominated the official inflows (**Table 5.5**). Furthermore, the additional SDR allocations from the IMF (of US$ 2.8 billion) also contributed to the higher external financing this year. The gross inflows into the NPCs – amounting to US$ 1.1 billion – also provided an important source of external financing for the government.

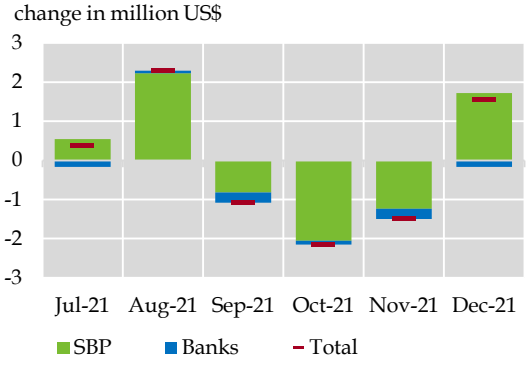
Meanwhile, within multilateral support, the ADB dominated, with almost US$ 1.1 billion in financing for Covid-19 vaccine procurement. Inflows from the IDB were mainly in the form of a short-term energy import financing following the global pandemic.

5.4 Exchange Rate and Reserves

The availability of external financing played an important role in sustaining the SBP's FX reserves position during H1-FY22. On the other hand, FX reserves held by commercial banks declined during the period, offsetting the slight rise in official reserves and resulting in a marginal drop of US$ 515 million in the overall FX reserves, which reached US$ 23.9 billion by end-December 2021.

The breakdown shows that the SBP's FX reserves had risen by a substantial US$ 2.0 billion in ssQ1-FY22, mainly in response to the receipt of Eurobond proceeds in July 2021 and the additional SDR allocation from the IMF in August 2021 (**Figure 5.10**). However, maintaining the reserves position proved challenging during Q2, amidst a significant widening in the current account deficit, along with the repayment of a prior Sukuk. Even though official borrowings were higher in Q2 on a net basis – including US$ 3 billion in deposits received from Saudi Arabia – the SBP's liquid FX reserves fell by US$ 1.6 billion in the quarter, reaching US$ 17.7 billion by end-December 2021.

Breakdown of Change in Pakistan's Liquid FX Reserves in H1-FY22 **Figure 5.10**



Source: State Bank of Pakistan

On the other hand, commercial banks' reserves declined by US$ 902 million during the period to US$ 6.2 billion by end-December 2021. The drop mainly originated from a significant uptick in trade financing extended by banks during the period.[15] Within trade financing, stronger demand was noted from importers. Importers tend to borrow in foreign exchange at lower interest rates, when they expect the exchange rate to remain relatively stable over the short-term.[16]

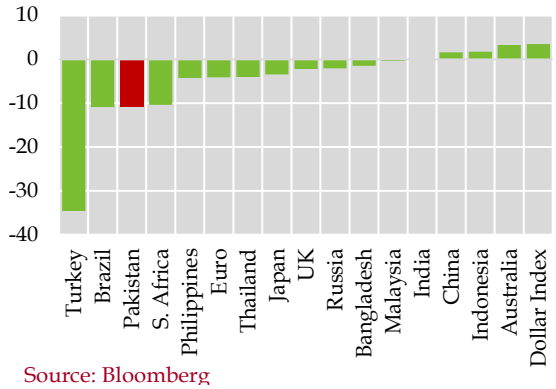
The external account pressures also manifested in the interbank exchange rate, where the PKR depreciated 10.7 percent against the US Dollar during H1-FY22. However, the US Dollar itself had appreciated against the currencies of many EMs and advanced economies (**Figure 5.11**). For many EMs, the exchange rate depreciations partially reflected the deterioration in their trade and current account balances amidst consistently rising global commodity prices. Moreover, with inflation consistently exceeding the US central bank's 2 percent target, the Federal Reserve, in November 2021, indicated an upcoming shift in its post-Covid monetary policy stance, when it decided to reduce the pace of its asset purchases. Then in

[15] Commercial banks' liquid FX reserves are calculated as their FE-25 deposit holdings, after excluding the trade financing extended by them. During H1-FY22, banks extended US$ 675 million in trade financing, against a retirement of US$ 94 million observed in the same period last year.

[16] This is because importers bear the exchange rate risk when they borrow in foreign currency. When they borrow in PKR, they bear no exchange rate risk, but have to pay higher local market interest rates.

Change in Major Currencies against US Dollar in H1-FY21 **Figure 5.11**

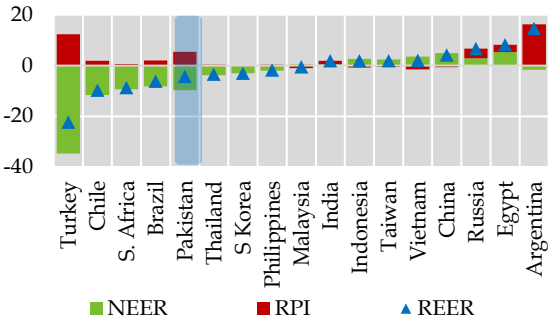
percent change b/w end-Jun & end-Dec 2021



Source: Bloomberg

Change in REERs of Major EMs during H1-FY21* **Figure 5.12**

percent change b/w end-Jun & end-Dec 2021



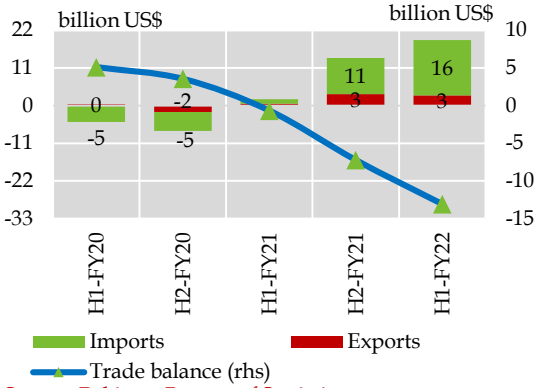
*JP Morgan Effective Exchange Rates (deflated by CPI)

Source: Haver Analytics

December 2021, the Fed further reduced the pace of these asset purchases, and signaled multiple interest rate hikes for 2022. These decisions contributed to a further strengthening of the US Dollar against other advanced and EM economy currencies.

Meanwhile, Real Effective Exchange Rates (REER) of EMs displayed a mixed trend during H1-FY22 (**Figure 5.12**). Price pressures, as captured by the Relative Price Index (RPI) generally contributed positively to the change in REER of many EMs, offsetting a general weakening in the nominal effective exchange rates (NEERs). In Pakistan's case, the rise in RPI could not offset the NEER depreciation, and resulted in a REER depreciation of 4.3 percent during H1-FY22.

Breakdown of Change in Trade Balance **Figure 5.13**



Source: Pakistan Bureau of Statistics

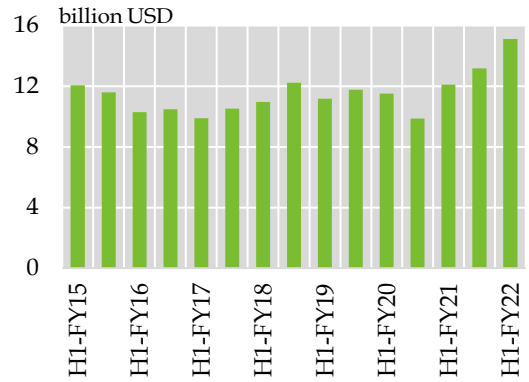
5.5 Trade Account[17]

The trade deficit rose to US$ 25.4 billion in H1-FY22, more than double the gap seen in the same period of last year. While exports rose by 24.9 percent YoY, the 66.6 percent increase in imports more than offset the gain from exports in this period (**Figure 5.13**). Moreover, the Q2-FY22 deficit was higher compared to the first quarter, as the imports pressure increased with the progression of the first half.

Importantly, Pakistan saw exports of US$ 15.1 billion in H1-FY22; with hefty

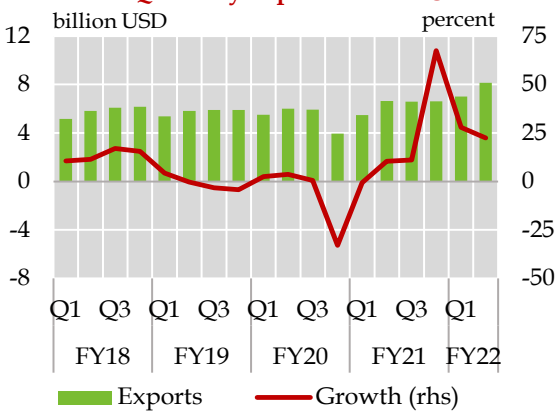
[17] This section is based on customs data reported by the PBS. The information in this section does not tally with the payments record data, which is reported in **Section 5.1**. To understand the difference between these two data series, see Annexure on data explanatory notes.

Pakistan's Half Yearly Exports **Figure 5.14a**



Source: PBS

Pakistan's Quarterly Exports **Figure 5.14b**



Source: PBS

contribution from textile shipments, mainly apparel, home textiles, cotton yarns and cotton cloths. Both positive price and quantum effects supported the growth in textile exports. Among non-textile exports, rice, petroleum crude, chemicals, fruits and vegetables, and sesame seeds were the major contributors.

While an increase in the global commodity prices supplemented some gain in exports, it affected Pakistan's imports more adversely, as energy prices specifically witnessed an unabated increase in this period. More than 22 percentage points of the total increase in imports were contributed by the energy products' imports, driven largely by the global energy prices. Moreover, a significant increase in imports of medicinal products, specifically vaccines, was a major source of an inflated Pakistan's import bill in H1-FY22. Besides, high palm oil prices increased the edible oil import bill. At the same time, ongoing economic activity raised the demand for machinery and transports.

Exports

As per Customs data, exports increased by 24.9 percent to US$ 15.1 billion in H1-FY22, highest in any half (**Figure 5.14a**). The growth is a significant acceleration from last year's 5.1 percent growth. In absolute terms, both quarters of the first half saw a spike of around one and a half billion dollars against corresponding periods last year (**Figure 5.14b**).

With respect to destinations, Pakistan's exports to traditional markets, mainly the EU-27, US, UK, and China, rose significantly during H1-FY22 (**Table 5.6**). Besides, Malaysia and Central Asian Republics (mainly Kazakhstan and Uzbekistan) received increased shipments, with the latter appearing as an emerging market for Pakistan's exports.

In terms of products, growth in exports was broad-based in both Q1-FY22 and Q2-FY22. Strong performance by the textile sector was reinforced by non-textile

Destination-wise Exports of Pakistan during H1 **Table 5.6**

million US Dollars

	FY17-FY20 avg.	FY21	FY22	YoY change in FY22
EU-27	2,971	3,453	4,082	629
Netherlands	*438*	*623*	*768*	*145*
Spain	*459*	*446*	*585*	*139*
Italy	*343*	*362*	*463*	*101*
Germany	*639*	*796*	*846*	*50*
US	1,851	2,417	3,303	886
China	859	1,090	1,658	568
UK	820	1,032	1,102	69
Africa	700	662	775	113
UAE	431	482	609	127
Bangladesh	349	312	469	157
Afghanistan	621	518	335	-184
Malaysia	81	90	229	139
S. Arabia	167	200	187	-13
CARs^	35	47	134	87
RoW*	2,009	1,808	2,244	436
World	10,894	12,110	15,125	3,015

^ Central Asian Republics; * Rest of the World

Source: PBS

exports, which is promising for attaining sustainable growth. To put things in perspective, in H1-FY22, contribution from the non-textile exports (8.9 percentage points) towards overall exports growth (24.9 percent) was the highest since H1-FY09.[18]

Within non-textile exports, the major contributing products were sesame seeds, maize (corn), rice, refined copper, ethyl alcohol, and petroleum crude. Whereas in the textile sector, major products were: textile materials, including cotton yarn, cotton cloth, and synthetic textiles; and value added textiles, including apparel (knitwear and readymade garments) and home textiles (bed wear and towels).

Performance of the textile sector of the country was enabled mainly by higher unit values realized as a result of higher cotton prices, strong demand, increased capacity utilization, and installation of new plant and machinery. Government's and SBP's policies have helped create a conducive environment for the textile industry to enhance its exports. Those policies included competitive energy prices, subsidized lending through refinance schemes—TERF in particular, tariff rationalization of key textile imports, and higher sales tax and customs duty refunds on YoY basis.

Textile exports cross US$ 9 billion mark for the first time—in any half fiscal year

Textile exports rose by 26 percent to US$ 9.4 billion in H1-FY22. This growth was mainly spurred by positive price effects across different products. Reinforcing the price impact, shipments of most of the products were also over and above same period last year (**Table 5.7**).

Apparel exports (knitwear and readymade garments) increased by 29.7 percent to US$ 4.3 billion in H1-FY22, from US$ 3.3 billion last year. In line with Q1-FY22, the impact of higher unit values far exceeded the impact of higher shipments in Q2-FY22. Besides apparel, there is home textiles (bed wear and towel) in the major value-added textiles, whose exports rose by 18.7 percent to US$ 2.2 billion in H1-FY22. Here, higher shipments mainly carried the year on year gains, particularly in Q1-FY22.

[18] This comparison includes only first halves of fiscal years.

Major Textile Sector Exports **Table 5.7**

million US Dollars

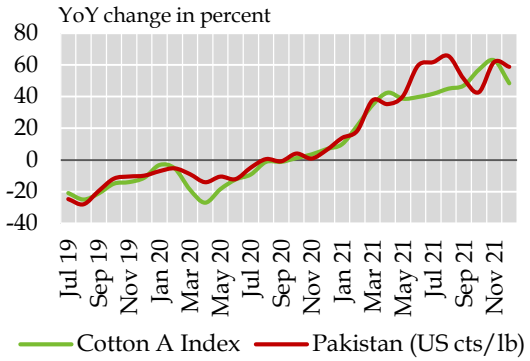
	H1-FY21	H1-FY22	Change	QE	PE
Apparel	3,340	4,332	992	55	937
Home textiles	1,840	2,184	344	321	23
Cotton fabrics	935	1,135	200	102	98
Cotton yarn	401	610	210	17	193
Textile made-ups (besides home textiles)	379	422	43		
Other textile material	304	385	81		
Art silk and synthetic textiles	168	225	57	-97	154
Tarpaulin & other canvas goods	62	57	-6	-7	1
Yarn other than cotton yarn	13	28	15	8	6
Total textile exports	**7,442**	**9,381**	**1,939**	**-**	**-**

Note: 1) Apparel = Hosiery (Knitwear) + Readymade Garments; Home Textiles = Bed wear + Towels
2) QE: Quantum Effect; PE: Price Effect

Source: PBS

Price effect: In H1-FY22, higher cotton prices had a significant impact on the export unit values of major textile products. Cotton prices, both in the domestic and international markets, had begun to inch up on YoY basis following the first wave of the pandemic (**Figure 5.15a**). Domestically, major factor was rising demand for local cotton supplies amidst strong demand by the exporting sector. In order to meet the domestic shortfall in supply, Pakistan has been importing cotton aplenty, so it is being affected by rising international prices (**Figure 5.15b**). The international price run-up could be explained by the post-pandemic international commodity price boom. Global cotton supplies were outstripped by recovering demand, originating mainly from China, Bangladesh, Vietnam and Pakistan, putting upward pressure on the cotton prices.[19, 20]

Movement in Prices of Raw Cotton in Domestic & Int'l Markets **Figure 5.15a**



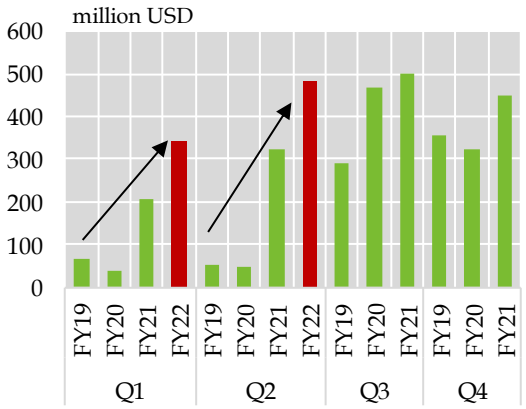
Source: Emerging Textiles

To put things in perspective, Pakistan's average monthly cotton fiber price in 2021 stood at 98 cents per pound, which was almost 1.5 times the 2020 average, and ranked highest in a decade. Same is true for the cotton A index, that evaluates the cotton prices in the international market.[21]

Quantum effect: For both apparel and home textiles, higher volumes could be explained by both demand-side and supply-side

[19] For details, see **Chapter 5-External Sector, SBP's State of the Economy Report for Q1-FY22**.
[20] It may be noted that world cotton production had declined by 7.6 percent YoY to 24.3 million MT in 2020/21. Source: Cotton: World Markets and Trade, February 2022, USDA
[21] Source: Emerging Textiles

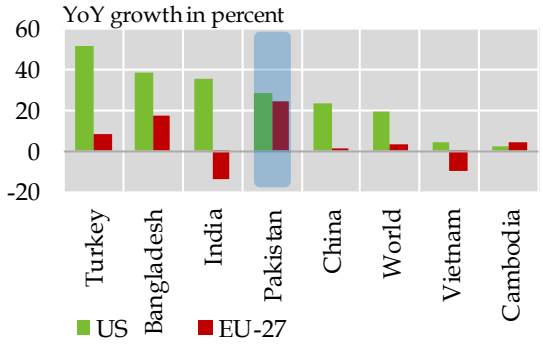
Raw Cotton Imports of Pakistan **Figure 5.15b**



Source: PBS

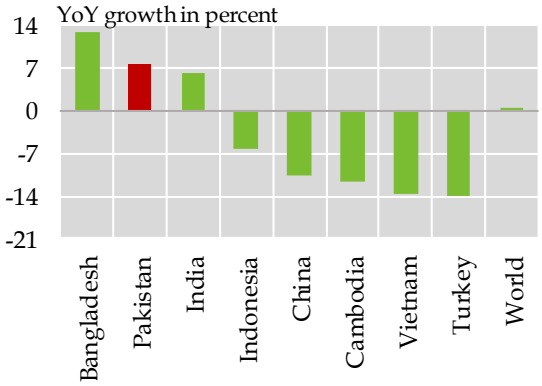
industry, which helped realize and sustain higher orders from the major buyers. This phenomenon partly reflected in much higher working capital offtake by the textile and apparel industry. In H1-FY22, the industry registered net borrowing of working capital loans (including the trading finance) to the tune of Rs 275 billion—18 times higher than the net borrowing during same period last year. Moreover, the industry also set on capacity expansion course, as evident in the rising textile machinery imports over the last few quarters.

Growth in Quantum Apparel Imports of the USA & EU-27 in H1-FY22 **Figure 5.16a**



Source: OTEXA & Eurostat

Growth in Quantum Apparel Imports of the UK in H1-FY22 **Figure 5.16b**



Source: UK Trade Info

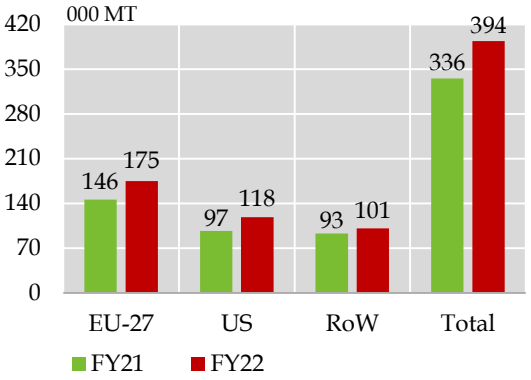
factors. On the demand side, there was strong demand from the major destinations—the US, EU-27, and UK (**Figures 5.16a, 5.16b and 5.17**). There was robust recovery in the EU-27 apparel imports from last year's dip. Pakistan seems to have sustained the influx momentum of rising orders from FY21.

On the supply side, there was higher utilization of existing capacity in the textile

Higher capacity utilization and expansion could be attributed to the government's and SBP's facilitative policies for the export sectors of the economy, with the textile sector being the major beneficiary. Those policies were as follows. First, the Temporary Economic Refinance Facility (TERF) and Long Term Refinance Facility (LTFF) prompted Rs 73.4 billion worth of textile machinery imports in H1-FY22, which were 94.9 percent higher year-on-year (**Figure 5.18**

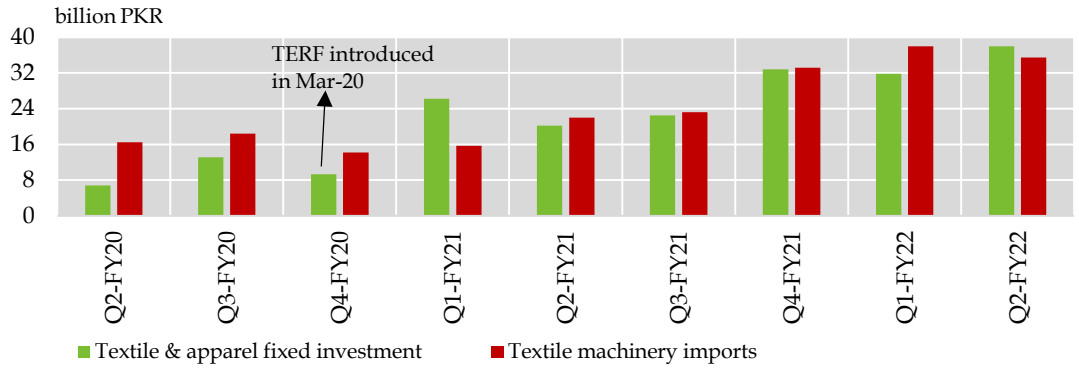
shows the quarterly breakup).[22] Second, regionally competitive energy policy – fixing gas supply to the exporting industries initially at US$ 6.5 per MMBtu and later at US$ 9 per MMBtu, and power at 9 cents per KWh[23] – facilitated the industry. Third, tariff rationalization of a number of textile imports, like artificial staple fibres, synthetic yarn, knitted fabric, and polyester yarn, facilitated the value-added manufacturing sector.[24] Fourth, industry's liquidity position had also improved during H1-FY22. On the aggregate, customs duty refunds were Rs 20 billion in H1-FY22, as against Rs 6 billion same period last year; similarly, sales tax refunds were up by Rs 25.4 billion to Rs 123.5 billion YoY in H1-FY22.[25]

Pakistan's Quantum Home Textiles Exports in H1 **Figure 5.17**



Source: PBS

Textile Machinery Imports Picking Up Strongly Since the Start of TERF **Figure 5.18**



Note: Fixed investment includes LTFF & TERF; values represent outstanding loans at the end of each quarter
Sources: SBP and PBS

[22] It may be noted that there is a lag impact of fixed investment on a firm's output. TERF had been introduced in March-2020; so investments made using TERF/LTFF ever since have had lagging impact in the ensuing months and quarters, including first two quarters of FY22.
[23] Gas tariff subsidy was revised in November-2021 from US$ 6.5 to US$ 9.0 per MMBtu for the province of Punjab; this revision was intended for the gas being used by the industry for power generation in its captive power plants. For general industrial use, the subsidy rate stayed unchanged at US$ 6.5 per MMBtu.
[24] There were some items, mainly raw cotton, whose tariffs had been already rationalized in FY21. This had been done to facilitate the import of key textiles for the value addition. www.commerce.gov.pk/decisions-of-tariff-policy-board-tbp-implemented-under-finance-act-2021-22/ accessed on January 15, 2022.
[25] Source: Federal Board of Revenue

Among other major textile products, cotton fabric exports rose by 21.4 percent to US$ 1.1 billion in H1-FY22. Volumes recovered from last year's fall. Similar was the case with cotton yarn, as its export value rose by 52.3 percent to US$ 610.4 million. As with other textile products, there was a positive and significant impact of higher cotton prices on the export values of both cotton yarn and fabric.

Non-textile exports post significant contributions to headline exports

Non-textile exports increased by 23.1 percent, or US$ 1.1 billion, to US$ 5.7 billion in H1-FY22, accelerating from last year's one percent growth rate. Noteworthy contributions were made by agro-food products, namely oilseeds (sesame seeds), rice, maize, fruits and vegetables (**Table 5.8**). Other products included refined copper, petroleum crude, and ethyl alcohol (undenatured).

Agro-food exports

Agro-food exports rose by US$ 450.7 million and clocked in at US$ 2.5 billion in H1-FY22; they had declined by 7.7 percent last year. Within the agro-food sector, oilseeds exports were recorded at US$ 155.6 million, as compared to US$ 36.6 million last year. Both the quantum effect and price effect were positive, with the former being more significant. Within oilseeds, sesame seeds made the major contributions. Higher volumes of sesame seeds could be traced to China, where exports rose by 71 million kg to 88 million kg in H1-FY22 on YoY basis (**Figure 5.19**). This, in turn, could be partly attributed to the Phase II of CPFTA, under which the tariff rate on sesame seeds was reduced to 0 percent from 9.0 percent.[26]

Major Non-textile Exports **Table 5.8**

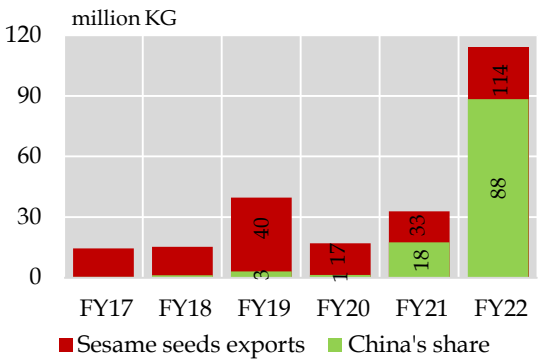
million US Dollars

	H1-FY21	H1-FY22	Change
Refined copper	190	345	155
Sesame seeds	35	157	122
Chemicals	248	354	106
Ethyl alcohol	*129*	*201*	*72*
Rice	963	1,067	103
Basmati rice	*228*	*304*	*76*
Non-basmati rice	*735*	*763*	*28*
Maize (corn)	9	89	80
Petro crude	44	107	63
Total	2,370	3,187	817
Non-textile, total	**4,668**	**5,744**	**1,076**

Source: PBS

Rice exports saw a jump of US$ 103.4 million to US$ 1.1 billion in the first half. Major contribution came from basmati rice, which recorded exports at US$ 304.1 million—US$ 75.7 million more than last year. Rice production was up 0.4 million tons in FY22.[27]

Pakistan's Sesame Seeds Exports and China's Share in Recent Years in H1 **Figure 5.19**



Source: PBS

[26] The CPFTA Phase 2 had come into force on January 1, 2020.
[27] Provisional figures provided by MNFSR

With unit values in check, export volumes rose 0.2 million tons in H1-FY22.

Basmati rice exports were led by higher volumes despite being pressed down by soft prices. These higher volumes could be traced to two Central Asian Republics—Kazakhstan and Uzbekistan, where Pakistani exporters are making inroads. Against a meagre US$ 3 million worth of basmati rice exports to these destinations in H1-FY21, there was US$ 57 million worth of exports in H1-FY22. Exports to Kenya and Somalia almost doubled to US$ 34 million in H1-FY22. Besides, there was decent growth in exports to the UAE as well.

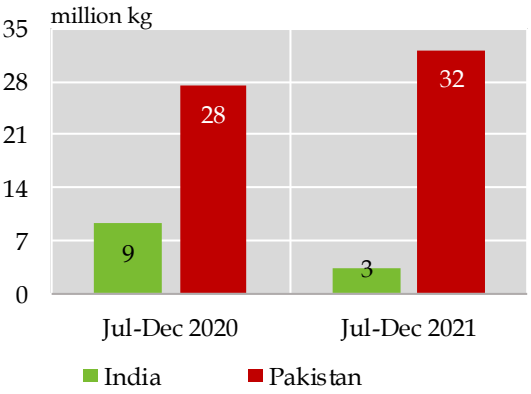
On the other hand, non-basmati rice exports rose 3.8 percent to US$ 762.7 million in the first half. With quantum effect supplanting the negative price effect, the major thrust in volumes came from Malaysia, Madagascar, Cote d'Ivoire, Philippines and Kazakhstan.

Apart from sesame seeds and rice, major contributing product to agro-food exports was maize (corn), as its exports jumped by US$ 9 million to US$ 89 million in H1-FY22. This massive jump came on the back of higher shipments to Malaysia, Vietnam, and Oman.

Copper exports boosted by price and rising share in China

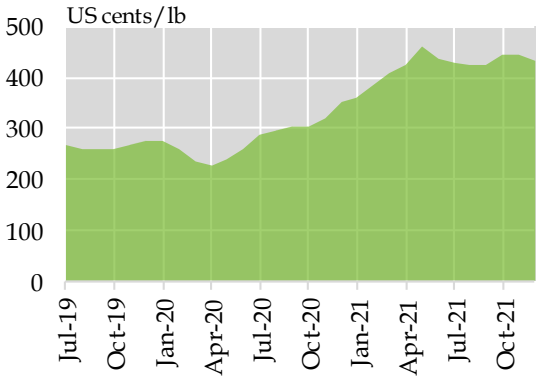
Refined copper exports rose by US$ 155 million to US$ 345 million in H1-FY22. Elevated copper prices in the international market significantly pushed up the metal's export values (**Figure 5.20a**). In terms of volumes, almost the entire increase came from China. Pakistan's share in China rose from 41 percent to 47 percent between the first halves of FY21 and FY22. China's imports from Pakistan have risen amidst a decline from India (**Figure 5.20b**). India's refined copper exports have been contracting due to lower production; on the other hand, Pakistan's refined copper has duty-free access to China under CPFTA-2.[28]

China's Imports of Refined Copper from Pakistan & India **Figure 5.20a**



Source: China Customs Statistics

Price of Copper in the International Market **Figure 5.20b**

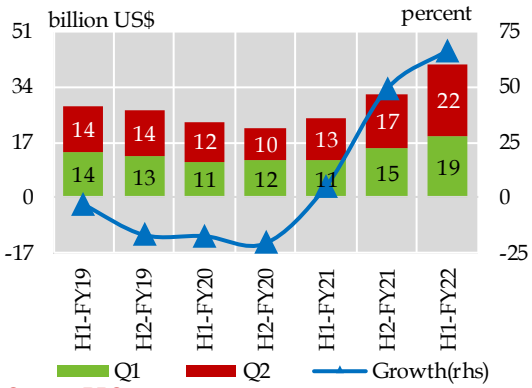


Source: Haver Analytics

[28] Source: https://www.commerce.gov.pk/protocol-on-phase-ii-china-pakistan-fta/ accessed on January 15, 2022.

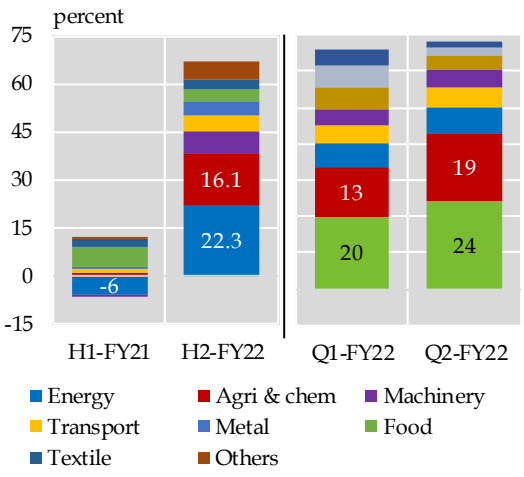
Besides agro-food products and copper, petroleum crude exports were up 144.4 percent to US$ 106.8 million, partly due to the low base effect. Soaring crude prices also complemented higher volumes. Lastly, exports of ethyl alcohol (undenatured) increased by US$ 72 million to US$ 201 million in H1-FY22.[29] All of this increase came on the back of higher shipments to China.

Quarterly and Half-yearly Trend in Imports **Figure 5.21**



Source: PBS

Key Sectors driving the Half-yearly and Quarterly Imports **Figure 5.22**



Source: PBS

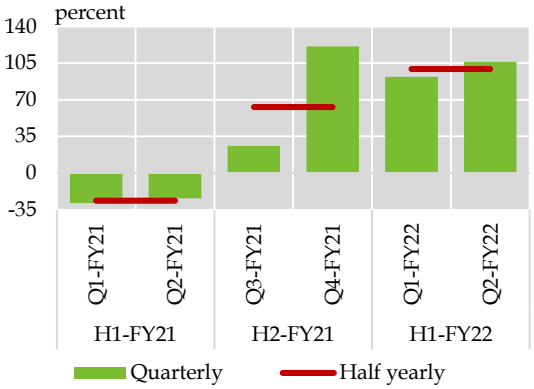
Imports

Pakistan's imports witnessed a sharp 67.0 percent increase YoY, reaching US$ 40.8 billion, in H1-FY22 (**Figure 5.21**). The growth momentum gained further traction as the H1 progressed, with Q2-FY22 ending with a higher quarterly rise compared to Q1-FY22.[30]

Key sectors that drove H1-FY22 imports were energy, agricultural and chemical, machinery and transport (**Figure 5.22**). Energy contributed 22.3 percentage points in the overall growth in H1-FY22, while this sector's share was negative in H1-FY21, primarily due to lower international crude oil prices prevalent at that time. Moreover, agricultural and chemical group, including Covid vaccines, added 16.1 percentage points in the growth of imports.[31]
Besides these two group's contributions in double digit, machinery and Transports contributed significantly in import growth while share of the Food and Textile receded compared to that witnessed in this period of last year (**Figure 5.22**).[32] Improved

[29] Undenatured ethyl alcohol is the pure form of the chemical.
[30] Imports increased by 65.8 percent in Q1 while the same rose by 68 percent YoY in Q2-FY22.
[31] Moreover, share of the energy, and agriculture and chemicals groups has strengthened further in Q2-FY22, to 24 and 19 percentage points, from 20 and 13 percentage points respectively in Q1-FY22, as the global energy prices remained at higher level and returning Covid, with new variants, lifted the demand for medicinal products.
[32] Machinery and Transports contributed 7 percentage points and 4.9 percentage points respectively. Moreover, Food sector's share reduced to 3.7 percentage points in H1-FY22 from 6 percentage points recorded during H1-FY21.

Figure 5.23 **Quarterly and Half-yearly Growth in Energy Price Index**



Source: World Bank

agricultural output has taken off some pressure of food imports.

Elevated global energy prices kept the energy imports at higher level

Global energy prices remained at a higher level in H1-FY22, experiencing a 99 percent increase YoY in H1-FY22 (**Figure 5.23**).[33] This sharp increase was contributed by not only the lower base effect when average prices were 26 percent lower than its preceding first half-year, but also due to the volatility arising from a host of demand and supply factors in oil and gas markets.[34]

On the demand side, the quicker than expected recovery in the global economic activity continued to fuel global oil demand. The adherence to the output quota by members of OPEC+, marginal increase in supply from US shale, and policy uncertainty related to transition to cleaner energy from fossil fuel, have created supply constraints in the oil market.

The situation was a bit different in the gas market. Besides economic recovery, prolong cold winter in the Northern Hemisphere, lower wind power generation in Europe, and drought like situation that curbed the hydropower output in Brazil and in some surrounding countries spurred the demand for natural gas. Covid related disruption, on the other hand, delayed maintenance work scheduled in 2020 for some gas fields till 2021. With gas demand recovering sharply, these planned and unplanned outages at some LNG liquefaction plants, unforeseen repair works, and project delays weighed heavily on the supply in the global gas market.[35]

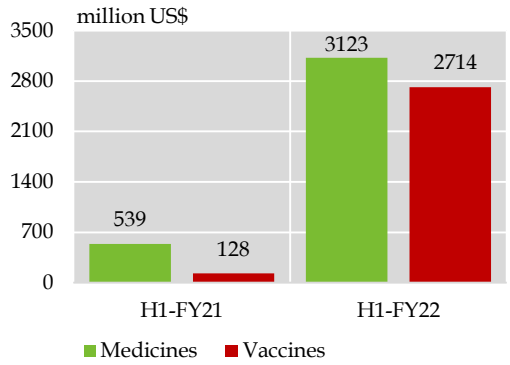
The situation in oil and natural gas market had spillover effect in coal market, as many countries switched to coal for electricity generation. As a result, price of coal also soared in this period.

Medicines, including vaccines to control Covid spread, supported the sharp increase in imports

Medicine imports increased by 479.4 percent to US$ 3.1 billion in H1-FY22, while its imports were limited to only US$ 0.5 billion in H1-FY21 (**Figure 5.24**).

[33] Source: World Bank
[34] International Energy Agency, available at, https://www.iea.org/commentaries/what-is-behind-soaring-energy-prices-and-what-happens-next, accessed on January 15, 2022.
[35] As per the estimate by IEA, the global LNG supply outages was 27 percent higher in the first nine months of 2021 compared to the 2015-2020 average for the same period. Most of these outages were unplanned, available at, https://www.iea.org/commentaries/what-is-behind-soaring-energy-prices-and-what-happens-next, accessed on January 15, 2022.

Half-yearly Import of Medicines and Vaccines **Figure 5.24**



Source: PBS

Development of vaccines to curtail the spread of Covid-19 were in early stages in the latter half of CY2020, and those rolled out were in short supplies during this period. Therefore, countries had to rely on administrative measures; employing stringent lockdown, and enforcing social distancing as a tools to curtail the spread of the virus. In 2021, however, a number of multinational companies and medical organizations came up with the vaccines that are effective in mitigating the impact of the Covid on human health.

As a result, vaccine imports witnessed a huge increase in H1-FY22 (**Figure 5.24**). More specifically, while the country imported US$ 128.1 million worth of vaccines for human use (apart from Hepatitis vaccine) in H1-FY21, the volume of the same imports rose to US$ 2.7 billion; more than 21 folds in H1-FY22. Especially, in the month of December 2021 alone, Pakistan imported around US$ 1.0 billion of medicine, specifically Covid vaccine, on account of booster jabs to curb the spread of new variant, Omicron, in the country.

Energy imports

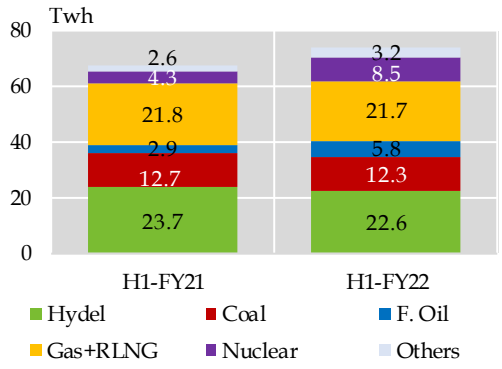
Energy imports rose to US$ 10.2 billion in H1-FY22, around 114 percent higher from US$ 4.8 billion in the same period of the last year. While higher international energy prices were a major driver (**Figure 5.23**), rising energy demand in wake of the recovering economic activity led to a broad-based increase in quantum imports, thereby almost doubling the energy import bill (**Table 5.9**).

Key Petroleum Product Imports during H1-FY22 **Table 5.9**

	H1-FY21		H1-FY22		Change	
	000 MT	million US$	000 MT	million US$	000 MT	million US$
Crude Oil	4,605	1,323	4,574	2,419	-32	1,096
Petroleum Products	7,135	2,169	9,201	5,078	2,066	2,909
Motor Spirit	4,249	1,265	4,967	2,853	718	1,588
HSD	1,803	539	2,692	1,456	889	918
Furnace oil	648	186	1,069	538	421	352
LNG	3,877	1,048	4,900	2,422	1,022	1,374
Others	537	231	479	306	-57	74
Total energy	**16,154**	**4,771**	**19,153**	**10,225**	**2,999**	**5,454**
Coal	9,251	618	9,746	1,347	495	729

Source: PBS

Share of Fuels in Power Generation during H1 **Figure 5.25**



Source: PBS

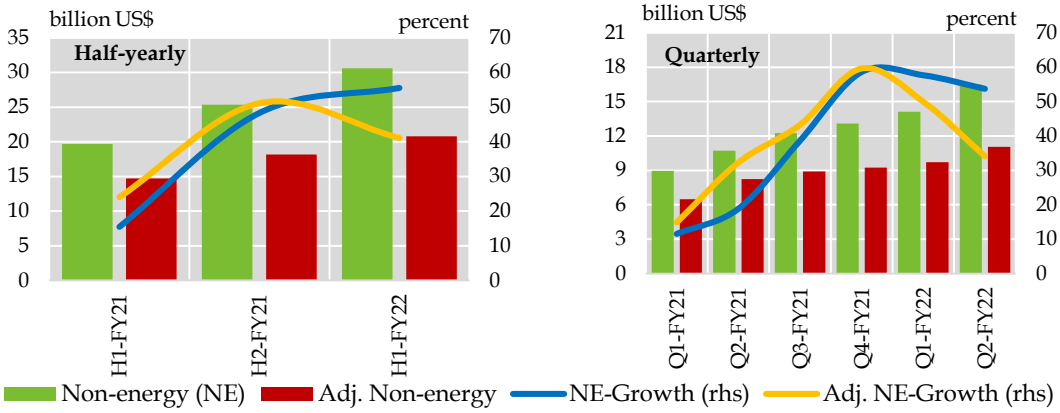
Specifically, the quantum imports of the petroleum products rose by 29 percent in H1-FY22 on the back of a sharp 49.3 percent and 65.0 percent YoY rise in HSD and furnace oil imports respectively during this period. While increased activities in commercial freight, agriculture, and construction sectors raised the demand for HSD, the demand for furnace oil was solely driven by the power generation (**Figure 5.25**).

Importantly, power generation during H1-FY22 has increased by 8.7 percent YoY to 74 Twh (Terra watt hour) from 68 Twh generated in this period of FY21, despite a 4.8 percent YoY decrease in Hydel generation during H1-FY22.[36] To mitigate the impact of higher international energy prices and lower hydropower generation, the generation mix received a tilt towards the nuclear energy, wind energy and furnace oil. Share of nuclear energy increased to 11 percent in power generation in H1-FY22 from 6 percent witnessed during the same period of last year. Similarly, share of furnace oil rose to 8 percent from 4 percent registered in this period.[37]

Non-energy imports

Non-energy imports increased to US$ 30.6 billion, rising by 55.1 percent YoY in H1-FY22 (**Figure 5.26a**). However, the quarter wise breakup suggests that YoY growth has decelerated in Q2-FY22. A number of policy measures were adopted in Q2-FY22 to arrest the slide in macroeconomic fundamentals

Non-Energy Imports **Figure 5.26a** **Figure 5.26b**



Source: PBS

[36] River inflows declined by 6.4 percent YoY during H1-FY22. Source: WAPDA

[37] Apart from importing, power sector has also used the stock of furnace oil held with the local refineries.

and to ease off the rising import pressure. These include, raising of the policy rates by 250 bps during Q2-FY22, jacking up the Cash Reserve Requirements (CRR) by 100 bps,[38] subjecting 114 more imported items to the cash margin requirement (CMR).[39]

These measures may have contributed to expediting the deceleration in non-energy imports in Q2-FY22, in particular, those less effected by the exogenous shocks like global commodity prices or Covid. Also, Machinery imports have received policy impetus under various schemes to promote exports. Therefore, adjusted non-energy imports (excluding palm oil, Covid vaccines, and machinery-*san* mobile phone) shows a significant deceleration in Q2-FY22 compared to overall non-energy imports (**Figure 5.26b**).

Agriculture and Chemical

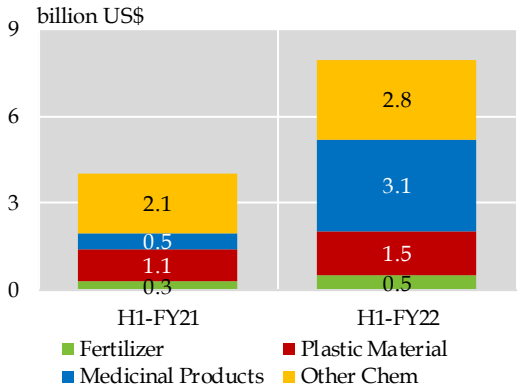
Imports under Agricultural and Chemical group rose by 97.3 percent YoY, to US$ 8.0 billion in H1-FY22 (**Figure 5.27**). Apart from medicinal product (specifically covid vaccines), import of plastic materials and a host of Chemicals remained high in the wake of the reviving economic activity. Most of these imported products under both heads are used in industries, while some plastic materials are also used by the households and some of these imported chemicals are used by the agricultural sector.

Fertilizer imports, on the other hand, increased by 60.8 percent YoY to US$ 523.4 million in H1-FY22, from US$ 325.5 million in H1-FY21. However, in term of quantum, fertilizer imports declined by 6.1 percent YoY, reaching 913.5 million tons in H1-FY22 from 973.1 million tons in H1-FY21. As discussed earlier, global gas prices have witnessed an unprecedented increase recently, and globally fertilizer sectors are also experiencing a spillover effect. By the end-December 2021, index of global fertilizer prices have rose by 73.7 percent since June 2021.[40] Moreover, DAP prices have increased by 23.2 percent which Pakistan imports mostly, while urea prices have increased by 126.3 percent in this period. This resulted in decline in the quantum of fertilizer imports in H1-FY22.

Machinery

After the agriculture and chemical group, machinery was the second largest contributor, with US$ 6.0 billion in Pakistan's non-energy imports. This volume of machinery imports is only bettered by 6.1 billion of these imports in H2-FY17 and H2-

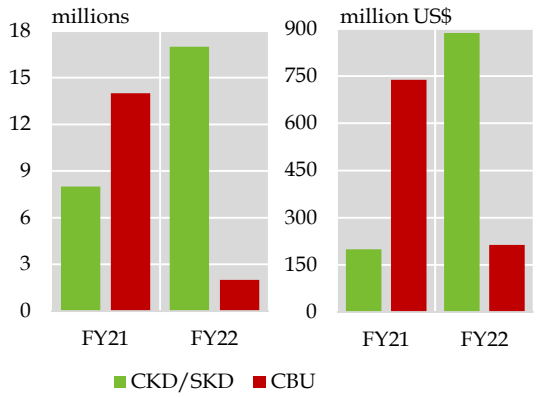
Agricultural and Chemical Imports Figure 5.27



Source: PBS

[38] DMMD Circular No. 20 of 2021, available at: https://www.sbp.org.pk/dmmd/2021/C20.htm
[39] BPRD Circular letter No. 30 of 2021, available at: https://www.sbp.org.pk/bprd/2021/CL30.htm
[40] Source: World Bank.

Mobile Imports during H1 **Figure 5.28**



Source: PBS

FY18, when a number of projects under CPEC were taking off. In H1-FY22, however, higher economic activity and push for exports led to a broad-based increase in the demand for machinery, imports of which rose by 40.2 percent YoY in this period.[41]

Within machinery group, cellular phone imports remain as a major head since H1-FY21, nonetheless, the dynamics of these imports have changed significantly compared to last year. In term of number of units, the cellular phone imports declined by 13.4 percent to 19.2 million units during H1-FY22. In terms of value, however, mobile phone imports rose by 16.8 percent YoY, to US$ 1.1 billion, in H1-FY22.[42] Semiconductor chip shortages propelled the prices of the mobiles sets globally, which resulted in the increased payments for the relatively lower number of mobile sets during H1-FY22.[43]

Importantly, imports of CBU mobile phones almost have been replaced by the CKD/SKD mobile phones (**Figure 5.28**). In H1-FY22, Pakistan imported 17 million CKD/SKD unit with US$ 887 million against 2 million CBU units with US$ 214 million. Comparatively, in H1-FY21, Pakistan had imported 14 million CBU units with US$ 738 million against 8 million CKD/SKD units with US$ 200 million. Incentives announced under the Mobile Device Manufacturing Policy (MDMP) 2020 for locally manufacturing cellular phone have encouraged a number of manufacturers to produce mobile phones locally, which resulted in the substitution of CBU cellular phone imports with the CKD/SKD imports.[44]

Apart from mobile phones, disbursement under LTFF and TERF led to increased imports of textile machinery, which witnessed an 89 percent YoY increase to US$ 436.4 million in H1-FY22.[45] Ongoing activity in CPEC and non-CPEC projects in tandem raised the demand for the power generating machinery, which increased by 21.1 percent to US$ 1.0 billion in H1-FY22.[46] Moreover, ongoing work on transmission and distribution networks led to higher imports of the electrical equipments like

[41] For details of the export promotion schemes, see SBP First Quarterly Report FY22 on State of Pakistan's Economy. Note that the widening in CAD during this time period is also due to imports of machinery which bodes well for investment and productive capacity of the economy.
[42] On the contrary, Pakistan imported mobiles worth US$ 938 million in H1-FY21.
[43] Average cost of per unit of mobile imports were US$ 38.5 in H1-FY21, while this amount rose to US$ 75.9, increasing by 97.4 percent YoY.
[44] For details on MDMP-2020, see **SBP Annual Report on State of Pakistan's Economy FY21**.
[45] Textile sector, including manufacturers of wearing apparel, availed PKR 339 billion of loan under LTFF and TERF during H1-FY22.
[46] For details of these power generating projects, see **SBP Annual Report on State of Pakistan's Economy FY21**.

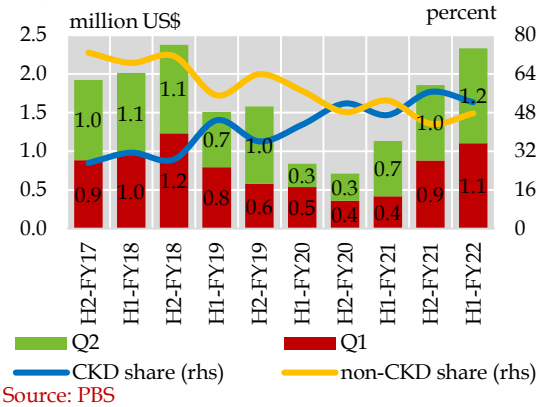
transformers, circuit breakers, cables and consoles.[47] Moreover, the increasing cost of power has led domestic consumers to switch to the solar energy, which increased the imports of Photovoltaic cells in the country.[48]

Transport

Transport imports increased by 105.8 percent to US$2.3 billion during H1-FY22; marginally lower from peak imports of US$ 2.4 billion seen H2-FY18 (**Figure 5.29**). At that time, record imports of ships and vessels for breaking, and aircrafts and its parts, besides CKD/SKD vehicles with 29 percent share in the overall imports, fueled the transport imports.[49] This time, the CKD/SKD transports with 52 percent share drove the increase in the overall transport imports. Incentives provided under Automotive Development Policy 2016-21 has brought new automobile manufacturers, and led to the introduction of new variant of vehicles, in Pakistan's automobile market. This resulted in the greater imports of the CKD/SKD vehicles in the country.

Nonetheless, the absolute volume of transport imports remains high primarily due to its demand; mostly for cars, SUVs and buses. Anecdotal evidence suggests that the burgeoning demand has widened the delivery lag for newly manufactured cars/SUVs from 2 months to 6-8 months. This has also raised the 'own money' exorbitantly high- the 'rent' a purchaser has to pay in order to eliminate the delivery lag of the purchase of the new vehicle. As the automobile manufacturers are fluxed with order and cash inflows (money paid by the purchasers in advance for the purchase of car/SUV), the number of policy measures adopted to curtail demand are yet to be reflected in the automobile sector.[50]

CKD/SKD Driving Transport Imports **Figure 5.29**



Source: PBS

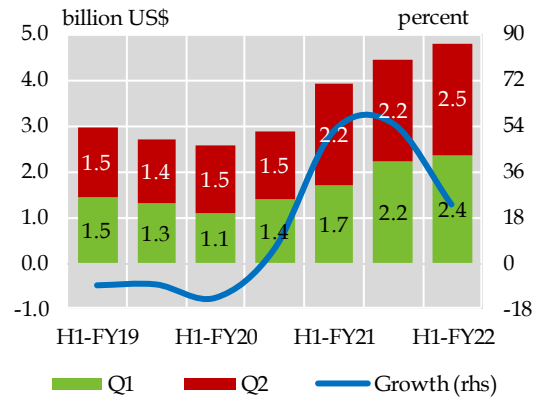
[47] As per NTDC, a number of transmission and distribution projects are undertaken to strengthen the power transmission and distribution network in the country. For details, visit https://ntdc.gov.pk/revised.

[48] Pakistan imported US$ 262.8 million of photosensitive semiconductor in H1-FY22, while this amount was only US$ 126.2 million in the same period of last year.

[49] For detail see **SBP Annual Report on State of Pakistan's Economy FY18**.

[50] Apart from the policy measures discussed above, SBP also attempted to restrict the demand for automobiles by amending the prudential regulation for consumer financing. The key measures include, restriction the amount of the amortized payments to the 40 percent of the monetized salary of the borrower, reducing the maximum tenure for the car financing from seven years to five years, and increasing the minimum down payment from 15 percent to 30 percent, and limiting the overall auto financing limits by one person from all banks/DFIs (in aggregate) to Rs. 3,000,000 at any point in time. Source: https://www.sbp.org.pk/bprd/2021/CL29.htm, accessed on January 15, 2022.

Trend in Food imports **Figure 5.30**



Source: PBS

Food

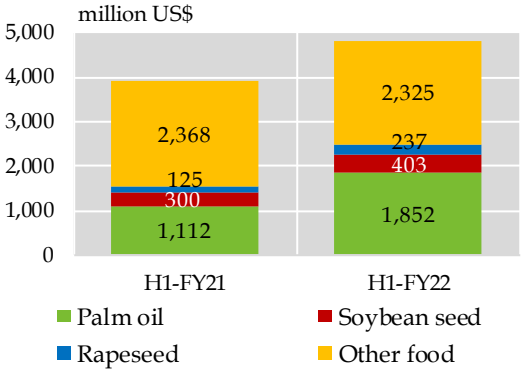
Food imports rose to US$ 4.8 billion, increasing by 23.4 percent YoY, in H1-FY22. In H1-FY21, food import bill was US$ 3.9 billion (**Figure 5.30**). Quarter wise breakup shows that these imports have decelerated sharply in Q2-FY22, growing by 11.9 percent YoY, compared to 38.1 percent growth witnessed in Q1-FY22.
Importantly, the import of edible oil (palm oil) and oil seeds (soybean and rapeseed) weighted heavily on the food imports due to increase in the global commodity prices.[51] Together, these contributed almost 52 percent in the total food imports in H1-FY22 (**Figure 5.31**).[52]

Specifically, Palm oil imports increase by 66.5 percent YoY, to US$ 1.9 billion, while imports of Soybean seed and Rapeseed, have increased by 34.5 percent and 89 percent YoY respectively in this period.[53]

Supply constraints in the key palm oil producing countries, Indonesia and Malaysia, and rising demand from India and China supported the record increase in the global palm oil prices.[54] Dry weather in Brazil, Argentina, and Paraguay, on the other hand, has depressed the soybean seed's output forecast from Latin America, resulting in a sharp increase in the global soybean seed prices.[55]

In Pakistan, soybean seeds is used as a key ingredient for making feed for poultry,

Contributions of Edible Oil & Oilseeds in Total Food Imports **Figure 5.31**



Source: PBS

livestock, and aquaculture (fisheries). Steep rise in global prices of the commodity depressed some local demand for this seed,

[51] Palm oil prices rose to a record US$ 1,344.8 per metric tons in January 2022, increasing by 104.9 percent from end-June 2020.
[52] Excluding these, Pakistan's food imports declined by 1.8 percent YoY in H1-FY22.
[53] Pakistan imported US$ 403 million of soybean seed and US$ 237 million of Rapeseed respectively in H1-FY22.
[54] For details, see **SBP Annual Report on State of Pakistan's Economy FY21**.
[55] Average first half soybean seed prices have increased by 28 percent YoY during H1-FY21. Source: World Bank

as poultry sector- a major consumer of the soybean based feed- is struggling due to higher input cost and sluggish transmission of these input costs to the poultry's consumer prices.[56]

On the other hand, wheat imports declined by 28.4 percent YoY, to US$ 473.6 million in H1-FY22. Though Pakistan expects decent wheat crop in FY22, the government's strategy to build strategic reserves though imports of wheat was setback a knock by the higher international wheat prices,[57] thereby resulting in the decline in the import of the commodity.[58]

Import of sugar, however, has increased by 49.5 percent YoY to US$ 189.3 million. Noticeably, bumper sugarcane crop led to 22 percent increase in the sugarcane output in the country in FY21. Moreover, sugarcane crop is expected to increase further by 8.2 percent in FY22.[59] Despite a significant improvement in the supply of sugarcane, the consumer price of sugar was rising in the domestic market due to bottlenecks in the sugar processing industry. To control this trend, government allowed the import of sugar in H1-FY22.

Similar to wheat and sugar, cotton output has increased by 32.7 percent YoY to 9.4 million bales against the target of 10.5 million bales. Despite the significant improvement in supply of cotton, rising exports by the textile sector led to increased demand of the commodity in the country. In H1-FY22, Pakistan imported US$ 824.8 million of cotton, 55 percent YoY more compared to this period of last year. In contrast, Pakistan imported US$ 532.1 million of cotton in H1-FY21.

Metals

Demand in auto sector and expansion of economic activity in housing sector increased the demand for iron and steel and its scraps. Import of iron and steel increased by 80 percent, to US$ 1.5 billion and that of iron and steel scraps increased by 30.4 percent YoY to US$ss 1.2 billion.

[56] Pakistan: Oilseed and Products Update, February 08, 2022, available at: https://www.fas.usda.gov/data/pakistan-oilseeds-and-products-update-9, accessed on February 15, 2022.
[57] International wheat prices have increased by 24.4 percent YoY in H1-FY22.
[58] For FY22, government has set the target of 28.9 million tons for wheat production and raised the minimum support price for wheat.
[59] Source: Ministry of National Food Security and Research (MNFSR).